Panel 7

Integrity, Ethics and Transparency: can these pillars of TRUST be secured by regulation?

Moderator:

Patrice Robineau, *Senior Advisor to the Executive Secretary, United Nations Economic Commission for Europe, Geneva*

Speakers:

Prof. William K. Black, *white-collar criminologist and former senior financial regulator, Associate Professor of Economics and Law, University of Missouri, Kansas City*

Eliot Spitzer, *New York State Attorney General (1998-2006) and former New York State Governor*

Jan L. Handzlik, *Specialized Lawyer on financial crime, Member of Greenberg Traurig, Santa Monica*

In his introduction the moderator **Patrice Robineau** reminded briefly that the UN was very open to the input of NGOs, including from the private sector and professional associations like CIFA (which has a special consultative status with the Economic and Social Council of the United Nations). With regards to the subject of the panel, he made three points: 1. In discussing integrity, ethics and transparency, nothing can replace individual behavior, and the importance of education and leadership is absolutely key. But since individuals do not always behave with integrity, ethics and transparency, regulation and enforcement institutions are needed. 2. So the question arises as to which regulation is most appropriate? In the EU, overregulation is more and more perceived as counterproductive and as giving a bad image of the bureaucracy. "Now the mantra is not deregulation or overregulation but better regulation", said the moderator. 3. Even with good regulation, in order for values such as integrity, ethics and transparency to be respected, there is a need for compliance programs, enforcement mechanisms and possible punishments. "It is key to have both regulation and some control of its effective implementation", concluded the moderator.

"Ethics is really essential", said Professor **William Black**, "it is what makes the world actually work when it actually works – which it doesn't always do". Punishment regimes are at best third best solutions, he said. They are expensive, both in terms of direct cost and opportunity costs of people being held in prison. They come after the facts, which means after the damage. And usually they can be applied only against fairly egregious activities, while there are many activities which aren't criminal or not effectively subject to prosecution but are really bad for the world. "Ethics can stop that kind of behavior where the criminal laws cannot", said the panelist. Further, there is a danger with punishment regimes to try to stop the most sever forms of criminality with approaches which can lead to people going to prison for some relatively minor things, or actions that arguably didn't

