CONVENTION OF INDEPENDENT
FINANCIAL ADVISORS
A Non-Profit Foundation

A Non-Governmental Organization in special consultative status
with the Economic and Social Council of the United Nations

White paper

11th international forum of the CIFA

April 24-26, 2013, Monaco

Can the world financial system be reformed?

Report of round tables and debates

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Acting for ethical, sustainable, and efficient finance

"Ethics and the governance of financial markets and services est d'une is of crucial importance for promoting healthy and balanced development on a global scale. It is in this spirit that interests of CIFA and the United Nations intersect."
CARLOS LOPES,
Assistant Secretary General of the United Nations,
Former Executive Director of UNITAR

How to limit the risks of toxic and opaque financial products? How to combat – in an ethical and effective way – stock market bubbles, systemic crises, and economic crime? How to reconstruct the markets based on the responsibility and competence of the financial actors? How to involve professionals in the development of regulations and governance principles that they will need to apply?

To protect the fundamental rights of the citizen on the markets and to put finance back at the service of investors, CIFA – a recognized non-profit organization acting in the public's interest – has provided a forum, in association with more than 750,000 people across the world, for considerations regarding the questions facing financiers. This has been made possible thanks to numerous professional federations and associations. The author and custodian of the Charter of the Rights of the Investor, submitted to the UN in 2008, CIFA obtained its special consultancy status with the United Nations within the framework of the Economic and Social Council (ECOSOC); it is accredited by the Conference of the United Nations for Commerce and Development (CNUCED) and is a partner of the United Nations Institute for Training and Research (UNITAR) for the establishment of innovative training regarding the them "Ethics and finance."

For eleven years, CIFA has organized an international forum that draws practitioners and regulators to hear the best international specialists. This forum constitutes one of the most important global events for the financial world.

www.cifango.org

White Book

XIth International CIFA Forum 2013

Monaco, 24-26 april 2013

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Opening Ceremony:

• Guy Raymond COHEN:

It gives me the utmost pleasure to welcome you and declare the XIth International CIFA Forum officially open. For me, the opening of this forum is an emotional and joyous moment because it is a culmination of all the preparation done throughout the year. This work gave me an opportunity to appreciate how efficient and enthusiastic the teams are.

For over 10 years, CIFA has been striving to change the economic paradigm. CIFA wants to make financial reform part of the trend being shaped by the economy of wellbeing and sustainable development. Forum after forum, day after day, CIFA seeks to restore trust in finance by protecting the fundamental rights of ordinary citizens, savers and investors on the financial markets. This newfound trust must be supported by a concept of finance that is healthier, more modern, fairer, more equitable and more responsible. We need the help of every CIFA member and partner to conceive these new foundations for the financial world. So I would like to thank everyone who made this forum a reality, sponsors, speakers and conventioneers.

• Pierre CHRISTODOULIDIS:

For over 10 years, CIFA has been warning the economic community and financial markets against the dangers that the deviant acts of the few poses for the many. The endless series of scandals have caused the loss of thousands of billions of dollars and ruined the lives of millions of people.

Statistics bear this out: Europe has 20 million unemployed and 43 million part-time workers. The unemployment rate in the United States is 7.6%, 12% in Europe and 26% in Greece and Spain.

Since its inception, CIFA has attempted to resist and protest against financial misconduct and the assortment of abuses that plagues the financial system. CIFA informs representatives of the regulatory authorities of this wrongdoing. CIFA advocates principles that are straightforward, rational and universally recognised. You do not have to be a financial expert to understand them. Our message is neither moralistic nor authoritarian; it is simply concern. Listening to this message would help restore trust in the markets.

I would like to thank my colleagues and their teams for the work they do every year to try and advance CIFA's solidarity and ethos even further.

• **Nestor OSORIO:**

Since 2008, the world has been in a serious economic and financial crisis that has set off a job crisis that is crushing people in vulnerable situations, especially the younger generations. In some southern European countries, the unemployment rate among young people can reach 40%. The only way to generate steadier growth across the board and create jobs is through concerted actions, particularly in developing countries.

That is why the ECOSOC talks have deliberately focused on the question of a place for science, technology, innovation and the potential culture holds in restoring growth. New information and communications technologies play a key role because they are expected to help open access for everyone to science and innovation. People are eagerly awaiting the conclusions of CIFA's discussions and I encourage you to immediately give us any recommendations that may be devised in your roundtables.

We must allow the younger generation to expand their creativity in education, science, technology and culture. We must create the right conditions for creating jobs. We can give future generations new values and new jobs through cooperation. One of the greatest challenges for businesses today is training and recruiting skilled labour and making sure workers remain competitive.

The Millennium Development Goals are designed to reduce poverty and stimulate growth. But setting these needed transformations in motion cannot happen without a structural and systemic approach. We must develop credible strategies that foster global development by promoting growth rooted in the inclusion and creation of jobs while securing environmental sustainability. We have acknowledged the private sector's role in this strategy and know we can always count on CIFA's support for the Millennium Goals and the post-2020 agenda.

The causes of the financial and economic crisis we are in are obvious. The governance is not working properly; it was not able to forecast another crisis. Our global system of governance has to involve developing countries more in the international decision-making process and when setting standards. An effective system of economic governance demands the active participation of civil society and the private sector. On this note, I am pleased to know we can count on the cooperation of CIFA and other segments of civil society.

The United Nations has a central role to play in global governance. Therefore, its effectiveness must be shored up so it can contribute to introducing a more intelligible framework that allows for more comprehensive policies.

It is equally important to advocate for corporate ethics and social responsibility. Over a decade ago, CIFA formed a partnership with ECOSOC that has expanded to include education and training. All countries should have competent financial advisors to protect consumers.

I have high expectations for this forum and the discussions that will take place here. The poor and the vulnerable have the same right to dream as anyone else. It is important that CIFA helps us make these dreams come true.

I wish you an excellent 11th forum and great success in your talks.

• Jean CASTELLINI:

I would like to introduce this forum's ambitious theme by citing Shakespeare: "If you can look into the seeds of time / And say which grain will grow and which will not, / Speak then to me." Since I do not have the power to predict the future, I will limit my remarks to giving you my opinion on the feasibility of reforming the global financial system. That said, I care deeply about this issue, just like the questions on transparency in financial markets and centres.

I would like to say a few words on Monaco and some of the initiatives that stand as testaments to the seamless cooperation between the government, the institutional world and professionals that is making it possible to continuously improve the services customers receive from our banking and financial centre.

The occupation of independent financial advisor does not exist in Monaco; advisors practice their profession in financial management companies or institutions. Monaco's marketplace is organised around a sensible regulation system, vigorous productive businesses and professionals who take on additional skills needed to supply measures that reflect the best international practices. Its sound and vibrant marketplace has good oversight and has largely developed over the last 15 or so years. There are laws regulating financial activities, the formation of new mutual and investment funds, anti-money laundering bills and laws against funding terrorism. The first laws passed in the 1990s were endlessly adjusted and in 2007 the Financial Activities Control Commission was created. Our legislation was adapted and modelled after the best practices and standards in global oversight. This fact has been confirmed by all the audits we have undergone in the last few years. The banking profession in Monaco is regulated by the French authorities, more specifically by the Prudential Supervisory Authority, which means we are fortunate to have support from one of the best regulators in Europe. We work with the Authority in a partnership that strives for excellence. So, I would like to stand up against the stigmatisation of the Principality and certain other small countries. The OECD uses four criteria to define a tax haven.

The first is low or no taxes. Yet, Monaco survives on taxation and the income taxes that make up the vast majority of the government's financial resources, the very foundation of our growth. The two major taxes, the VAT and the income tax, are the same as in France. We have never sought to use any form of fiscal dumping to illicitly attract companies to the Principality.

The second criterion is lack of transparency. As I have said, banking is supervised by Banque de France and the Prudential Supervisory Authority.

The third criterion is no exchange of information. On this point, I would point out the great progress the Principality has made. Until recently, we only had a tax treaty with France. As it now stands, we have signed this agreement with 27 countries throughout the world and negotiations are currently under way with some 20 other nations. We are advancing at our own pace with the resources limited by the size of the country, but we are taking on the process, which we acknowledge to be immutable.

The final criterion is a lack of any real economy activity. For the record, there are more people who come to work in Monaco every day than there are citizens. We know it is to our advantage to have this workforce and know-how. I would emphasise that border strongholds are job creators and help France's regions mitigate relatively stagnant growth. Monaco's economy is very diversified and extremely vibrant.

We believe that sound government finances guarantee our continued prosperity. We are not inclined to resort to extreme measures because we are debt-free. The spending we generate does not go to repaying loans, but rather to investing in the future, building public works and housing. The state plays an active role in the Principality in symmetry with banking and financial professionals.

I wanted to make these specific points on the truth about Monaco. I am anxiously awaiting the outcomes of your work here. I hope your discussions are excellent and very constructive for CIFA.

"SCIENCE, TECHNOLOGY AND INNOVATION AND THE POTENTIAL OF CULTURE FOR PROMOTING SUSTAINABLE DEVELOPMENT AND ACHIEVING THE MDGs"

Moderator:
Hanifa D. MEZOUI, , Senior Advisor, Humanitarian Affairs and Civil Society, High Representative for the Alliance of Civilizations at the Office of the United Nations and ECOSOC, International Association of Economic and Social Councils and Similar Institutions (AICESIS), Member of the Executive Committee, CIFA

Speakers:
- Jean PING, Former President of the African Union, President of the 59th Session of the UN General Assembly, former President of OPEC;
- Me. François LORIOT, President Bar Association for Inter-Governmental Organizations and Vice-President AIFOMD (UN-MDG training);
- Prof. William K. BLACK, White-collar criminologist and former senior financial regulator, Associate Professor of Economics and Law, University of Missouri, Kansas City, United States;
- Andrei ABRAMOV, Chief, DESA NGO Branch, ECOSOC

• HANIFA D. MEZOUI:

As the United Nations celebrates its 67th anniversary and CIFA holds its 11th forum, together CIFA and ECOSOC decided to construct the theme for this first roundtable around one of the key issues in the Millennium Development Goals: the role of science, new technologies, innovation and culture in sustainable development. Our goal in this discussion is to look at how the financial sector can help orient these endeavours toward sustainable development.

• Jean PING:

The financial sector plays a critical role in sustainable development. The freedom to start businesses and invest underpins innovation in every sector. Yet, it is also important for policies to guide investors. For example, investors do not see Africa as being very attractive, which is illogical when you know that there are over 1 billion people and vast resources in Africa. Not to mention, Africa only produces 4% of the world's pollution. Yet Africa has no permanent member on the United Nations Security Council. International regulations on ecology are not enforced on the continent and are halting its growth. Africa needs financial support so it can support its own development and growth, but it also needs a platform where it can be heard by international public opinion. In this respect, CIFA has a vital role to play in the United Nations where it must be speak for those who have no voice.

• Andrei ABRAMOV:

The theme chosen for this forum is very salient and quite relevant to the current situation. Indeed, the goal is to reinvent the global economic, financial and social model and not to change it. The Rio+20 summit focused on the fact that the world has reached a critical point where nearly two-thirds of our natural resources are in decline. The current economic model has no protections for the environment or strategies for reducing poverty and improving the quality of life for those who have reached high consumption levels. Creating a new growth model entails changing consumption patterns, adjusting prices, accounting for pollution and the impact of oil consumption on the climate.

Everything we do should be geared toward social well-being and the financial sector must be part of the general economy, not go it alone.

We live in a time of constant change. We have to invest in science, technology and innovation, especially in developing countries that have some relative catching-up to do in these areas but are nonetheless offering support. Firstly, the financial sector has to play a more active role in the economy and allow for changes in the core model. We have to play the role of facilitator in the economy by steering the economies of some countries towards geographic segments that need investments. When that happens, the people can share in the wealth. The problem is that while some of the obstacles between the financial sector and the real economy have been toppled, many of them are still in place.

In 1999, President Clinton decided to end the separation between commercial and investment banks. This then allowed companies in developed countries to de-localise some of their output and some capitalists accumulated the surplus. All of these factors led to stricter regulations of the financial sector and speculators looked for ways to make more money. This has become the key objective, hence why the financial markets widened the gap of inequality.

There has been a series of financial crises since the 1980s that have triggered economic crises. I would like to go back to two global crises: the 2008 crisis in the United States and Europe's sovereign debt crisis. The financial markets and the banks panicked when they realised they were holding massive amounts of toxic loans. In 2010, Greece needed a €175 billion bailout, Portugal required €78 billion and then Ireland needed €67 billion and Cyprus €10 billion. This crisis was borderless and now seems to be spreading into Slovenia and Malta. It is probably the biggest financial crisis in all of human history.