have the evil intent typically expected from the law. This can be further compounded by diverse forms of discrimination. "One key area of ethics is also professional restraint by prosecutors and regulators, not to go to the maximum of their power and not launch 'jihads' against people for personal reasons." Punishment regimes are also flawed with a "deterrence trap". Economist and Nobel Prize laureate Gary Becker formulated a "deterrence theory", a rational deterrence model, which states that the penalty should be in inverse correlation to the percentage of people who are actually caught. So in case of a very sophisticated fraud, explained Professor Black, if you are able to catch only one person in a hundred frauds, Becker's theory is to absolutely crush that one person in order to achieve rational deterrence. As a critic to this theory, the panelist argued that in order to have rational deterrence you need to know the actual incident, but in case of fraud based on deceit you don't know the actual incident, so you cannot have rational deterrence. What is more, you cannot realistically crush the people you catch in fraud. The problem, said M. Black, is that it destroys the firm, and destroying a large firm can mean destroying 30 000 jobs. "It's not going to happen, we can't go in front of a jury and blow up major firms every three weeks", he said. So there is a real deterrence trap when you are only able to find a relatively small percentage of the frauds. In fact, Becker's deterrence theory is based on the classical idea of the Homo Economicus, which views man as a rational and completely self-interested actor. The speaker pointed out that recent works, including the book "Moral markets" which is quite triumphal about the virtue of markets, view the Homo Economicus as a sociopath. Instead of deterrence, William Black said he would put forward the value of what in philosophy is referred to as virtue ethics. Studies found that people, far from meeting the homo economicus model, are actually prone to cooperation, value fairness, find reciprocity absolutely critical and hate fraud, said the panelist. "We seem to be frequently moral and altruistic creatures, and virtue tends to breed virtue, according to studies". Citing the classical economist Adam Smith, the speaker said that the author warned against monopolies in saying that "people of the same trade seldom meet together, even for merriment and diversion, but the conversation ends in a conspiracy against the public, or in some contrivance to raise prices". Corporations are a disastrous form of organization, officers will always be unfaithful and cheat the shareholders. So while Adam Smith's poor view of human morality doesn't seem to be supported by empirical studies, he was right about cartels, said the panelist. "And there is still a problem with officers and shareholders, but this problem was ignored by conservative economics praising the virtue of markets". In their book, Easterbrook and Fischel for instance write that rules against fraud are not an essential or important ingredient of securities markets, since markets automatically get rid of fraud, noted the speaker ironically. "This kind of classical view is based on a series of premises, which turned out to be wrong", said Professor Black. Easterbrook and Fischel said that honest firms have the unique ability to send signals of honesty, and investors have incentives to look for these signals. Here are the three signals they name: 1. Hire top-tier audit firms – because they will have such an interest in their reputation that they would never permit a fraud. But in fact it turns out, said the panelist, that because of the principal-agent problem, all the top frauds go to top-tier audit firms and get clean opinions, since reputation is valuable to the fraud. 2. If the CEO owns a material amount of stock in the company, he must be honest, because he "bounds his performance", he cannot profit unless the firm does. "This is nonsense", said the panelist, "it is through inflation of stock value, by inflating earnings, that you create massive flows to the CEO, who walks away from the radioactive crater, as the directors at Lehman did, as some of the richest people in the world." 3. Extremely high leverage is a unique signal of honesty, because if you had extreme leverage, you had only two choices: either be really good and highly profitable right away so you can meet the interests on the debt, or you will fail almost immediately, in which case you cannot cause much damage. "All three of these alleged signals of honesty of course are actually mimicked by dishonest firms, because all three of them aid fraud", said William Black. "The leverage is obvious at this point. The top-tier audit firm is your best ally. And the compensation system is the best

way to take money out without going to prison." It turns out that the firms that were supposed to be the best and most profitable, the most honest firms according to Fischel's theory, were the most fraudulent ones. It turns private market discipline into an oxymoron, concluded the panelist.

Can government resolve and restore trust when it comes to integrity, ethics and transparency, asked the next speaker, **Eliot Spitzer**. "I am not quite as optimistic as William Black", he said, "so my first answer will be 'no' regarding integrity, 'no' for ethics and 'maybe' for transparency." But not wanting to be quite as negative, he said he would actually upgrade his answer to 'maybe' for all three questions. "Maybe there is something government can actually do about this". M. Spitzer was astonished by the strong current push for government intervention and re-regulation, whereas until just two years ago the intellectual foundation to economic policy and theory in the US was that government had no role to play whatsoever. "We have moved across this spectrum with such speed that I don't think we have asked ourselves the hard questions about what works and what doesn't work", he said. He recalled the story he told in a previous session about the executives of Merrill Lynch who as a line of defense argued that they were not as bad as their competitors. "That to me was a crystallizing moment in terms of the first predicate for government intervention, because only government can enforce rules of integrity." This to him was the most important lesson to take home. Yet it doesn't mean that government alone can succeed. "All the rules in the world are for naught if individual behavior, which is really what guides and dominates our inter-personal relations, doesn't live up to those standards", he said. "A few prosecution here and there won't do it." This is where the problem really is: "when that tantalizing 10 million dollar bonus is hanging in the balance, too frequently the conduct of people involved does drop to the lowest common denominator, which calls out for government mandates and government thresholds, or at leas to define what proper behavior must be", explained Eliot Spitzer. Because the rational of companies will be to do what others in the market do. This line of thinking was pervasive in the recent Goldman Sachs hearings, as well as in other industries such as the pharma industry for instance, said the former Attorney General. So rule number one must be that the government has to set standards and define what integrity means. But the example of the Sarbanes-Oxley legislation in the US shows that setting strict rules is not enough. "Even with Sarbanes-Oxley things didn't change", noted the panelist. "Because the rules are not only easily circumvented, but many people will simply ignore them, and as prosecutors we must then try to catch the people who commit frauds and try to create a deterrence effect. But this hardly works either, because we are not really going to indict Merrill Lynch and destroy it." Citing the example of tough enforcement against Arthur Andersen, Eliot Spitzer said that in retrospect it was now seen as disproportionate and the deterrence effect didn't work either. So yes, governments must set standards, but enforcement of those standards will not have the proper effect through the market, he concluded. What governments must do, then, is articulate standards of fiduciary duty with much greater clarity than we have done. "Again the Goldman Sachs testimony was exhibit one in that category, when the witnesses could not say that they act in the best interest of their client. This shows the welter of conflicts of interests that pervades in the industry." So the real failure of governments over the last number of years, according to the speaker, has been to disaggregate the conflicts of interest that are so pervasive in the financial sphere. These conflicts need to be unraveled so that people in the market know what is going on, pleaded the panelist. Another key element in this discussion is executive compensation. "Anytime you did into executive compensation and take a look at who the compensation consultants are, you will find out very quickly that they too strong conflicts of interest. They believe their client is the CEO, not the shareholders! So of course they are going to push the compensations through the roof!" Here also the principal-agent dilemma applies, as these consultants have other businesses with the company that they try to keep. "Again this is a conflict of interest that hasn't been mediated and thought about properly", argued