Certain features of the financial markets promote instability. For every dollar that comes out of the real economy, $40 is earned on the financial markets. The bubbles are bursting faster and faster, and we should not forget that we still do not know exactly how many toxic loans have yet to surface. The IMF thinks we are talking about €800 billion. It is absolutely crucial that we reinvent the financial sector and integrate it better into the actual economy.

It seems like a good time to address the issue of market efficiency. It is a matter of abolishing the reserve system, banning market investments with borrowed funds or even instituting government control of the financial and banking sectors. All of these ideas are worthy of consideration, but we do not actually know how to fix the situation or how to regulate the financial sector.

We have witnessed bad capital investments, yet one cannot help but notice that some governments are clearly incapable of managing the situation. It is vital that we find examples of the right way to handle it and share best practices. The sovereign debt is an especially thorny problem because the people are the ones who suffer.

We need to find urgent solutions. CIFA has vast experience in these matters and clearly protected the rights of investors. The United Nations could use this knowledge to bring the financial sector back into the real economy.

• **Hanifa D. MEZOUI:**

I would now like us to listen to the analysis of William Black, a specialist in white-collar crime.

• **William K. BLACK:**

The Millennium Goals are designed to obtain the following results by 2015 (compared to 2000 levels):

- Eradicate extreme poverty by over 50%;
- Provide primary education for everyone worldwide;
- Achieve gender equality (give more power to women);
- Reduce the infant mortality rate by at least two-thirds;
- Improve maternal health and lower mortality by 75%;
- Fight diseases like malaria;
- Institute sustainable development;
- Create a global partnership for development.

These goals are quite astute because they are critical. Science and technology will help achieve some of these objectives given that, with the exception of the advances made in retrovirals to treat HIV, all of the science we need has already been available for a century. Thus, it is about seizing opportunities that have existed for a very long time. The only new components are innovation and culture, which brings us to the issue of organising the economy. It is not satisfactory in its current state nor is it conducive to achieving these goals.

Many of these objectives are intertwined. Improving primary education for women helps reduce maternal mortality, keep the number of undesired pregnancies down and thereby changing the fertility rate. Over the last 30 years, we have come to realise that improving the state of the family starts with educating the mother. Yet, this is where we encounter a cultural obstacle because some of these topics remain very controversial in some countries and this includes developed countries. For example, the United States is a very conservative and religious country and progress has been halted on contraception because politics is influenced by concern for how a certain section of the population will vote.

Most of these goals will be achieved by embarking on efforts to address water and sanitation. These are essentially the two vectors behind the spread of disease. The problem goes back millennia and we know that all we have to do is improve the supply of drinking water to bring down the number of chronic disease and infection. From a technological standpoint, it would have been possible to make these improvement 60 years ago but we were dealing with a political problem.

The first goal – eradicate poverty – harks back to the economy. The basic answer is we have to tackle to issue of China and India and then Africa, in that order. Until now, it has been impossible to substantially reduce poverty on that continent but at least the developed countries have realised it did not make sense to close off populations with crushing debts.

Another goal deals with environmental sustainability. It is important that we all share these objectives. The issue had been highly focused on climate change and carbon, but this goal has ceased to mention these factors. This deliberate omission will in turn come into conflict with the goal to eradicate poverty because alleviating poverty actually creates pollution, as we can see in India and China.

China generates the most pollution in the world, although the United States still holds the lead on per-capita pollution. India is on the path to using the same growth tactics as China, so we can expect a sharp rise in CO_2 and methane. Unless all the scientists are wrong, we should expect to see a substantial problem in this area.

• Hanifa D. MEZOUI:

I will now give the floor to François Loriot.

• François LORIOT:

A new concern has been emerging in recent years, the issue of ethics. We talk about MDG ethics, the entrepreneurial ethics of corporate social responsibility. These new terms describe situations that have existed for several decades. The underlying causes of this shift can be found in the aftermath of World War II. After the war, a series of tribunals were organised that shed light on the conduct of some banks and how certain people had provided funds to finance the extermination camps. The rulings of these tribunals sparked the spread of ethics in the business world. CEOs had to begin adopting behaviour that was more humane and in 1947 the United Nations passed the convention on human rights.

This prompted a new movement in the 1950s. Business leaders became more concerned about the consequences of their actions and their investments. At that time, bankers did not think they had to be held accountable for their dealings. Since then, this has become a universal preoccupation.

The CIFA rules demonstrate that its mission references human rights, from which no one is exempt. We hope that everyone who works in the financial sector will adhere to the same commitments.

My association is an AIFOMD association. We have worked a lot on MDG issues and for the last decade have initiated a number of projects. In particular, we have met with many financial decision-makers to explain to them how the MDGs apply to the world of business, investment and banking. This concept should be linked to the notions of competition and profits. It goes without saying that some institutions have become leaders in MDGs and social responsibility.

We recently opened a centre in Thailand to promote the MDG concepts and corporate social responsibility in the business world of Southeast Asia. People study at the centre and then return to their home countries and spread our values.

We have not yet managed to eradicate extreme poverty. We have learned that this goal and the sustainable development goal will be extended to 2030. We have given many companies a new vision of the world and a more ethical way to conduct business. I encourage CIFA to continue its efforts in these matters and would like to offer a few suggestions. The first suggestion would be to upgrade your website and create a link between the MDGs, sustainable development and what independent financial advisors can do to promote these sorts of efforts.

• Hanifa D. MEZOUI:

Thank you for those sound recommendations. One of CIFA's front-line initiatives, and one we are very proud of, pertains to the rights of investors. CIFA has helped make technology and science a stronger part of development. Thanks to its work, in spite of today's climate of unrest, it is raising questions about the status quo and paving new inroads.

Can we reform the global financial system? This roundtable will help open that discussion and we will talk about it throughout the forum. Jean Ping is now going to offer a few conclusions.

• Jean PING:

Rather than conclude, I am going to add to the discussion. With regard to the environment, since Africa is not polluting it is capable of shifting directly over to green energy and bypassing the Indian and Chinese model. In fact, we have sun and the largest rivers in the world. The problem lies in the science and technology to move towards this green energy; the developed world jealously guards these human resources. We have no money to pay for them so the countries that have them would have to donate them to us for the good of humanity. We are all in the same boat and need to work toward a common goal. Even though we do not pollute, we are suffering from the consequences of extreme environmental changes.

The second problem is education and disease. This issue ties in with problems with technology and finances and the Millennium Goals. One of the goals is education for all. This is rather easy to achieve but we still need adequate resources, particularly in communications. Enrolment in primary education is under 50% in some desert regions. The only way nomad children can take classes is through technology. The other goal on fighting disease can also be reached with technology. There is a telemedicine programme in India that provides information to the most remote areas. A programme like this would be very useful in Africa. Furthermore, African peasants are not aware of changes in the price of goods and do not know when shippers are coming to collect their harvests. Simply using a mobile telephone would solve these problems. Applications like these are simple in developed countries but are incredibly valuable on our continent.

Speech by Brother Marie Pâques

"Searching for meaning" Crises, Business, Spirituality

I recently wrote a book called "Searching for Meaning" in support of our political, entrepreneurial and banking brothers who were particularly mistreated during the 2008-2009 crisis. We have heard a lot about «bosses from hell» and «greedy bankers.» Despising an entire profession that does amazing work for the good of humanity is not fair and is distorting reality. I think this was a moral crisis that took on financial excesses. In light of the nonsense being reported by the press, I felt it was important to speak about it.

I would like to divide my remarks into three parts: we got ready for the party, the party was ruined and then I ask you to plan the party so we find a peaceful coexistence.

In the monasteries we are constantly reminded of the end of our lives and our fleeting time on earth, and I think it is important to think about why we are here. According to the Christian tradition, humans are made in God's image and are able to make choices and to love. It is because we have a common nature that we have a common destiny and we are bothers and sisters in humanity, equal in dignity. People need the social element. We are all shaped by our interactions with others and a peaceful coexistence leads to developing new skills that we can contribute to the common good. People shape themselves with those around them and develop these potentialities.

The law must respect the dignity of human beings and this dignity should be linked to the common good. Governing amounts to finding a balance between the good of one human being and the common good. Certainly, we find this negotiation in the banking profession, which is a noble profession because development is not possible without investment.

Putting the common good over the good of one person is a wrong that must be made right. The common good demands a quest for peace. Peaceful coexistence requires peace, peace requires justice and justice requires sustainable and integral development for all humans.

We must advance this sense of an overall view of the world in all professions so that every decision is settled within a vision of peace and justice. Failure to remember this purpose amounts to corrupting finance.

If we are ready for the party, we are also capable of ruining it. Voltaire said, "What makes and will always make this world into a valley of tears is the insatiable greed and implacable pride of men." Greed and pride threaten peaceful coexistence and ruin the party. Greed is a misguided desire to always make more money with disregard for others. It is self-imprisonment fuelled by pride, which reflects immoderate self-love. At the same time, hundreds of thousands of people are living in poverty and this leads to despair and rebellion.

Thirdly, we are made to plan the party. Gandhi said, "Replace greed with love and everything will fall into place." What is love? To love means to involve yourself, to choose the other person, to choose to put that someone else's good before your own. Love comes at a cost and love means making sacrifices. Love is the premise behind brotherly and friendly relationships as well as macro-relationships. Love should resolve social, economic and political relations.

Love should be disinterested. This dynamic is a source of peace, joy and inner happiness. Love lasts and endures. Love weathers injustice and we must learn to accept unrequited love. The pinnacle of freedom for humans is to love without bounds, without expecting anything in return, by withstanding injustice. Love always forgives. This is what Christian charity is. It can help transform our world today into a world of celebration. Love takes care of the good of others and the good of all.

All the great writers of scripture or throughout human history were great because they were agonizingly wounded by the suffering of their fellow humans. The burden of the world is upon the shoulders of men and women and it is a heavy burden.

I do not know what you have contributed to peace and justice, but the theme of this seminar is, "Can we change the rules of finance to steer it toward contributing to the common good?" Yes, I think it can happen. We must all listen to our conscience; that is how you can achieve great things.

In life, there is more joy to give than to receive. We have predicated ourselves on this fact to devise a global concept to prove there is more happiness to give than to receive. Solidarity will save the world and finance will be a tool.

Thursday, April 25th

The session is chaired by Indira Tasan, Editor-in-Chief of Banco Magazine.

Welcome address

• **Indira TASAN:**

Hello everyone. Do you know what the fourth largest country in the world is with a population of about 250 million people? This country is the world's 16th largest economy in terms of GDP. The disposable income of its middle class is growing at a rate of 5% per year. We are obviously talking today about the financial crisis, but the world does not amount to that alone. In fact, the country I am talking about creates 10 million jobs every year and is seeing strong economic growth. Last year, it was also rated favourably by Moody's, Fitch and other agencies. Its sovereign debt is only 25% of GDP. Of course, I am talking about Indonesia! Banco would like to open its first Asian office. There are wonderful opportunities in asset management in Indonesia. Demand in the sector is constantly rising and Indonesians are looking for new types of investment. According to a McKinsey report, our sector will see double-digit growth in Indonesia from 2010 to 2013. We think the market is very dynamic and stimulating.

Saving the world financial system: who will pay?

Roundtable speakers:

- Lenore Elle Hawkins, MBA, Partner, Meritas Advisors, San Diego, USA
- Luca Fantacci, Associate professor, Department of Policy Analysis and Public Management, Bocconi University, Milan, Italy
- Daniel Mitchell, Senior Fellow, Cato Institute, Washington, USA

• Indira TASAN:

Where will the money come from to save the financial system? Will it come from institutions that were bailed out? Will it be paid by investors, shareholders, bond holders, perhaps taxpayers? Will the central banks continue printing bank notes?

• Lenore Elle HAWKINS:

Firstly, we have to analyse the problem. Right now the tendency is to believe the market will not have fulfilled its role. That implies the market was working normally before the crisis, but that was clearly not true. Incidentally, Alan Greenspan wanted to stabilise the markets and implemented a risk management policy. Once the markets were strong enough to avoid a recession, the risk controls could be lifted so the economic community instituted more aggressive policies. For example, the banks could approve riskier loans and increase their profits.

In 2006, the rules were changed but market players were not really aware of it. Interest rates skyrocketed 425 basis points in 18 months. The bank were then assured they would be protected, that there would not be a recession... At the time, the financial leaders had very little experience with that kind of recession. They did not anticipate this turn for the worse. These people had been trained for 20 or 30 years to think that the government's control systems would stop any recession.

Institutions in the United States, in particular, wanted to increase lending facilities. Every month in the United States the Federal Reserve was buying 90% of all bond issues. What money were they investing? The stock market was constantly going up but the payouts were far from spectacular; a 3% return is low when inflation is at 2%. People in the system in turn started taking more and more risks, especially bank managers in a move to raise available credit, whereas they were simultaneously being criticised for not managing risks well a few years before. That is the paradox in which we now find ourselves. And that paradox is even more insufferable because we are in the middle of a financial depression. Asset managers, investors and pension funds are being forced to take an increasing number of risks to yield a decent return on their investments. "Run-of-the-mill" portfolios are in no way adjusted for the climate – considering the aging of the population – in particular, they are taking on some extremely high risks. It is very difficult to earn any returns from them. Who will pay? The people who have money! And this money will be taken by the people who need it.

• Luca FANTACCI:

I am very concerned about the future. For about five years now, the behaviour in dealing with the crisis, especially from the central banks, is similar to the behaviour that caused the crisis. You mentioned the moves made by Mr. Greenspan and the "soft" monetary policies. Those are essentially the attitudes people adopted to deal with substantial debts. The government is struggling to pay their debts and, once again, they have turned to the central banks. But the central banks can avoid paying their own debts and just print more money. This results in distorting the entire system and in our current situation no one in the market seems to be taking any more responsibility for their own decisions – it is the opposite of how it should be.

People are taking more and more risks. Granted, risk is inherent in the financial world. Yet, expansionist monetary policies wrongly create the impression that there is no more risk. This is not a desirable viewpoint in the least. The players have to assume the risks for the investment decisions they make between, for instance, loaning to a borrower who can pay it back and loaning to a borrower who poses a serious risk. So, I think the way the crisis has been handled is clashing with the monetary policy structure and the financial system's operating mode. It does not appear possible to resolve the situation until we leave the international monetary system. The system was founded in 1971 based on the premise of creating money without any real offset. I am not saying we should return to the gold standard, but we must reinstitute a genuine link between money and the actual economy.

There is one idea I think should be adopted that was brushed aside in the Bernanke era. Keynes had mentioned a sort of international "clearing house" and wanted to institute a global unit of currency separate from national currencies. That way the national deficits of countries would not show up in the system. They could then print money to pay for goods and services that were in both the buyer's and the seller's interest. Keynes stressed the need to plan for the destruction of the money as soon as it was created. Therefore, debtor countries have to pay their debts and creditor countries spend this credit instead of accumulating it. The thinking was to work our way back to a balanced position.

• **Daniel MITCHELL:**

We cannot consume more than we produce! If a country or sub-group of the economy wants to consume more than it produces, sooner or later the bubble will burst. Who will pay?

First of all, I would compare capitalism without failure to medicine without health. If some people in the system are prepared to take risks and let others bear the consequences, it means private profits are being made and offset by social losses. This is an absurd tactic. For example, the banking sector in Cyprus committed a serious mistake using its clients' money to buy up loads of Greek bonds. That led to the crisis. Who is going to pay when the Cypriot banks have failed? It should be the shareholders and then the bond holders and then the people with uninsured bank accounts and lastly the taxpayers. That is sort of what happened in a very awkward way. It would be rather expedient for the global economy and the banking system if the Cypriot situation were seen as an example, then major investors would probably pay more attention to the situation in other countries, in their own financial system, etc.

I would also like to mention the fiscal crisis. There are serious problems in Italy, Spain, Japan, France, etc. Twenty years from now every country will be having problems. Who will pay then? The government, once again, will respond with inadequate solutions by bailing out some country or institution, buying their debts, etc. Yet, in public finance matters, governments cannot spend more than the economy produces. Unfortunately, politicians have probably not learned this lesson and are thinking in the short term. So we are heading for an increasing number of fiscal crises. Many countries are already seeing social unrest in the face of rising taxes, unemployment, mounting deficits, etc. Society will begin to unravel and everyone will pay in the end.

• Indira TASAN:

Do you have other outlooks for the future that are more optimistic?

• Luca FANTACCI:

I find it difficult. The crisis will not end on its own. For that to happen we have to take action and offer solutions instead of projections.

Europe is a topic of major concern. In effect, as you mentioned a relatively decent agreement was reached in Cyprus. Solutions like that have to become the standard, in other words making the people who are responsible for the debts pay them back. That said, this is not the path that has been taken so far in Europe or elsewhere; we have been supporting creditors and debt-creators more than anything. States and central banks played a key role in this process.

Our economic systems are producing more than they consume, but the issue lies in delivering what they produce to the markets. Unfortunately, governments increasingly took over the task of linking production and consumption and public demand disproportionately and unfairly compensated for private demand. This approach is only a worst-case scenario when responding in macroeconomic terms. We have to create a system that would not generate systematic supply surpluses in relation to demand and thereby would not constantly require government intervention.

Keynesian theories were misunderstood. Keynes neither invented nor recommended government spending, but he believed that in his time it was difficult to not rely on it. So, we have to drop the illusion that spending and public indebtedness holds protectionist virtues. When Keynes proposed a global currency, he thought that money should have to represent real assets. The solutions proposed should follow that logic.

The fundamental problem in Europe has to do with foreign debt; substantial credit is being accumulated in Germany and Scandinavia and the Mediterranean countries are accumulating debts of about €1,000 billion. This chasm must be closed by encouraging the Mediterranean countries to pay back their debts and the northern countries to spend their credit. This would restore the balances within the European Central Bank and serve as a good starting point.

• Lenore Elle HAWKINS:

One cause of the problem is the mass mentality. For decades, we thought the powers that be and regulatory authorities were protecting us. Ratings agencies supplied false information, as we saw with the mortgage lending institutions Freddie Mac and Fannie Mae. So the banking sector and financial industry, in particular, thought they were protected by regulators. But, by definition, regulators are more designed to focus on details, not innovate. You cannot have one without the other. We needed to obtain some feedback, especially on the failures. A few years ago, small rather well-managed banks fell victim to other larger banks that took them over, even as those large institutions were posting very high debt levels. The well-managed banks then received low ratings because they had been bought out, unlike some large banks that were acting irresponsibly. In the end, this scenario "blew up." Then the central banks intervened and the root of the problem was never solved. We are somewhat to blame for the situation because we were the ones who elected the political rulers in power. Right now – and this is on a positive note – people are second-guessing the common belief that governments are the protectors. I think the fact that conflicting opinions can be expressed is positive.

There is probably no one solution that will allow everyone to protect themselves against risk. We are looking for returns on our investments. Even if we try endlessly to eliminate risk, we cannot get rid of it completely. The only thing we can do is diversify. Returns are still in the hands of those who are close to power and collect the profits.

• Indira TASAN:

You point out that we cannot produce more than we consume, and vice verse, but that observation also boils down to a question of scale. At the microeconomic scale, for example between a chocolate factory and a baker, it is easy to adjust supply and demand. At the global scale, however, it undoubtedly calls for some education since we have to consider different cultures, etc.

• Lenore Elle HAWKINS:

I think feedback is essential. A factory that supplies more than its customers demand would rack up inventory, lower its prices and end up changing its production schedule. In a market that is truly functioning properly, habits can be changed based on the resulting feedback loop. These mechanisms default when it pertains to government policy. For example, there is no proof the economy's supply and profits go up when central banks raise liquidity. What about systems to provide feedback to these banks? Incidentally, we are now dealing with Basel III, but investments in sovereign debt were not very productive in the aftermath of Basel I and II. So governments do not have all the information or "market intelligence." The models have to be diversified and competition brought into play between the systems instead of forcing every country around the world to adhere to a single regulatory model that may be defective. This single model was designed by bureaucrats and is not necessarily the best option.

What the central banks, governments and regulatory authorities are doing is distorting the financial markets. That is an issue of deregulation. It is crucial that we restore a healthy relationship between lenders and borrowers. The subprime crisis essentially changed the paradigm. It used to be that when a banker approved a loan, he had to verify the borrower's ability to pay it back. If lenders can now sell loans to someone else, who does not assume the risk themselves and then resells the loan, the financial system is being stripped of its accountability. Holders of shares or bonds should show some accountability and be concerned about the content of their securities. The financial crisis revealed this was not happening. Thus, we must accept failure and analyse the risk, for example, of the mortgage system. The market believed there was no risk as long as housing prices were going up.

There is no moment of debt payment today, meaning the moment of truth between the borrower and the lender. Bond holders are not obligated to wait until the end of their loan terms, they can securitize the debt and resell it by assuming liquidity in the market. The credit risk has now turned into a liquidity risk. But who is taking on this risk? That is where the central banks come in; if holders of securities do not have a buyer to resell them to, the central banks buy them. This has created the illusion they are generating liquidity in a market that will ultimately not be liquid. So liquidity is both the solution and the problem.

How did we get here? Bonds were considered to not carry any risk and this notion was supported by the Basel agreements. And bonds were poorly "labelled" by the agencies, which gave them an "AAA" rating. This then penalised market players who would have wanted to make their own assessment of the situation and the risks since everyone else on the market was actually buying and selling securities quickly and earning more money while being protected from failure. That was a genuine "lack of accountability premium" on the market. In turn, the people who were trying to make informed decisions and thoroughly assess what they were buying for their clients were the ones who paid the price because the bigger market players were not being as cautious.

• Indira TASAN:

In the United States, who is going to bail out the states that are on the verge of bankruptcy? What solutions could be implemented?

• Dan MITCHELL:

You are most likely referring to California and Illinois, which cannot repay their debts and may potentially go under. I do not think the federal government will put the matter up for a vote in Congress, but it seems as though the Federal Reserve may buy their debt. Yet, if the Fed begins buying the debts of irresponsible states, like the ECB took over Greece's and Portugal's debt, where does it end? That would only exacerbate the lack of accountability we are talking about.

I hope there will not be a bailout system like that and I also do not think the other states want to bail out states that have been irresponsible. California is in a very difficult position and has decided to raise taxes. Unless the Fed comes to its rescue, it risks going bankrupt, especially since entrepreneurs may leave the state if their taxes increase.

• Indira TASAN:

Why, for example, did we recommend investing in Iceland? At the time, the country was rated "AAA" and no one could have predicted its failure. First of all, this is an example of a need for institutional accountability in conducting assessments. But as advisors, what options do we have to obtain any in-depth knowledge of the situation of banks, brokers and other bodies?

• Lenore Elle HAWKINS:

I hope our profession and related professions will exercise much more scrutiny going forward. For example, some real ratings competition could be instituted with independent ratings. Then we would have actual analyses, not only the ones done by agencies that have a monopoly. Their recommendations have essentially proved to be questionable. But we need sound advice, particularly when the climate is strained. In a period when the markets were relatively stable, investing in a good company and holding on to the securities worked relatively well. That approach no longer works. A long list of macroeconomic factors can now change the odds.

Our work will then become increasingly independent and market players will pay more and more attention to independent assessments that are not issued by such and such institution that has obviously fallen victim to conflicting interests. Ratings agencies cannot conduct truly objective analyses if they are too closely linked to an institution. These agencies are even paid by the institutions they are supposed to be evaluating.

• Dan MITCHELL:

Ratings agencies issue their assessment of a situation, but do not assume any risk, which means the very concept of relying on these agencies may seem absurd. We want to be responsible financial advisors. But we lacked a climate of accountability where our good decisions are rewarded and vice verse. This system, which is based on the principle of irresponsibility, was invented some 30 years ago. The crisis did not actually begin five or six years ago. The lender-borrower relationship changed as securitization became the norm. We now have to look at the underlying issues, not just restore this lender-borrower relationship but also address the liquidity problem on domestic markets. A sort of tax would have to be levied on financial transactions, but it should not introduce more distortion. If the only distortion encourages long-term investment, that would be a step toward a more responsible and sound environment.

• Participant:

I worked with the regulator. Historically speaking, the situation did not necessarily start 30 years ago. The "re-regulation" began one year after the deregulation laws were passed. That saved billions of dollars. In

1989-1990, we realised some market segments had to be subdivided. Alan Greenspan refused to open a fraud investigation even though he knew that 90% of the loans were fraudulent and in some way or another had been created by the banks. At the time, the head of the Office of Thrift Supervision was supposed to be regulating the businesses that were likely the root of the evil, but instead he killed the regulations and oversight in force. Alan Greenspan stressed a need to stir up competition. In the end, London wound up winning the race against the Americans. But today there are about a dozen scandals coming out of London's financial district!