the speaker. An analyst at Citibank captured this reality about the world of investment banking and finance in general: "what used to be viewed as a conflict of interest is now viewed as a synergy". For the companies involved in these conflicts, they are indeed synergies as they get to make money on both sides of the transaction! But it certainly isn't a synergy from the perspective of the client, which is theoretically the perspective we are supposed to be looking at, noted Eliot Spitzer.

So what do governments have to do? Set standards for behavior, redefine the market in terms of conflicts of interest, and most importantly it needs to restore what used to be called competition theory, or antitrust law. Why is that so important, asked the panelist? "Because at the end of the day, competition theory is what will rip apart the conflicts of interest", he said. Smaller, more atomized companies that actually compete with each other, rather than large investment firms or a limited number of pharmaceuticals or car manufacturers, then genuine competition will emerge. The panelist cited the successful anti-trust cases against Standard Oil in the 19th century, or against AT&T, which set off a wave of innovation in the telecom sector the likes of which had never been seen before. Eliot Spitzer gave three reasons why, despite the fact that he favors government articulation of rules, he only answers "maybe" to the fact that government can enforce integrity, ethics and transparency. 1. General deterrence doesn't reach far enough down into the mass of the economy to be that effective. 2. None of this works if you don't have the right people in government enforcing the law. "With all the discussion now about new rules of regulation being imposed, if I had to chose between writing new rules or choosing new people to enforce the existing rules, I would rather chose the people to enforce existing rules. There is more than enough latitude in the existing rules to do what needs to be done. What has been lacking is the will on the part of the regulators to actually do what needs to be done. But when we have a crisis, we like to pass a new law, because this creates a fiction. The fiction is that if we only had the law in place before, the crisis wouldn't have happened. Thus it exonerates the regulators who fail to do their job by the existing law and it provides a distraction so that instead of focusing to the businessmen who committed infractions we focus on writing the new law. This explains why we have so little prosecutions in the current crisis, and why we don't have more focus on why the regulators who already had the existing power to do what needed to be done didn't use that power to do much more. I don't think there is any question the New York FED had the power all throughout this crisis to restructure and de-leverage and require additional capital from banks and prevent much of what caused the crisis. I don't think there is any question the OCC and the SEC could have done what needed to be done. The point is, these agencies failed, and this is the history of the regulatory process. This is why I have a big question mark as to the ability of the government alone to restore our economic well being in terms of more transparence, ethics and integrity."

As a final note, the speaker mentioned another argument in favor of government intervention which has been ignored until recently, the issue of externalities. Just like externalities in the field of the environment constitute market failures requiring government intervention, debt has become some sort of externality in terms of systemic risk. "Debt has become so pervasive in our economy, be it sovereign debt or the debt of Lehman Brothers, Citibank and the likes. Debt has gotten so enormous that as an entire aggregate effect our economy could not digest it. It works as an externality because each little piece of debt in each transaction from each private company or sovereign nation looked at individually isn't so terrible, each can be rationalized in isolation, even a subprime loan. Yet debt is to systemic risk what CO_2 is to global warming. Each individual contributor doesn't see, and cannot appreciate, the larger consequences of his or her actions. And therefore we need a systemic risk regulator, just like for externalities. This is an argument we haven't been using so much, and we need to explain what government does and why it does it, so we don't go from crisis to crisis. What we need is a greater coherence and logic, an intellectual foundation to what we are doing and why we are

doing it."

Jan Handzlik offered a different perspective on the debate of the panel: "We have had an academic and a former prosecutor, I am a defense counselor, representing companies and individuals who are accused by prosecutors such as M. Spitzer and analyzed by academics such as M. Black". He started by noting that the law already imposes very substantial duties on companies and individuals: duty of care, duty to act responsibly, duty to look out for the interest of all the affected parties. "The question, really, is how can you mandate ethics? How can you compel people to act with integrity? And can you do that through government regulation?". To him the answer to that last point is no. How then to have an impact on the key individuals, the regulators, people who run the corporations and work at them? "It is absolutely clear that good people are needed in all of these positions, because without good, moral people of good character in those positions the game is lost to begin with", said M. Handzlik. In this respect, he asked who actually do corporate officer and directors of major corporations represent? The traditional view, he answered, and the one we are familiar with, is that they represent the shareholders, and their duty of loyalty and fidelity is to the shareholders. They are responsible for maintaining and increasing the value of the company in a responsible and ethical way for the public good. "Yet what we have seen in the recent past, going back to the 80's and 90's, with Enron and now the subprime crisis, is that the view on the part of the officers and directors is that they are acting for themselves. Their interest they try to promote is a self-interest, and for this reason a lot of manipulation took place to achieve short term gains, pump up the stock, inflate the balance sheet artificially, sell bundles of bad loans as quickly as you could, in a process that gets self-perpetuating", said the panelist. In fact, he ironized, they are acting for the benefit of the shareholders, the major shareholders that is, themselves, when they are artificially pumping up the value of the company. And what is the view now in terms of the interests and the focus of corporate officers and directors? "The view in government and many regulators is that the executives and directors of a company should actually be looking out for the interests of the investing public", explained the speaker. "No longer are they simply representing the existing shareholders of the company, who of course are members of the investing public, no longer should the be looking out for themselves, but they should really be protecting the investing public in general." Similarly, the traditional role of a lawyer or counsel is to represent his or her client to advance its interests and prevent damages, continued M. Handzlik. But under much of the new regulation and enforcement through litigations, the general counsel of the company really has many masters and must act in an independent and conflict free fashion. And he or she has to be willing to tell the directors and executives of a company when they are crossing the line, are not adopting the appropriate conduct or not disclosing certain information to the public. "They have to deliver a message that management doesn't want to hear in many cases", commented the panelist. This new view of the responsibilities of corporate officers and lawyers is being enforced through recent prosecutions of the Department of Justice in the US, said M. Handzlik. Referring to the title of this panel discussion, he added that using regulation, enforcement action and prosecution to compel ethical behavior was not a good practice and not a good way to advance public policy. "You can't enforce ethics, you can't compel integrity through regulations. Certainly a prosecution or enforcement action can instill fear, it can cause individuals to change their behavior and might create deterrence on others for a short period of time. But in my view you cannot enforce ethics on a long term basis by using the heavy hand of regulation." The reason, he suggested, is the human factor. Individual character, which is formed early in human beings, is a key factor. "Training, education and regular updates are necessary so that people are conversant with the law, understand their duties under the law and as a corollary, understand what is right way or the wrong way to act." How do you then motivate the individuals to do the right thing and act with integrity and ethics, asked the panelist? "I think the simple answer is to demonstrate to them and convince them that by acting in an ethical manner they are