If you are interested in a different viewpoint than Fox News, I would be delighted to give you more information.

• **Participant:**

Liking the free market does not mean liking fraud. Fraud should be punished, yet regulations should not be too heavy or limiting. The best discipline on the market comes from using an approach where can people fail personally and lose their money. So I denounce intervention from central banks and the current regulations.

• **Lenore Elle HAWKINS:**

The problem stems from the fact that governments and central banks are intervening on the market to save certain people from bankruptcy. What would happen without this massive intervention? People who had made bad decisions would of course be punished, but others who had not made bad choices would also have suffered losses. That is where the system poses a problem because we are unwittingly taking on risk. Typically, investors are rewarded for their investment because they assumed a risk. If they lose their money, it is not necessarily the result of a bad decision but for the very fact that the world carries risk. Yet, this cannot work if the market ultimately obscures the risk. Government policy itself is forcing us to make increasingly risky investments. Twenty years ago, without too much risk you could make decent retirement yields. Now it means taking on excessive risks. If they are being forced to purchase assets they do not want and if events take a turn for the worse, investors will ask to be compensated and protected. In concrete terms, even more distortion has to be created on the market. This puts us in a real vicious circle. At the end of the day, who is going to pay for it? Future generations will. In a certain way, the sovereign debt winds up stealing them. Young college graduates in Spain, Greece and even the United States have no hope for the future. They cannot find a job even though they are fully qualified and have taken out loans to pay for school, etc.

Did the banking regulation solve the problems after the 2008 financial crisis, or did it create new ones?

Roundtable speakers:

- Anthony Saunders, John M. Schiff Professor of Finance, Leonard N. Stern School of Business, New York University, New York, United States;
- Louise C. Bennetts, Associate Director of Financial Regulation Studies, Cato Institute, Washington, D.C, United States.

I. Reasons for the crisis

• Louise C. BENNETTS:

First, I am going to look at the reasons provided for the crisis. No one really defines the problem the same way.

Financial institutions in the United States have too many leveraging effects. A lot of banks had subprime mortgages that were accepted as risk-free in the American regulatory system because of their leverage effect.

Other analysts cite a liquidity problem. American investment banks rely heavily on short-term financing. That is probably why massive amounts of liquidity were injected into the system.

Some claim there is another reason. The problem had to do with distortion in the mortgage market and some put the figure at US$3.5 trillion. The government's role is blamed for triggering the crisis, but in 2007 there were 27 million subprime loans, which is a huge amount.

Still others think the crisis was caused by a proliferation of complex financial instruments that concealed the risk. Some point out that in 2007, right before the crisis, the accounting system changed and the fair price – the current price – replaced long-term value. This caused major capitalisation problems for the banks. One of the other reasons for the crisis was a lack of clear options for large banking institutions to fail, which reasoned they were "too big to fail." The "easy money" policy and low interest rates are also cited as reasons. They created a bubble by coercing people into not realising the value of their long-term investments.

The crisis is most likely connected to a combination of all these factors, some of which are more significant than others. The last factor was probably the most substantial.

Conversely, some elements did not cause the crisis. The first of them is trading; 2008 was not a stellar year. Investment banks had assets on their books that they did not sell, these were low-level transactions. What's more is investment activities were linked to the retail banking business. For example, Canada, Australia and South Africa have integrated banking systems and have never had a financial crisis. In 2008, the banks that were experiencing problems were purely investment banks, or thrift banks.

II. The outcome of the Dodd-Frank Act

The US Congress approved the Dodd-Frank Act in June 2010, six months before the Commission published its report on the causes of the financial crisis. Barack Obama's advisor Rahm Emanuel believes lessons can still be learned from the crises. So, the Dodd-Frank Act was another move in a long effort to push regulation through Congress. It is hard to measure the implications of the mandatory provisions in the law. Dodd-Frank introduced a new regulation on derivatives. In addition, the law was supposed to limit the dependency of investors on ratings agencies. Unfortunately, right now that is the only provision that has been set aside. Next, the law gave rise to a Liquidation Authority that could oversee failures of large financial institutions. Lastly, it raised the asset thresholds required of banks.

1. Limiting the systemic outcomes of bank failure

There is no public bailout system in the United States, by that I mean a system funded by taxpayers. A new strategy was implemented called the Single Point of Entry Recapitalization Procedure. Small individual savers, for example in Cyprus, are not insured. The United States now has this insurance. When a financial institution fails, a sort of holding company is created with bond holders to manage its banking functions. In a certain way, the other lenders become investors in this new financial institution. This is also true in the United Kingdom. Depending on the state of the market, either the institution is recapitalised or it changes owners.

This kind of recapitalisation only works for the holding company. This means Dodd-Frank prevents the situation being treated differentially –following local procedures, one country at a time– at subsidiary levels. This puts bond holders on an even playing field, unlike what happened at Lehman Brothers after September 2008.

That said, other regulators are doing things that conflict with this approach, for example what the Fed is doing with foreign banks. Banks with extensive dealings in the United States are being required to restructure their American companies under an intermediary holding company that has to be capitalised separately to meet the Basel III standards. Branches with over US$10 billion in deposits must have their own capital and follow American requirements, which resulted in a lot of collections and duplications. American regulations may also conflict with their country's own laws. Plus, parent companies will be less inclined to help foreign subsidiaries that run into problems in the United States.

The United Kingdom, on the other hand, decided to protect retail banks by separating them from investment banks. We should be deeply sceptical of how this system will work and how to only safeguard part of the business if they are not kept entirely separate from one another. The Vickers Commission has indeed opted for a more general approach but this legislation contains a sort of financial protectionism to protect British banks from foreign competition. But there were most likely other ways to protect depositors. Rodgin Cohen, a top attorney on failures in the United States has pointed out the risk of "Balkanizing financial services" and constricting the flow of capital across borders.

2. Reforming derivatives

Strict monitoring of complex financial products is not without its problems. The majority of them are managed by American banks throughout the world. The CFTC (Commodity Futures Trading Commission), however, applies very strict rules for both American nationals and, indirectly, non-US actors doing business overseas. The CFTC thus has extraterritorial jurisdiction and wants to regulate all the market players. Last week, nine finance ministers sent a letter to the US Treasury Secretary expressing their view that this method was unacceptable.

To conclude, it is too early to say whether initiatives like Dodd-Frank will resolve any problems. Efforts are under way to deal with the failures, but this law seems rather unwelcome and poorly implemented.

III. Basel III: outcome and consequences

• **Anthony SAUNDERS:**

Will Basel III turn the banks into highly regulated "public utilities" like the gas or electric company?

Historically, banks have been intended to meet the real economy's demand for credit. They also acted as intermediaries and, with the interest rate spread, made it possible to make money. In other words, banks make money through interest rates by lending money. They enable the people to whom they lend the money (sometimes) make money through the leverage effect. Lastly, they were financial innovators. I think Basel III will negatively impact these three functions of banks.

Basel II stipulated that banks had to have 8% of their loans in capital. Basel III imposes stricter requirements that dilute the leverage effect. It adds 2.5% to the initial 8% of capital for provisions plus a 2.5% "countercyclical" requirement as well as a 1-3.5% requirement for 29 banks labelled as systemically important. The list of these banks is updated regularly: Deutsche Bank, HSBC and Citibank, for example, are obliged to have a total ratio of 15.5% of capital. This will reduce the amount of money available for loans and as long as Basel III is enforced in all lending institutions, credit will be limited.

Banks now have to meet liquidity ratios and balance out assets and short- and long-term withdrawals. At that point, the banks cannot make any more money through spreads. Furthermore, securitization was unfairly criticised since it did have some positive effects. It made it possible to increase liquidities on the financial markets, multiply assets in the real estate market, etc. Under Basel III, securitization will become extremely costly.

And banks will look more and more like public utility companies. When that happens, we should be asking ourselves whether the Basel process has gone too far. Basel III actually creates imbalances among market players because more restrictions are put on big banks than small ones. They have lost sight of the founding principle behind the Basel process to create fair and uniform conditions. For that matter, Basel III actually generates more complexity. The ratios are highly technical to calculate and the banks are beginning to baulk. I think it would be better to go back to debt-to-capital ratios that improve the leverage effects with a few minor adjustments.

IV. The effects of the Volcker Rule

The Volcker Rule cannot be compared to the Glass-Steagall Act, which was designed to separate corporate banks from retail banks. It restricts banks and their subsidiaries from trading private equity to 3% of assets held for longer than 60 days or an entity's private equity.

In addition, a holding company cannot own more than a 3% interest in a hedge fund or private fund. But the positive side of the rule is that it stops banks selling toxic assets at a loss, like they were able to do before. In contrast to the Volcker Rule, the Vickers Rule in the UK protects retail banks thereby protecting deposits and not the holding company. For all that, none of these provisions actually separates corporate banks from deposit banks like the Glass-Steagall Act did. So, I do not think the banking system will substantially restructure itself.

Oversight of European banks: moving towards a European SEC?

Roundtable speakers:
- Prof. Dr. Martin Janssen, ECOFIN Research and Consulting AG, Zurich, Switzerland;
- Leong Sze Hian, Financial Advisor, Past President, Society of Financial Service Professionals, Singapore.

• Indira TASAN:

Some political leaders, for example President François Hollande, would like to create a European oversight body. Others, like Angela Merkel, think it would be better to work out the details before embarking on such a reform. However, the idea is gaining traction. In any case, would a European oversight body like this be more effective in dealing with a financial crisis than the SEC in the United States?

• Martin JANSSEN:

What are the banking system's objectives? For the most part, it is the financial intermediary in a market economy. This is basically the concept of private ownership and in this context, governments do not grant banks subsidies when they fail. There is no systemic cross-border arbitration or preferential treatment for owning government bonds. Banks can easily join forces by optimising their lending portfolio. Banks with liquidity problems are either nationalised or enter bankruptcy.

In 2008, the banking oversight systems stopped working. There are many state-owned banks in Europe. Capital levels were low, like for UBS (accounted for under 2.5%). The banks were using their own risk calculation methods, which were peculiar at best. Therefore, the system proved to be ineffective in the face of a crisis.

What changes have been made since then? The banks have become even bigger. Basel II was never applied in the United States and Basel III will not be either. In Europe, enforcement was postponed until 2019, so it will not be used if there is a crisis before then. The "too big to fail" concept still applies. Banks are protected from the impacts of taking excessive risk. So the structures that caused the crisis have not changed.

What factors have changed since 2008? Some banks in some countries were nationalised, if only partially. The two large global banks in Switzerland increased their capital. The German government gave guarantees to the big banks and state-owned banking groups. The ECB lowered its interest rates. The result was a vicious circle where European banks can now borrow at almost 0% and government bonds can be sold at a much higher rate. The Basel regulation is debatable because the banks do not need capital to buy state-issued bonds. But if the states go bankrupt, the banks will fail too, so each party is trying to figure out how to ensure the other is not liquidated. This approach is detrimental for the future. In the end, two latent objectives were sought to raise taxes and regulate the markets more heavily to limit competition.

What is the current situation? The rating process for risks does not work well. Europe does not have an integrated banking market like the United States. Bank portfolios are not very diversified. Some are very local and support local risks and they may have problems in the next crisis with implications for the entire banking system. So, the situation has become worse. Right now we have to introduce a more integrated European banking system with strict rules on failures and liquidation without falling back on taxpayers. However, protectionism will rise.

More regulation is not desirable. Oversight of state banks is no longer independent, yet the ECB's purpose is not to monitor these large banks and prevent them failing. Sometimes these big banks survive at the expense of small banks and financial consulting firms.

• Leong SZE HIAN:

Oversight, banking regulations and the European financial sector must change. The current regulations are not working because they were reactive to the crisis, rather than proactive. Regulators have been assigned the wrong missions, objectives and key indicators; they protect the system but wind up harming market players instead of protecting them.

Rather than trying to protect the financial system, in a time of globalisation regulators should be finding ways to make the financial sector more competitive. When the financial crisis began in 2008, the first thing the affected countries said was they would guarantee deposits in all banks, both state-owned and private. Yet, we live in a highly globalised world. Many people working in the financial sector are not citizens of the countries where they live.

For example, France's economy is not very healthy, unemployment is rising, etc. The proverbial pie is constantly shrinking. The very point of regulations should be to prevent problems by making it bigger.

I think the question put before us today, "saving the world financial system: who will pay?" is the wrong one to ask. If you work for a financial institution, are you really concerned about that? No. Instead, the question should be, "How do we make money in this environment?"

A newspaper recently asserted that in 2020

Switzerland will have lost its position as the top destination for large fortunes. Indeed, governments take a keen interest in private banking centres like Luxembourg and the Caribbean. The wealthiest people are looking for less turbulent places to put their money.

What does that mean for us, the advisors and financial institutions? If you are playing a football match and the rules change halfway through and not in your favour, what do you do? Do you keep playing on that pitch? If you live nearby, of course you would do. But how would it be if someone asks your players to go play on a different pitch where the rules had not changed? In the same vein, the rules for European financial institutions keep changing. At the end of the day, it begins scaring off customers – they, too, can go play on another pitch. And that is exactly where our problem lies because our customers may move their money somewhere else.

The current processes, the fact that money is being pumped into the system while extolling the virtues of austerity, is only adding fuel to the fire. Europe did not retain the lessons learned in Iceland, Greece and Cyprus. Even if there is a European SEC, the problem will still not be resolved because it is first and foremost political. If the regulators do not change the objectives, the problems will persist. In order to solve these problems, regulators have to be able to make unpopular decisions that will nonetheless be good choices for people in the long term. Do you worry about whether a competitor might suggest your customers move their money somewhere else? If you are a financial advisor, you definitely do. Do you want to protect your customers? To do that, will you help them move their money elsewhere? I think I have explained the greatest threat both for Europe and your profession. However, this threat may turn into a huge opportunity for you since all these advisors have come to Monaco to help their customers open offshore accounts.

• Indira TASAN:

Above all, customers worry about their money being safe. That is the general context that regulators, the industry and financial advisors should keep in mind, not any specific detail. Rules in the financial sector may have been slow to change, but real and necessary changes have been happening for 30 years. What is your opinion on this matter?

• Martin JANSSEN:

Most of the problems banks have encountered since 2007 and the ways they have reacted are because of regulators. In Europe, the problem has to do with problematic conditions in all countries. Most of them are not following the Maastricht guidelines. If another crisis happens it will be much more catastrophic than the last one. Political regulators have essentially not done what they needed to do. One crucial problem is the banks are undercapitalised, for example UBS. At the present time, the situation is even worse than in 2006 and we will not be able to withstand another crisis. Ordinarily, the regulatory authorities should be recommending tools to the parliaments so they can legislate and obtain the tools. It should not be the politicians themselves making the proposals. From that perspective, for example, the collective investment law passed in Switzerland poses problems.

• Leong SZE HIAN:

I was not referring to the finance industry as a whole, rather to individuals. Even if the financial sector grows, a country may still be in a recession. It is never too late to do something. In Europe and elsewhere, the law poses problems because it is looking to the past and mainly focusing on what we should have done. Instead, we should be learning lessons from the past and thinking about the future. It goes without saying that earnings in the finance world are very high, but it was the regulators and the politicians who created the situation themselves. We have to move toward more transparency and competition, those are the only possible solutions.

• Johannes MUCHITSCH:

It is surprising that the powers of the European banking authority were split up and moved to the ECB. What organisation or institution could act as the European SEC? For the time being, two institutions coexist that do not have any synergy.

• Martin JANSSEN:

London, Paris and Frankfurt share financial oversight powers. The ECB handles oversight for the 150 largest banks. But it is hardly the right organisation to do this. It would be better to create a powerful independent European institution to monitor the big banks. I do not see how that would be possible right now, just from a purely realistic standpoint. In the end, it is not as important to know "who does this and why?" so much as "what are they doing and how?" Proposals must be put forward to make any progress. One solution would perhaps be to create a body similar to the Financial Security Authority that used to exist in the United Kingdom to regulate everyone in the financial sector. Entrusting this role to the central banks is the wrong way to go.

• **Andrei ABRAMOV, United Nations:**

There is a simple mechanism behind financial crises where after an influx of foreign investment, a retreat happens just as quickly. That is what happened in Mexico and Sweden, among others. It is a major hazard for developing countries that have not experienced such a crisis. Brazil and Argentina went through financial crises because their financial systems are closed. In the long term, of course, the flows of capital would have to be released but in the short term, shouldn't regulators be concerned about how the money enters and leaves a given country? I believe these regulators and politicians caused the 2008 crisis, which could have been prevented with better transparency and competition.

• **Martin JANSSEN:**

Regardless of their decisions, all the regulators assured the big banks they would be protected against failure. So it is not surprising that these institutions acted they way they did.

• **Indira** TASAN:

On a practical note, how do we generate more transparency?

• **Martin JANSSEN:**

There are guidelines to achieve it, for example that the institutions must have 20% of their own capital on their books. That said, considering how complex their books are, banks are not able to accurately calculate this capital. Instead of the Basel III rules, which are very complicated and difficult to understand, we should pass rules that are simple, practical and easy to understand. But in reality, the banks have no interest in showing any transparency and if we allow them to not be transparent, they will keep acting as they always have done. The logical thing to do is if the regulations are not working, the regulator and the politicians resign. But they are still in their jobs! That is the fundamental problem. It makes no sense to keep managers in their jobs who have not achieved any promising outcomes.

• **Leong SZE HIAN:**

The job of politicians is to make proposals and be held accountable for them. So far, we have not heard any proposals. The industry could make them itself instead of leaving it up to the politicians. I feel that the industry, in other words competent professionals, should take on this responsibility and not just complain about the regulators. Neither they nor the politicians have the knowledge needed to do it. They will be helpless when the next crisis arrives if we do not offer them any direction. This is not the right place to make these proposals, but each of you can work on it individually and then meet in a workshop to exchange ideas. That could be the goal of the next CIFA workshop. I think this individual work is better than working as a group, which would result in proposals that rule out any risk-taking.

• **William K. BLACK:**

According to you, the banks cannot be blamed for the crisis because they were encouraged to do the wrong things. I think that is an unreasonable point of view. And then claiming the bank CEOs are devoid of any political and moral power, will that improve the situation? If a driver on a road obeys the speed limit at 40 kilometres per hour but conditions make that speed dangerous, then I for one think the driver is responsible.

It is about using your own judgement. I expect the CEOs of major financial institutions to have the expertise and sense of morality required to do that.

• **Martin JANSSEN:**

Indeed, we should expect people to use their own judgement, even if the rules are not written in black and white. The economy is a complicated matter; business leaders do not know all the risks. However, once the politicians give me the freedom to do something, why would I put other restrictions on myself? That is perhaps the heart of the matter. I understand what you are saying being an entrepreneur myself, but bankers are not really entrepreneurs any longer. Bank directors would behave differently if they had stronger requirements that penalised them harshly and personally if, for example, their institution's capitalisation fell below a certain level. The politicians have not devised these kinds of requirements, so they have led the bankers to act this way.

• **Indira TASAN:**

These CEOs are behaving just like any manager.

• **Andrei ABRAMOV:**

To return to the analogy the Professor Black used, I think the framework remains structured like this: drivers are not told there are pedestrian zones, etc. and go about driving at 40 kilometres per hour. They are not required to take responsibility for the consequences of their mistakes, other people are held accountable for them. Therefore, we have to find the institutional reasons that would motivate people to change their outlook.

Furthermore, because of regulation the system did not allow financial institutions to fail and in turn suffer the consequences of their actions. This reasoning made them unaccountable. Even the financial institutions that acted responsibly were penalised. Thus the big institutions often bought out the smaller ones that were being more cautious. From now on, people in the system have to behave like adults, which implies they take responsibility for their actions and, most importantly, their bad decisions. Until now, bad behaviour has pretty much been rewarded. So the irresponsible behaviour we are seeing should not be surprising.

• William K. BLACK:

No government authority forced an institution into making predatory loans. Even the Bush administration discouraged that type of loan. From a historical standpoint, not all the banks were saved in the savings and loan crisis. Some categories on the bottom of the ladder lost money and others did not.

What are the negative effects of bank regulation on the ability of banks to lend to the private sector? What are the consequences of the Basel III requirements?

Overview of alternative banking instruments not subjected to liquidity problems.

Roundtable speakers:

- Massimo Amato, Associate professor, Department of Policy Analysis and Public Management, Bocconi University, Milan, Italy
- Steve Young, Global Executive Director, Caux Round Table, Saint Paul, United States

I. Toward a healthier and thereby simpler financial system

• Steve YOUNG:

I am delighted to be here with you to share my thoughts, the first of which is about the need to subdivide all the entities that are currently too big to fail. For all of you who are not pleased with Basel III and do not trust regulators or the 29 institutions that wield power over today's global financial system, I have a solution to offer.

Whenever there is a concentration of power, systemic risk increases. Borrowers who are more wary tend to rely on their savings, exchanges are made in the old-boy network and volatility becomes strong. In late 2012, the liabilities of the four largest banks in the United States equalled 47% of American GDP. Twenty-nine companies were considered significant for the global financial future. What can we say about an industry ruled by a handful of actors? When the concentration is too strong, the temptation to cook up illicit deals becomes big. The megabanks hold 69% of the assets in the United States, community banks have 12% and medium-size banks even less. Countries, meanwhile, which create jobs and need capital, usually go to community banks or medium-size banks. In terms of GDP, the liabilities are 6.5% at JP Morgan, which has 5,800 subsidiaries much like its major competitors. The over-concentration is obvious and the government is virtually forced to intervene when one of these institutions fails. I was impressed by Alan Greenspan and his mea culpa after the crisis when he said, "We made our regulatory choices based on the concept that everyone working on Wall Street is very shrewd. They graduated from Harvard, Wharton School of Economics, they're reputable mathematicians. But since we can't predict how many mistakes a certain group will make, the only stamp we have is capital. So we are going to strengthen our requirements in relation to the capital." To my mind, this reasoning is shallow and lacking.

How can we protect the market, borrowers and taxpayers from systemic risk? The best solution is to diversify. But that is not enough because we then have to create reserves, take out insurance, set up a prudential management process. Yet, for years efforts to prepare for risk have never solely focused on diversification. The current proposal being put forth by the Chairman of the Federal Reserve of Dallas, Richard Fisher, is admittedly a bit vague and could be more coherent, but it is definitely a new approach in terms of the ideas it conveys. While waiting for this idea or different suggestions to be acted upon, our assets are being poorly evaluated and anxiety is the norm. We have to accept the fact that intermediation carries inherent risk. We borrow short term to refinance long term and have been doing so since the Roman

Empire. And we must understand that it is a complicated situation where every financial department has its own risk profile.

Requirements on capital and reserves were set up to pre-empt risks –the private risks of funds deposited by lenders and public risks related to liquidities and corporate funding. What ways could we devise to deal with this situation?

II. The experimental clearing house

• Massimo AMATO:

One approach to study is creating a compensation system. I have personally worked on developing an experimental clearing house with the city of Nantes. This actually involves designing financial instruments independent of constraints generated by liquidity problems. The clearing house that we devised for Nantes is completely independent of liquidities. It is based on another concept, the notion of bartering. How does the clearing house work?

The clearing house records the debts and credits of companies trading with each other in the Nantes area for the business they conduct in that region. It does not have access to all forms of trade, but it can accurately handle this portion of trade that occurs locally. In effect, this trade does not require a global currency. It only uses local accounting units that can be converted into euros but are recorded as such in terms of purchases and sales. The clearing house does not grant rights to credit that can be paid in euros but, conversely, in merchandise. A company located in Nantes will be registered as a customer and a vendor and tries to balance out its lending and borrowing accounts as much as possible.

Occasionally, it may be able to finance its working capital without going through liquidity markets. So it does not dip into its cash reserves and no longer has to go looking for a bank loan. It can also pay part of its wages in local currency. Some of this money can be spent by employees in its organisation. Participating companies also grant themselves loans to help with trade and receive more support from the clearing house.

With this clearing house we are upholding the liquidity concept as merchandise to buy and sell without having any maintenance costs or nominal loss. For five years now the clearing house's assets have been increasing and the currency has not been spent. We could also imagine the currency not as a reserve value that can be hoarded indefinitely, but as this tool that can help strike a trade balance in real terms. This currency should only be a reliable accounting unit and a method of trade.

In a clearing house, this currency is created by the trade itself but it is also destroyed once a company sells without buying anything. It is oriented toward bringing about a macroeconomic balance that is also compatible with that of all the participants. In 1944, the International Clearing Union of Keynes in Bretton Woods used the same concept for everything from global commerce to local trade.