acting in their own self interest", he answered. With a determined management setting realistic standards of behavior and conduct to its employees and putting in place a good compliance program. The speaker raised one important issue however: the playing field has to be level for all actors. "If a company is acting in a moral fashion and doing things right but its competitors are not, then it is not going to be very long before that company lowers its standards to catch up as a matter of survival." So insuring a level playing field between and amongst companies, which, assuming the good nature of human beings, enhances the ability of company executives to act in a responsible manner is a vital role of regulation, suggested M. Handzlik. Standards should be set through regulation and those standards should be enacted and enforced in-house by companies. If companies stray and violate the standards, then there is a role for enforcement, said the speaker. The individuals should be punished or even discharged, whatever their position in the company. Then finally there is a role for prosecution, added the speaker. "But criminal prosecution has to be employed in a very selective fashion, and not to punish the lower level folks who didn't have any real stake in the fraud other than keeping their job and keeping their boss happy, and who in fact would be the best witnesses for the government and the prosecution. But rather punish the decision makers through criminal prosecution, the people who have acted in willfully fashion, deliberately designed to really benefit themselves rather than the shareholders or the company or the public." Prosecution has to be used sparingly, insisted the panelist, because it is not an effective way to make public policy, to communicate what the standards and limits are and what will happen if you step over the line. So the role of regulation, according to M. Handzlik, is to ensure there are standards and also to ensure that there is a level playing field so that one company does not gain a competitive advantage over another company by using improper behavior and unethical tactics. But the speaker noted a troubling development in this respect recently. "In the Savings & Loan crisis of the 80s and 90s, there has been many prosecutions resulting in bankers going to jail and institutions being shut down. Yet over the past one and a half year with this crisis, something very peculiar has happened and continues to happen: the very individuals who were the most responsible for the problems that the world is facing have landed just fine. And they may be still in place at their companies, and with the notable exception of Lehman Brothers and a few others, the companies are still there. Nothing much has changed, and now the same companies and their lobbyists and lawyers are arguing against regulation of the financial system! This gives a perception that the system is not fair, that it favors the wealthy, moneyed interests, people who make political contributions and have access to policy makers and legislators or regulators, giving them an advantage over ordinary citizens or the small businesses. But if in fact the playing field is level and there are clearly defined standards, then you will see the companies acting not just for the benefits of the shareholders but also for the benefit of the company, themselves and the members of the investing public."

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QUESTIONS & ANSWERS

Question
What could in your opinion be the role of the press in this crisis, are they are still as embedded as they were during the Iraqi war with regards to the financial world? Can the press help the shareholders to be more active instead of leaving this to the regulators? What could be the role of the press, especially in the US, to help people to think a bit more about what is happening?

Eliot Spitzer
I think the press has played a critical role in revealing many of the malfunctions and much of the most egregious wrongdoing. The press, needless to say, has a spectrum of political, economical and ideological views, some have been historically utterly opposed to any intervention prosecutions or enquiry, others who are very good at digging, picking and pushing. And yet the role of the press, the "fourth estate" as it is sometimes called, has been essential in shedding light on where government and private sector actors have strayed.

Question
I would like to come back to the question of coherence, you said regulation can work only if its coherent. How do you think we could have a coherent regulation in the world? Because it is often a question which comes out when governments talk together about regulation. They argue that they can't implement measures, otherwise if they are the only one everybody is going escape from our country and go to another one where laws are maybe not as tough as ours. How do you think about this problem and what do you think should be done to get to a point where regulation is more global and harmonized?