There were already problems with structural imbalances between countries in the euro zone among the founding members of the EEC from 1950 to 1958. There was already an idea that multilateral cooperation among European countries allowed them to withstand the lack of liquidity that was hindering growth in their economies.

We are also making this proposal at the local level because we believe the purpose is not really to find out “what will save the system” but to make this rescue possible collectively and cooperatively.

• **Indira** TASAN:

If I understood correctly, you are proposing a revolutionary idea! In that system there are no bankers. Your proposal will have monumental implications in that it implies breaking up the banks. I understand people thought the solution is to eliminate these huge banking institutions. It is an ambitious, compelling and inspirational idea... But there is a “dark side.” What would happen if one of the participants decided to stop playing the game, to block the currency and no longer honour the price agreement?

• **Massimo** AMATO:

Once the big banks are broken up, we could endure several failures. The issue of systemic banks that cannot fail would become obsolete. When there are many participants and one disappears, it does not create ripples at the systemic level. Increasing the number of players also creates more competition according to a principle dear to Adam Smith: the more players there are, the more innovation there will be.

A friend of mine recently told me it would be better to let JP Morgan be bought out by an even bigger giant, like Google, even if the bigger one had no experience in banking and could turn it into something completely different or use the opportunity to reinvent the bank.

All the same, my vision is more rational. Bankers tomorrow will be the same as bankers today. Harvard graduates will continue to make mistakes and will have to suffer the consequences. I would perhaps not be so calm if I had entrusted my money to one of the banks that failed. In our system, in any case, the deposit guarantee covers anyone who follows the rules and stays below the US$25,000 limit. On the other hand, for people who prefer hedge funds and are speculative by nature, I can only wish them lots of luck.

• Jacques POTDEVIN:

Thank you for that interesting suggestion. It reminds me of a bygone system called the bill of exchange. You are reinventing it at the local level now by paying against a draft drawn from a supplier. But it begs the following question: what do you do if a large originator suddenly cannot pay their bills and starts a chain reaction? What insurances have you built into the system?

The "endorsement" was invented for the bill of exchange system where every endorsed draft could be passed between hands hundreds of times in absolute confidence since its security was guaranteed from the beginning.

• Massimo AMATO:

Thank you for that question. You remind us of the bill of change system and, by association, of Lyon, which managed commercial trading in Europe from 1542 to 1575. It is the oldest private monetary system in Western history, which managed European barter trading every three months without liquidities.

In order to construct a chain that is not weakened when links are removed, you have to create a circuit where every participant is allowed into the system in proportion to their ability to balance out their purchases and sales and setting interest rates accordingly using Keynes rules for his International Clearing Union.

The endorsement was rarely used in Lyon. A good market economy should champion the option to fail because those who are able to remove themselves from this danger are essentially contaminating the system. Our solution is to use local currency to set up a fund to cover liabilities. A percentage of the bank's commission on every exchange is set aside in a guarantee fund. If a failure occurs, the loss is pooled and covered by the fund.

It is not a matter of hoarding. Other barter systems were developed in Europe as well, including ones designed through private initiatives. In those systems every business had to put a portion of their goods into a collective store as collateral.

I will add that you cannot display two prices, one in euros and one in the local currency, which we sometimes call "cash currency." The exchange rate is 1:1, so there are no hidden fees. As for the banks, they are still playing their role to the fullest handling specialised medium- and long-term investments.

• Indira TASAN:

This brings us to the question of green-fencing.

• Massimo AMATO:

That is a general and exploratory concept. The guidelines for dividing up the institutions will then have to be determined, for example by line of business (trading, commercial bank, asset management, etc.) to be used to split them up, etc.

Next, how do we prevent them "re-concentrating" when there is a natural tendency to amass and increase in strength? We could come up with a tax or warnings from the regulator based on a given fee scale.

The market capitalisation for all the big American companies is lower than their headcount. They are no longer the stock market "stars" – bonuses and wages are automatically lower and some have to forego a standard of living they were accustomed to. A possible solution to this would be to institute a kind of annuity collection. If we can generate real competition, the industry will be a more modest size and the funds freed up will be diverted to green energy, for example.

• **Participant:**

Hello, I am from London. How can regulations incentivise banks to grant more loans to SMEs, which are the largest job creators nationwide.

An English poet, William Butler Yeats, wrote that «too long a sacrifice can make a stone of the heart.» Some SMEs in Spain generate 60% of the jobs in a country where the unemployment rate among youths under the age of 25 has reached 50%. How do you strike a better balance between austerity and growth? How can we increase flexibility? Is there a difference between southern and northern Europe? Spanish SMEs have to pay much higher interest rates when they borrow money than in Germany. Cultural and social differences also play a role as they affect how every population perceives and experiences problems that can be compared objectively.

• **Massimo AMATO:**

In Italy's case, SMEs no longer have access to credit and that will soon happen in France. A member of the Italian business confederation recently pointed out the large number of businesses filing for bankruptcy, not because of a lack of orders but because they had no cash to continue doing business. Mario Draghi's policy is mostly to blame for this. By providing the banking system with the €1,000 billion, he hoped to help small and medium-size businesses but nothing came of it.

Therefore, it is wise to find cooperative funding methods between these SMEs at the regional level from a fraternal perspective.

The Target II clearing house, which is designed to settle cross-border payments in Europe, was breakeven until 2007 recording debts and credits. All the countries were also at breakeven at the time.

I do not know if we can play the cultural difference card. Do we want the countries to actually hold on as a group? The wealth accumulated by the northern countries is not solely the result of better productivity; it also comes from speculation and, more specifically, the flight of capital. So the euro means something different in every country; whereas the German interbank market was up, the southern countries have no business activity. This state of affairs is normal and healthy as well because not all the countries can have the same level of commercial activity.

The countries that are doing well can count themselves lucky because they have not only managed to sell but sold more than they had hoped. A clearing house could work very well today according to Keynes' International Clearing Union rules. The Chinese bank governor recently asserted that his country was wrong in 1944 not to follow Keynes' recommendation to set up a national currency alongside the global currency.

• **Indira TASAN:**

I am very disheartened to see that at the end of a day dedicated almost entirely to examining our problems, we can spend so little time finding solutions. I am making a wish that we can return to this vital discussion next year.

• **Steve YOUNG:**

I spent many years working for minorities and SMEs in Saint Paul. When immigrant groups arrived at Deux-Phares, we could rely on character build, which was reliable and much more informative than collateral, financial checks and forms. The requirement today is to put an extremely sophisticated procedure in place at every level of the banking system. As a result, a great number of people are being excluded. Banking groups using the credit union model can overcome this barrier, not only by giving financial loans to individuals but also by doing it in a community spirit without «branding» people affected by accidents.

Friday, April 26th

Association Day

The impact of regulatory initiatives on the distribution of investment products & services.

Roundtable speakers:
- Vincent J. Derudder, Chairman, FECIF, Brussels, Belgium
- David Charlet, Chairman, ANACOFI, Paris, France

• Vincent DERUDDER:

The goal this morning is to explain to you how associations, companies and various trade groups are reacting to the changes caused by the crisis. As chairman of FECIF, which has 200,000 members in Europe, I am going to focus on describing EU intermediation.

We represent about 500,000 people in the intermediation sector, which includes agents, brokers and advisors. We lost 150,000 to 200,000 jobs after some of the French financial intermediaries disappeared. FECIF truly represents the industry since approximately 40% of people in the intermediation profession are members. Thirty-one percent of FECIF's members are captive agents who only work for one bank or insurance company. The other members are multi-captive agents, brokers or independent advisors.

FECIF's intermediary members also account for over 50% of the savings invested in northern Europe. This figure is slightly lower in the rest of Europe. France has fewer intermediaries than other countries. It essentially has a smaller number of banks, which includes La Poste that also collects funds. Talks are under way in Brussels about possible conflicts of interest in paying intermediaries in the savings account case. Intermediaries are basically in favour of regular fees, which does not work when a small percentage of the others are working for one-off fees. Some payment systems, for that matter, can be counter-productive. For example, intermediaries can be required to invoice for VAT, which is about 20% more and customers cannot deduct it.

Mr. Barnier is speaking for consumers, but no one knows them better than intermediaries. In a surprising way, the average customer's main concern is keeping what they have. Passing it on to their children or spouse is one of the other top reasons people invest. Regulations should take these factors into consideration instead of compensation for intermediaries, which does not interest the average customer. These facts come from a PwC study commissioned by the European Commission, which essentially wanted to conduct a study before opening talks. However, it did not see the report as positive and the Commission did not use it.

People in charge of regulations are not familiar with our business. Like in many countries and sectors, bureaucrats have their own view of society and, just like priests, keep repeating the same sermon. Removed from the real world, they only have a limited understanding of intermediation and what customers want. In particular, the authorities think that only a handful of financial conglomerates need to be regulated, which does not reflect what consumers want. The regulators are persuaded that our business is not fair, that we all represent some odd conflicts of interest and we are only looking to make higher profits, which is sometimes true. Intermediaries, on the other hand only have one thing in mind: their relationships with their customers. If an intermediary does not give the customer what he wants, they will go elsewhere. This compulsion is why intermediaries are well behaved around their customers.

The high level of knowledge intermediaries have about the markets, and the fiscal and legal environment, has also greatly improved over the last 10-20 years. Intermediaries today are indeed better educated and highly skilled in their field. The lack of training and professionalism is a thing of the past. Furthermore, it is tricky to monitor intermediaries because they evolve within small entities.

While some are implicated in various scandals and scams, the statistics show that very few complaints are filed with the regulatory authorities. Not to mention that the typical criticisms aimed at people in the financial sector are not true when it comes to intermediaries.

The cost of regulations is constantly rising. Intermediaries spend half of their time completing bureaucratic tasks like reporting. There are also very strict anti-money laundering requirements. IT companies were also able to take advantage of the situation by developing software programs to handle the regulatory requirements. What is more, the added administrative costs are passed on to the consumer. We are fighting alongside other associations across Europe to reduce these administrative processing fees. There was an important discussion about which information to give consumers. We would like it to be adequate, for example something like a one-pager containing the key components. It is still difficult to make the regulatory authorities hear this message.

Lastly, the environment we are progressing in is becoming increasingly bureaucratic. Unemployment is also rising in France and Italy. And the weight of the government's control over the economy is burdensome and counter-productive. I do not believe the crisis was caused by the spread of bad loans or the actions of a few traders who were gambling, but rather the enormous deficits of our governments that have been rising for 50 years.

• **David CHARLET:**

I am going to attempt to explain the current situation and how the directives we follow were constructed. Directives cannot be passed without the approval of the Council and the Parliament, which do not have a shuttle system like the French parliaments. European directives come about after a long trilogue process.

The ruling on the draft MiFID directive should have been issued tow or three years ago but is constantly being put off until the next month. This directive will have a very significant impact on our profession.

The UCITS V directive is also in the preparatory stages and will be immediately followed by the UCITS VI directive. Yet we still do not know what the UCITS V directive contains.

Incidentally, the IMD II directive cannot happen until the MiFID II directive is passed.

The PRIPs directive's objective was to simplify the documents we give our customers. Some products can be explained in two pages, but not all of them. Furthermore, some insurance policies contain underlying products that also have to have their own documentation, which makes the process complicated.

Lastly, it has been said that the talks about the mortgage directive would come to an end. In particular, the Irish announced they would not step down from the EU presidency until a decision has been made on this directive. This directive involves independent advisors and their compensation and, as such, is expected to be aligned with the MiFID and IMD directives.

MiFID II Rapporteur Ferber is striving to maintain a balanced system. The British representatives in the talks suggested that Europe needs to do what the United Kingdom did. We will soon know whether this is a positive development. The points of contention on the directive have little to do with advising and more to do with market organisation. The mortgage directive also seems to have more advisory-related content and is therefore looking like an opportunity for us.

Clarifications and explanations will be available in October. A trilogue will take place after a preliminary ruling by Parliament. It can only be transposed to national law in late 2014 at the earliest, even though the legislation has been expected since 2011. However, it has been confirmed that the UCITS V directive will be debated in May. The directive's rapporteur is a member of the Green Party, which does not share our concerns. There will also be a debate in July on the IEFM directive, which should clarify the rules for portfolios not covered by the UCITS V directive and are not regulated at the European level right now. IMD II is an important directive but a decision cannot be made on it until the MiFID directive or the mortgage directive is passed. IMD directive Rapporteur Langen has taken an aggressive stance. Going against the positions of the Green Party and the British, his standpoint may make it possible to consider our viewpoint. Lastly, the PRIPs directive will be debated in May in ECON. But we do not know when the vote will take place.