Patrice Robineau
It is a very important question because if we speak about these structural reforms which are discussed now, such as to separate the trading activities from the traditional activities, limiting the size of banks, controlling of the rating agencies, the capital ratios, etc, if this is not universal, it is really difficult to envisage a viable and efficient structural reform in order to face the systemic risks.

William Black
In the US context, if we had not gotten rid of the rules requiring underwriting of loans, which said you had to verify that the borrowers have the income to be able to repay the loan, then we would have saved a trillion and a half dollars. There were other crisis, Iceland would have still blown up, but that rule would not have hurt anyone. That is a perfectly prudent rule, it doesn't require a high level, its actually the minimum prudent level. Those are the kinds of rules that I think need to be in place, that would have worked very well. Similarly, I think we should emphasis the value of simplicity. I am supposedly relatively sophisticated in finance, but I would never buy anything other than plain vanilla. I think it is nuts to be buying more then plain vanilla. I wouldn't recommend to any of my relatives, no matter what their wealth position, to buy anything else than plain vanilla.

Eliot Spitzer
I think your question relates to regulatory arbitrage, which is the very real capacity of businesses to find a home that will give them a more favorable regulatory framework within which to operate. And we have seen this in the banking community, banks will go between state charters and national charters and take advantage of that. The best example of that recently is the lawyers in the Lehman context, where Lehman found a law firm in Britain that would give it the opinion it wanted on the Repo 105. They tried a couple of times I believe with domestic law firms, and they were a little uneasy. And so they bounced around to find a regulatory environment that was favorable. The only answer to that, at the end of the day, because arbitrage will drive regulatory thresholds down to a lowest common denominator, the only answer is for the regulators to get together and decide to act coherently and in a multilateral way, whether it is federal states in the US domestic context, or what we are now seeing, where at the international level the major financial centers are all saying we need to act in unison on these critical issues, and do it in a way that is simple and everybody will agree on those core principles that are necessary.

Jan Handzlik
That's the level playing field on an international basis that I was referring to, and I agree. I think the answer has already been given, but organizations such as CIFA have a role to play, which is to articulate the principles that should be applied globally and to communicate those principles to others. But truly harmonizing the regulatory regimes in leading countries would be a beneficial thing.

William Black
Yet in this context international arbitrage couldn't have caused a problem. The FED had authority to set minimum standards for all home landing in the US. Yet they refused to use that authority because they hated the idea of regulation.

Question
Something I haven't heard discussed much at all, even though it is part of some of the bills going through Congress. With regard to integrity, ethics and transparency, would anyone on the panel care to comment about regulation and particularly resolution of customer disputes through the process of compulsory pre-dispute arbitration?

Eliot Spitzer
It is a huge issue. You are right, the arbitration process hasn't been part of the conversation here today. Theoretically it is good to have a dispute resolution system that is a bit more efficient than the traditional litigation process back in the US, which tends to defeat claims that are too small to satisfy just the cost structure of litigation. Having said that, the way arbitration panels are structured has been grotesquely unfair to claimants. And I think this is something that warrants an enormous enquiry.

William Black
In fact there is a recent scandal, that broke out six months ago, where it turned out that one of the major arbitration entities was advertising to businesses 'we will be a friendly forum for you'. And they were forced out of much of the retail arbitration business.

Eliot Spitzer
Which of course is not too dissimilar to Harvey Pitt when he became chairman of the SEC between 2001 and 2003, saying the SEC would be a kinder, gentler SEC. This exists in many different contexts!