Without directly relating to our day-to-day jobs, some other directives will most likely affect our business. For example, the directive on the qualification level for specialists in regulate professions that is currently being discussed.

• **Vincent DERUDDER:**

In 2012, various European bodies issued 756,000 pages of documents. Over 600 amendments were proposed for the MiFID directive. The European Parliament is a perfect example of a bureaucracy where the Socialists and the Greens propose purely politically-driven amendments. The parties on the right are developing amendments that go in the opposite direction. Compromises between these stances are political and hardly relevant to the day-to-day lives of bankers and life insurance companies.

Crowdfunding and computerization of the banking applications,
by Daniel Nicolaes, President, BZB

The future of banking services will be mobile. Banks have invested US$10 trillion in their own bailout. This colossal figure is equal to the cost of World War II, the Gulf War, a lunar mission and the damages of the Japanese tsunami combined.

ATMs multiplied. Then computers helped simplify our daily lives and make us more mobile. Now we can do our banking on smartphones.

In an effort to prevent fraud, a cap has been placed on cash transactions of €5,000 and will be lowered to €3,000 next year. In addition, 70% of purchases will be made online and this could pose a threat to financial intermediaries. They should be revising their business model and seeking new directions. Although personal advising will still be necessary, consumers may not be prepared to pay for those services.

The American report Intuit 2020 raised some questions about how consumers are changing and adjusting the offer for this change. Brett King's book "Bank 3.0" says that banks are no longer places where people go. 300 million people have an Apple account. This is more than the total number of people enrolled at the three biggest American banks.

Everything is going mobile. Over 50% of traffic on Facebook comes from mobile devices (telephones or laptops). The rise of PayPal has made payment cards like American Express and Visa obsolete. Money is becoming virtual, for example, with the expansion of virtual currency on social networks.

Crowd-investing systems are also being developed. In these complex financial times, it can be hard to obtain a loan to fund a project. But it is possible to gather together many small amounts, for example by calling out to a group of friends on social networks and collecting the desired sum. Crowdfunding can be modelled as pre-sales, donations, rewards and loans. With presales, you know how much money is collected in advance and how much to manufacture. Loans can be social loans or P2B loans. Asset crowdfunding can be the outcome of a business angel's initiative. It entails profit sharing based on future profits. While Europe is still slowly moving in this direction, crowdfunding is quite developed in the United States. Since a Europe-wide regulatory and legal framework has not been defined, national interpretations dominate the landscape. Crowdfunding benefits the economy because it injects money back into the system thereby helping shift the risk from the bank to the individual.

So, these new funding methods do not pose a threat to banks, but rather to financial intermediaries.

Intermediaries enter into a long-term relationship with the consumer and view crowdfunding as an opportunity.

The point of view of the life insurance companies, by Alan Morgan Moodie, CEO, Association of International Life Offices (AILO)

This is my first time attending a CIFA meeting and I am delighted to be here. I would like to tell you about us and what we do on behalf of our members.

The association was founded in 1987 and represents some 50 companies working in various financial centres. We currently operate much like a lobbying firm where we work to represent our members at every level throughout the world. Our members manage a total of about €220 billion. We attempt to guide and monitor the amount of regulation. We also hold forums where our members can exchange ideas. We also advise on and support European educational programmes involved in training intermediaries. We operate through working groups and subcommittees tasked with addressing a variety of issues. Some committees deal with specific geographic areas, like Germany or Italy. Employees from member firms sit on the committees and working groups. So we have a number of experts at our disposal.

Work on the European directive on savings began in 2010. At the time, the conclusion was the directive would stop the generation of expected tax revenue. Luxembourg and Austria have only just changed their positions after having been obstructive, notably on the issue of confidentiality.

Our concern about MiFID II is that intermediaries who offer a range of products would be affected by the ban on commissions. This problem was submitted to the rapporteur. In 2008, Finland completely banned commissions and this resulted in a dramatic drop in the number of independent advising firms. It killed the intermediary market. Fortunately, Rapporteur Langen does not see commissions in a negative light and reiterated his favourable view at the last ECON meeting.

The IMD and PRIPs directives appear to be designed to cover all types of life insurance except death insurance. The PRIPs directive is expected to take on a new approach to insurance, which is a long-term agreement that only the policyholder can break. However, you can buy and resell an investment firm without signing a contract. Therefore, we would like insurance to be qualified as something different than ordinary PRIPs. In addition, we need to be able to explain why our products are more costly and why insurance can seem like a better solution than other types of investments.

Europe is making no headway in protecting policyholders. The various initiatives on this issue have died in the water. The Omnibus II directive, the forerunner of Solvency II, does not make it possible to measure guarantees over time and their underlying assets. Cross-border insurers will have to tackle a different method of analysis for 10-year assets, which will contribute to ending the single life insurance market. What is more, the fallout from the ban on commission payments is hindering the expansion of the single market. For example, there will be no reason for a Polish intermediary to sell the products of a company based on Luxembourg wishing to sell in Poland because he will not be paid. So the company will have to set up its own location and fill it with captive agents, which is extremely expensive. Brussels is no longer prioritising a single market. The Irish presidency, for that matter, has not scheduled any meetings on PRIPs or IMD.

We also have to deal with the FATCA directive, which mandates complete transparency and full disclosure. The United Kingdom pointed out the fact that the directive would not address taxation, which is already governed by several mechanisms. FATCA's objective is to find out what people own and where their assets are held. President Hollande in France has asked his Socialist ministers, who are nonetheless millionaires, to disclose their assets.

We are advocating for the cross-border industry, which has excellent products developed for sophisticated markets and should see growth. All of the governments will have declared bankruptcy by 2050. Social programmes and social security will have disappeared. This means people must save money and plan for their own retirement. Therefore, it would be wise to encourage savings instead of taxing it.

The point of view of the consumer, by Guillaume Prache, FINUSE

The regulator can address the issue in two ways. First, it could use the American approach and see the consumer as an ordinary human being with a brain who is able to make decisions. The European approach, on the other hand, assumes consumers are stupid and do not know what they are doing, which means civil servants have to help them make decisions. This approach also implies that by definition financial intermediaries are thieves and need to be closely regulated. These approaches impact the economy differently in times of financial crisis.

What do consumers think about all the regulations that are supposed to protect them? Most likely, regulators do not want to know the answer to that question. Investors want to operate in a stable environment where the law prevails and there are clear indications on the future. It is complicated to plan for the future in countries where the tax system changes several times a year. Thus, consumer protection begins with creating a stable economic environment. The sovereign debts of nations can be compared to toxic loans whose value has mostly declined. Today, one euro of France's sovereign debt is worth 50 centimes. Yet the entire pension system relies on sovereign debt. Unfortunately, the regulator refuses to come to grips with such matters.

• Vincent DERUDDER:

The PRIPs directive was a response to a European Commission's initiative dating back to 2006 or 2007 designed to ensure the products being sold were easy to understand for the average consumer. It is true that some agents led consumers astray and scandals broke out. With regard to complex instruments, the consumer had to be educated on how the various components fit together.

The MiFID directive worked well for investment services. At the time, Commissioner Bolkestein took a pragmatic approach to restructure financial services in Europe through six directives. Right now, there are nearly 100 directives governing financial services, which is ridiculous. We are mostly referring to MiFID II here but the first directive, MiFID, has not been fully implemented in all the 27 Member States.

The IMD II directive had a similar experience to MiFID II where it is being mentioned even though its first version has not been applied throughout the EU yet. The IMD II directive deals with insurance-related mediation and aims to regulate the distribution of insurance products and services. Life insurance is a very specific product that cannot be treated the same way as car insurance. Yet, the IMD II directive wants to address both topics.

• Jean-Pierre DISERENS:

We have a powerful lobby in Brussels that asks the right questions at the right time. Our future would be in jeopardy if the lobby were not protecting financial intermediaries. So I invite the attendees to become corporate or individual members of FECIF to support the lobbying efforts at the European level.

CIFA is using a top-down approach and working with the United Nations in its attempt to fight the senseless European regulations. More and more countries are voicing their support for the *Charter of Investors' Rights*, which will soon be ratified. The charter is designed to ensure everyone is free to honestly dispose of the money they make and invest it as they wish.
Once again, I urge you to give your support to FECIF to save the financial intermediary profession.

The future of intermediaries, by Michael Lodhi, CEO, Spectrum (intermediary firm).

I am going to provide you the perspective of an independent financial advisor. I believe I am the first independent advisor to speak this week, which is interesting.

Consumers need independent advising. And this need is patently obvious in our current financial environment. I am concerned about the future of my small company and the futures of my colleagues and customers. In times of sluggish growth, SMEs play an important role.

Do the regulators and politicians understand what we do? Vincent Derudder and I met with a member of the ECON committee, who immediately likened us to Lehman Brothers agents. The MiFID directive basically cites high-frequency trading and I am not sure the European regulators comprehend the significance of our contribution.

Life is getting longer. Savings is thus a key element and intermediaries can provide consumers retirement plans. Consumers are not very proactive in that area. Incidentally, I think retirement plans should be made compulsory just like car insurance. Brussels is talking about educating the public about financial matters, which is not very realistic. Why not also teach medicine and law in schools?

Advisors must make their customers more involved, primarily by educating them. I like to give my customers a free trial of my services because it is also a chance for me to get to know them and understand what they want. I can do this by not charging them fees. The initial interview does not cost me anything but time. I then just have to explain to the customer that they will be billed for fees if they want further services. Invoicing fees from the first meeting restricts the consumer's freedom of choice.

Right now, British banks are pulling out of the advising market. Product providers will be looking for new distribution channels and will not hesitate to go to Asia if Europe closes its doors to them. The least regulated countries are basically the most conducive for business. A shift like this would reduce the number of new intermediaries. Yet, consumers need us because we provide them proactive representation. As independent advisors, we have to work on improving advising standards and that will help attract the public's attention. ANACOFI and FECIF are lobbying for this and CIFA also supports it. We must support these organisations if we want a brighter future.

• Vincent DERUDDER:

I suggest we open a question and answer session.

• Participant:

I am a financial advisor from Australia and came here to learn about the situation in Europe. It is very similar to the situation in Australia where independent advisors are being excluded and large advising firms are growing thereby punishing consumers. It is the same problem around the world; regulators have too much power.

• Vincent DERUDDER:

You are undoubtedly right. European politicians want to force their world vision on everyone.

• Participant:

As the head of a French association, every quarter I receive some 500 pages of documents in English. We have to make the regulator aware of our services so they can become more familiar with our profession. Our lobbying efforts should focus on asking the regulator to try our services out for free.

• **Michaël LODHI:**

We contacted a club of retired European bureaucrats to offer them our financial services. That was a starting point. Bureaucrats in Brussels have a nice life, do not pay taxes and drive company cars. It would be appealing if they were paid with performance-based bonuses.

• **Participant:**

I represent the Canadian Institute of Financial Planning. I do not understand why, but Canada passed a ban on commissions. The free market should allow a variety of models to exist and give the best model a chance to prevail. Banning commissions will have unintended consequences, like making huge advising companies to become even bigger.

• **Vincent DERUDDER:**

You are talking about freedom. Some people do not like freedom and want to replace it with government control. We are fighting for freedom, but 25,000 people who are installed in Brussels and paid with our money are against this freedom. They also think we are idiots.

• **Participant:**

I am CEO of a small independent financial consulting firm in the United Kingdom and have not been able to collect commissions since last 1 January. So, we only receive fees and it is all for the better. Ending commissions has also helped clarify and improve transparency in the system. For that matter, we have not suffered any unintended consequences. A world without commissions is possible.

• Vincent DERUDDER:

The British market is highly sophisticated, so banning commissions can work there. But a ban like that could not work in Croatia, Poland, Germany or Italy. The Finnish model would make financial intermediaries extinct.

We endorse transparency and explain our payment scheme to our customers to leave room for negotiation, open a dialogue and then reach an agreement. In this way, the customer relationship is based on transparency and openness.

• Participant:

Commissions in the United Kingdom can be illicitly tacked on to the fees. I am equally concerned about the issue of capitalisation brought up by British regulators. Capitalisation would form a monopoly of captive agents.

• Participant:

Consumers should be given a choice between a range of approaches. We must be able to use a variety of products to attract customers.

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by Gilles Duteil, Director of CETFI, Aix-Marseille Université, Aix-en-Provence, France

As an adolescent, I was very impressed by an advert in a free paper by someone saying he had a foolproof way to kill roaches if you sent him a cheque for 100 francs. People who responded to the ad received an envelope with a little plastic hammer and a manual that said, "To kill roaches, aim for the head and hit them hard." The person who placed the advert was exonerated of fraud charges since there was no real fraud. The operating procedure provided was indeed effective, but demanded a degree of patience. Since then, swindles have become more advanced and they now rely on systems structured like pyramids.

Ponzi schemes are a marketing tool for spreading fraud. The swindler is looking to make a lot of money as fast as possible. Carlo Ponzi would offer investors high-yield investments using one-cent stamps that he agreed to buy back one or two years later for six cents. Communications in Ponzi's era were still not very advanced and swindles spread by word of mouth. Between 90% and 95% of people are captivated by easy money, a fact reflected by games like the Lottery and Euro Million. High-yield investments are always quite popular.

The Ponzi formula was more like a snowball than a pyramid. His system was to rob Peter to pay Paul while he played with the investors' money. Investors initially see a chance to make a very high-yield investment as a possible scam. But level-headed investors can be prepared to take the risk if given an opportunity to make a big profit. So investors are left to choose one of the options, for example by telling themselves, “Let’s try, just to see what happens” and giving Ponzi €10,000. Since Ponzi could not just pocket the money, he tries to make his future victim believe that his system works. Three months later, he shows up at the victim’s home to deliver the first quarterly interest payment. So the investor thinks the system is working and that it is not a swindle. But Ponzi only returned some of the investor’s original money. Three months later, the investor receives the second quarterly payment thereby confirming to him it is a very good investment.

The victim quickly contacts his friends and family to tell them about the investment he made. Victims typically introduced Ponzi to between three and seven new victims. Not to mention, the victim is pleased with his investment and invests even more money. The swindler experiments with redistributing some of this money to attract even more victims. This exponential growth, at a rate of three to seven times, provides the swindler several hundred victims.

Thus, the money is never invested and the swindler spends it as he goes. When a financial crisis hits and credit is shrinking, households tend to draw on their savings. So people began asking Ponzi to return the money they had invested. Since the money had been spent, the swindler has to find new victims to pay the old ones.

Since the 1990s, I have been fighting this largely identified phenomenon. I would like to thank Bernie Madoff for making the whole world aware of these schemes. But Bernie Madoff’s swindling did not put an end to Ponzi schemes, as was proven by the

Dumontier and Wilmaers cases. The Ponzi system relies on spontaneity and making yourself believe the system works.

The pyramid scheme is used for similar purposes, but it operates much differently than the Ponzi snowball. In pyramids, new investors have to pay an entry fee and bring in two new victims. In the 1980s, there were almost more pyramids in Delaware than people. Pyramids are well-built hierarchical structures that require new members to fulfil a contract before they leave. This contract usually involves bringing in new victims who also have to bring in new victims.

Swindlers are very reactive to the atmosphere and the economy. All of the swindles that I have studied for the courts involved a professional, such as an asset manager, advisor, financial expert, banker, attorney or legal notary. These people typically let themselves be persuaded by the swindler, sometimes by means of a small commission, which makes the scheme credible.

Swindling is based on the concept of outsized returns. In the early 1990s, 80-100% involved outsized returns. These days, a guaranteed rate of 5% over several years is outsized. A state-issued French bond is at about 1.75%. Today I learned about a fraud case where the swindler was offering a 20% return rate, which is absolutely insane in these times. So I ask that you learn how to recognise the irregularities associated with fraudulent schemes, the first of which is the return rate offered.

The person offering the product is usually the second irregularity. They will tell you about banks you have never heard of, like the "Carson Banc" registered in the Dominion of Melchizedek, which does not exist and whose name sounds suspiciously close to Carson

Bank. According to American sources, this Dominion has created about 300 fake banks. These banks were widely spread throughout the world and in court I have personally handled four cases involving fake banks in the Dominion of Melchizedek. A foreign bank must have a certificate from its own country that is then sent to the country where it conducts business. So you can go to the *Autorité de contrôle prudentiel* (ACP) and find an updated list of all the banking licences authorised in France.

In 1989, there was a credit crush that severely tightened access to credit. People began to dip into their savings and this worried swindlers. Using the same mode of operation, swindlers then invented international funding. Plus, in order to avoid the legal consequences, they typically refer to it as an international funding instrument instead of a loan. They ask their victims to purchase an arcane "standby letter of credit" that will be entrusted to a "master." According to the swindler, the master goes to a special market where he does buys and trades that can bring in 1-5% per trade and there are several trades per day. The swindler then explains to the victim that intermediaries are greedy and have to be paid before the loan can be obtained three to six months later. The «deposit» will be 10-15% of the loan amount. Some swindlers have gone so far as to dream up «self-liquidating loans» where the standby letter of credit continues to be traded on the private market and will thus pay off the debt itself. In various studies, we have estimated that these swindles were worth about US$10 million per day in the early 1990s through 2002-2003.

The Madoff fund started out as legal. Bernie Madoff was also Chairman of NASDAQ, so he was larger than life and investors trusted him. People were also prepared to beg to get into these instruments.

There are specific arguments that all swindlers use. They usually claim that the banks have control of the set-ups. They add that the systems are highly confidential and they should not talk about them. Some say only the investment is reserved for a few insiders, which makes the victim think he is part of a special club. The swindlers have a sense of irony and sometimes ask the victim to certify in writing that the funds they are contributing come from legal sources. The swindler also often says it is a very profitable risk-free investment, which is completely antithetical to modern financial theory. He typically says the deal is available immediately if the victim has the money ready. The swindler may also claim that there are no fees for the investment or the loan is non-amortising. That is the moment when the dream hatches and the prospect becomes a potential victim.

In my first few cases, I attributed the victims' willingness to believe to human stupidity, the likes of which I had never seen before. Little by little, case after case, I began changing my opinion. The goal of swindlers is to make their victims long for what he is offering. This kind of longing can put the victim in a dream state, similar to someone who spends a few euros playing the lottery and dreams of winning. People already see themselves as the winner, they dream about their new life and start making plans. This lure of profit exists in all the socio-professional categories, so they are all susceptible to potential scams.

Swindlers have a range of victims in their line of fire, like investors looking for new opportunities or people and businesses that need a loan, usually aided by innocent victims, believers or fools. There was a time when swindlers focused on football players because they were an easy target. They also targeted heads of ailing businesses who have a certain affection for their company and cannot get money from bankers because of their poor financial standing. The swindler often seems like a saviour to vulnerable people.

Swindlers usually ask that the money to be wired to foreign countries. Placing it overseas essentially makes litigation more complicated because it requires mutual aid and often an international commission to take evidence, some of which are only implemented two years after the fact. The first wire transfer is usually done to a reputable country, but then the money is immediately sent to places offshore with tight banking secrecy.

The criminal justice system treats violent crime and financial fraud in completely different ways. Victims do not ask for violent crime, but financial wrongdoing implies the victim made a request or even a petition.

To make themselves more credible, swindlers create offshore companies with names that sound like real banks. For example, I have seen "Barclays Credit and Loan." Some swindlers also use the names of existing banks or insurance companies and names of actual employees who have nothing to do with the scam. Others go so far as to use the letterhead of large banks. In the 1980s, this meant they had to pilfer pages of letterhead from the bank.

While the set-ups usually have flaws that are easily identifiable, some swindlers use arguments that are so complex that even an economist may have trouble detecting any trickery. Sometimes the victims want their banker to look over the deal and ask him to attend a meeting with the swindler. The banker does not usually understand anything that is said, but instead of admitting he does not understand it he tells his customer he had heard about the product adding that it is illegal in France. The customer signs the papers the next day.

Swindlers frequently use the services of accounting experts who know the ailing companies and help the swindler find the right clientele. One French swindler, in particular, had an attorney deposit cheques, which made him look more legitimate to the customer. On the lookout for anything that may make them more credible, swindlers also use politicians and legal notaries.

When fighting financial wrongdoing, you have to know the basic fraudulent instruments and always be on alert. It is important to disseminate information to your clientele. Yet, they still may not believe you. In this case, you can avoid civil lawsuits against you for failure to advise by sending a registered letter. Information networks should also be created between professionals. Without necessarily saying that someone is a swindler, it is important to share information about a suspicious person or investment. For instance, many times the AMF (French financial market authority) has had to warn various professions about the dubious nature of some products. You can also report a case to the authorities. The AMF has a special office that is increasingly effective and can answer your questions, which is also true for the ACP (prudential control authority). In addition, you are required to report suspicions to the CRFs (advice and financial risks). It is indeed best to discourage swindlers by making it difficult for them to run their scam. Lastly, when you receive a subpoena, you should facilitate the legal process by responding quickly, for example. You cannot hide behind professional secrecy with the criminal judge. However, you should still find out the legal context of the investigation.

In your honour, I have written a collection of warning signs found in fraudulent contracts, which I will give to CIFA. It will be available on the CIFA website.

To give you an example of a warning sign, scams usually contain a «letter of intent» saying the victim states he wishes to join the scam. I have also seen many times that scams stipulate the term of the instrument as a certain number of years plus one day, for example "five years and one day." While questioning someone in custody, I discovered that this extra day places the deal off the books. Another warning sign is a spelling error in "*uniform customs and practice*" of the International Chamber of Commerce, which is sometimes spelled "*uniform customs and practices*."

Right now, the losses for banks caused by corrupt employees and financial wrongdoing is on the rise and the banking community is starting to feel it. In the recent DO Conseil case, the civil parties and attorneys tried to put the blame on Société Générale for not showing enough vigilance with the pool of capital it received. I am anxiously awaiting the court's ruling.

I invite you to become an active member in the fight against financial wrongdoing by being cautious and vigilant. Do it for your customers. Furthermore, asset managers are usually part of the criminal proceedings, are investigated for organised fraud rings and risk 10 years of prison, a €1 million fine and being permanently banned from the banking profession. It is in everyone's interest for you to know how to detect fraud.

Making the transition to holistic financial planning

by Marty Kurtz, CFP, FPA Chair 2012

RPA is delighted to have become a member of CIFA and sent nine of its members to this forum. Society is undergoing extremely profound changes right now. For instance, in terms of social networks I estimate we are in year five or six of a 30-year trend.

I am an independent financial advisor and am now president of my own company in Illinois. The market makes choices and people gravitate toward products they are comfortable with, so all of the options should be available. In the book "Megatrends" John Naisbitt calls "high tech high touch" a megatrend. Current technological changes are creating a demand for independent and personalised financial advising. Everyone needs a third party to talk to about life and money. And the world is becoming more complex, which makes this personalised advising even more necessary. People have three types of problems: easy problems, complicated problems and complex problems. Personalised advisors help people solve complex problems. Where easy and complicated problems can be solved quickly, complex problems need a third party to listen and motivate.

The way knowledge is treated has also changed. There was a time when we had knowledge that customers did not. Customers paid us to know the answers to their questions. These days, independent financial advisors are teaching customers to live with a degree of uncertainty. We try to improve the customer's decision-making process to improve its effectiveness. Consequently, we have to have an ontological view of our role with our customers and of the meaning of our existence. While this view is needed to ensure the survival of our profession, it was not really mentioned over these last three days. In particular, I attended seminars that were supposed to teach us to gain our customers' trust, which I think is dangerous. Our job is not to gain our customers' trust, but to earn it.

Conclusion

Jean-Pierre DISERENS:

The next CIFA Forum will take place in Monaco on 23 April 2014. We are truly looking forward to seeing you there. I am now going to read the resolutions we wrote after our three working days, which will be submitted to ECOSOC at the United Nations :

"*1. Financial intermediation makes it possible to create and protect wealth and to create institutional public assets that advance human dignity, happiness and wealth preservation.*
2. Financial intermediation makes private capital available to companies working for the public good. This vital resource helps advance science, technology, innovation, culture and the Millennium Goals. The greater the risk taken by intermediation, the more prudential regulation for the public interest is needed.
3. The private interests of customers and their independent financial advisors are aligned with the community's interest. Responsible intermediation conducts a sustainable assessment of assets and prevents volatility, bubbles and collapses in the market.
4. The imbalances of interests and losses brought about by the collapse of the credit market in 2008 were neither compromised nor fully offset by effective prudential countermeasures. There are still instabilities and inconsistencies in the global markets.
5. Innovations in financial intermediation are reducing the size of conglomerates and local clearing houses designed to encourage transactions and create new non-profit ratings agencies."

Contributing partners:

Groupement Suisse des Conseils en Gestion Indépendants (GSCGI), Genève

Association nationale des conseillers financiers, Paris

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