Question
I am not from this industry and I have been absolutely horrified at the deliquescence of integrity and ethics on what I have heard in the past three days. And I agree with M. Handzlik when he says it basically goes back to the individual. I'll go back to M. Demandolx's presentation when he talked about his father and grandfather's ethics and his own ethics I believe, which is all a matter of education, starting from the family. Now the family has renounced a certain number of its duties. However, I think integrity and ethics starts with individual and there is no amount of regulation which can change that. So, first education, and also repetition. I worked with a company in the past, DuPont de Nemours, who had a policy of safety and security. And based on that policy of security, they had a very low level of insurance of its own factories. Because every individual working in DuPont was submitted week after week to the repetition of what he had to do to be secure in the company, how to move in public, how to move in the house, how to move everywhere. His life was based on security. It was repeated everyday. If an individual got out of that security policy, if we had three accidents – and by accidents I mean the slightest accident, if you cut yourself you had to report it – three accidents and you were

out of the company. It was as simple as that. And I can assure you that 35 years after leaving DuPont, it is still engrained in my guts, security is a way of life. And I think ethics and integrity are a way of life. Now, in industry, you have the ISO9000 standards. Within that level of quality you have to educate your operators or the people who work for you. Depending on the company it is repeated every week, every month, every year and these are the rules we abide by for ISO9000. Now shouldn't that ISO9000 be on the integrity and ethics base also for the individual? If you work in a certain industry, you have to have a certain level of integrity and ethics. You should have to be certified to ISO9000, not only certified, but every year you have to repeat that exam in front of a examining board. And there might be different levels of integrity and ethics depending on the level you have in that company. But by repeating that, and this is where I think the regulators can impose the repetition of the rules of basic integrity and ethics which have got to belong to that industry, by repeating and repeating, it will take maybe years, but you will re-instill something that has, to my understanding, totally and completely disappeared from the industry, because of greed. And because people have gone away of thinking integrity and ethics as the family of M. Demandolx did.

William Black
What you are referring to is the ethics of Socrates. His emphasis was habit, that this happens because you were brought up and it becomes a habit its insisted upon and it must be consistent, it must be demanded by the community, the peers, your parents and eventually it will be internalized as we would say in the modern era, and it would become a habit and you would simply do it. That's certainly true; I would say it raises a way to make many of the things we have said consistent. No one believes you can mandate ethics by regulation. Our function is to prevent the perverse incentives that occur when there is a Gresham's dynamic, when cheater prosper, or where you deliberately create adverse selection, such way that you are going to produce widespread fraud, liars loans. We can and we must intervene to stop those perverse incentives. This is the level play field that Jan talked about, that can only be leveled if there is someone there that says "No u cannot prosper by cheating".

Question
We are talking about independent financial advisers and I think we use this precaution system that has just been put forward to us because we wouldn't survive otherwise, if we don't apply it everyday. The people we have been talking about have been Enron, Lehman Brothers, Goldman Sachs, these are large companies. Now I think apart of that level, which we have discussed and seen the pitfalls, there is another thing that strikes me, it is the national states. Because you just mentioned that you can't borrow more than you can repay, which was the basic of the subprime. Now I think if you make an analogy with Lehman Brothers in the financial sphere, I think Greece is going to be the scapegoat of the national states.. And any other countries will be let off and continue to borrow and put their future at risk with no control at all.

Eliot Spitzer
States do have the unique capacity to tax, which changes the dynamic at a certain level. It doesn't mean its good policy. I am not disagreeing with you at all about your bottom line conclusion that the degree of state leverage and government borrowing is way beyond to what is either rational or can be justified in the long run. I happen to believe that the short term deficit that the US government is building up right now was necessary to avoid an even deeper economic cataclysm, the longer term trend lines in terms of spending obviously are now finally beginning to get serious attention, and so your bottom line conclusion is right. The only footnote that I would add is the differential between private and public sector is the capacity to tax, which does change the complexion of the analysis.

William Black
But your sharper point about lying is certainly the case. No one should be allowed to proceed through a pattern of lying, Greece proceeded under a policy of lying with Goldman providing the way to do that. And so in the US, the metaphor I tried to get across when you have these kinds of deceptions, we have on the passenger side's mirror a warning that says "objects in mirrors are closer than they appear". When you have accounting fraud, bankruptcy is closer than it appears. But it looks bright and pristine, unlike it is a real image right up to the point where it explodes.

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