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Financial Reforms: progress or degeneration?

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INTRODUCTION

The aim of this short study is to make an interim assessment of the financial reforms launched after the 2008 crisis. Various measures have been implemented together with many consultations, surveys, impact studies and new regulations. Work has focused on the financial system. This has gone hand in hand with monetary and budgetary policies that were launched to support and consolidate economic activity and to overcome imbalances, causes or effects of the crisis. What is the state of play after so much work and discussion? First and foremost, we note that the intellectual nature and origins of the accounting and prudential measures at the heart of this debate have not been fundamentally challenged. The reforms have been more a response, via the juxtaposition of often pertinent measures, to all of the problems that have been identified. Secondly institutional and political responses have led to increasingly complex all kinds of rules. The question now is: can we say that the result comprises a real improvement to the system?

Our analysis does not provide an extremely positive answer. It raises further constraints. We have seen developments that reveal significant change in the balance of power between various political, economic and administrative players. But this has had but limited effect to date. It seems therefore that for the last five years deadlock has dominated and that in the face of slow developments, instead of enjoying the benefits of real progress, we are witnessing rather more the emergence of a new danger in the degeneration of the Western economic system.

TIME IS MOVING ON

It is five years since Lehman Brothers, one of the five biggest American and world investment banks, went bankrupt. In 2008, two of its counterparts also just escaped that fate and had to be sold off. The bankruptcy of the financial system's elite led the world economy into a crisis of singular violence from which we have still not recovered.

Since then politicians and economic leaders the world over have been working to introduce reforms, which they said were necessary. G20 meetings have succeeded one another. In the US and in Europe politicians have debated proposals. They have approved laws. They have decided upon measures to take. They have talked of issues like transparency, own funds, separation of activities, better regulations, the fight to counter tax havens and regulations, and more recently, the fight to counter the fiscal optimisation of large groups. All of this has given rise to a plethora of names and acronyms defining laws and directives such as the Dodd-Franck Act, FTT, EMIR, AIFM, Basel 3, CRD IV and Solvency II. New structures have been created as in Europe the EBA, ESRB, EIOPA, ESMA, ESM. They cover all financial activities, insurance banks, markets and public finance.

Can we say however that there has been any real progress in terms of organisation or security since the start of the subprime crisis? In other words can we say that collectively professionals in the financial sector now have, in the wake of these reforms, the tools at their disposal for them to respond better to the expectations of their potential, private business clients, both state and private institutions effectively and in reasonable conditions from a cost point of view? And this, in conditions which mean that the risk of further requests for bail-out be greatly reduced? Some promote the real changes that have occurred since these decisions were taken. In support they also invoke the settlement of the acute phases of the crisis, and even the USA's recovery in justification to a positive response. But nothing can be taken for granted.

Dare we even say that the reforms have produced the desired effect whilst they have not yet been implemented or have only be partially put to the test?

Hence in the US nearly three years after its adoption only two thirds of the measures included in the Dodd-Franck Act have been implemented. It has led to interminable discussion. As a comparison, after the implementation of the recommendations put forward in the Larosière Report in Europe, it took the challenge made to the euro and public finances before any real progress was made – at least in terms of Europe wide centralising powers and the creation of intervention capabilities. The euro zone has emerged politically. Its leading institution, the ECB had earned its stripes as a powerful central bank: as a technical platform for financial transfers between countries, it is now the guarantor of last resort in the zone's financial system.

However diagnoses of the causes of the financial crisis were drafted in 2008 and 2009. We should recall, as an illustration, those which received the most media coverage. Hence there was leveraging, shadow banking, the presence of tax and regulation havens, procyclicity created by accounting and prudential standards, the influence of the ratings agencies, the unexpected effects of regulations, which were supposed to generous – like those that encouraged the most fragile categories of the population to take on debt, poorly understood and even flawed mathematical models, greedy behaviour on the part of professionals and even the effects of trade imbalances between major economic zones, not forgetting the burden of public deficits.

As we saw afterwards some of these diagnoses were widely accepted by international structures. They were the base of the developments we have seen. But the return of a certain degree of calm has now witnessed their disappearance in the main from the media radar screen and also political agendas. It has to be said that everything has been done for the situation to return to "business as usual". Bank balances have lightened, especially in Europe, own funds have increased; the lame ducks have been absorbed or liquidated. The bad banks are managing their stocks of toxic assets: everything is fine. Dishonest traders have been punished, a ratings agency is under investigation, the scheming over LIBOR has been sanctioned and somewhat late fines have been set. The volume of shadow banking is levelling off. What more do we want?

PROBLEMS PERSIST

The core of the crisis or rather crises that have succeeded each other since 2007 is the excessive gap between the debt incurred by all types of economic agents and their ability to create wealth. From virtuous debt for investment we have moved over to debt that has substituted revenues to support increasing consumption in economic activities. Depending on the country in hand households, businesses, financial institutions, banks, States, public authorities have all given in to this facility to varying degrees.

It is true that they have been encouraged to do this via the structure of international trade which has facilitated borrowing thanks to the maintenance of low rates and monetary creation, a poor controlled consequence of trade imbalances stabilised by the inappropriate [1] setting of exchange rates. Indeed we should recall [2] that two elements structure world economic activities: international trade and the monetary system. The financial system comes in addition to the first two. It has led both to the generation and management of this debt and also to the development of activities based on what is systematically an asset for those who carry them. Hence excessive debt continues.

Debts, which represent three to five times the GDP of most Western countries, and which were mostly private before the crisis, have now mainly become public in nature. Recovery plans, reduced revenues, and support to struggling banks explain the sharp rise in public debt over the last five years in nearly all countries. Hence in the US – gauged in terms of a percentage of the GDP, debt totals 350%. Whilst business debts remain stable, those of banks and households are decreasing, but the federal state's debt has more than doubled.

The financial constraint linked to this debt cannot always be borne by Western economic machines. The central banks admit this. From the FED to the ECB, not forgetting the BoJ and the BoE – all have flooded

1. For an explanation of this mechanism that was criticised in 1931 by Jacques RUEFF, cf. page 72 and those that follow in Dettes et monnaie de singe Hubert RODARIE Editions Salvator 2011

2. Ibid above.

their systems with liquidities and reduced their rates to zero. After globalised finance, global ZIRP (*Zero Interest Rate Policy*), which is a powerful sedative has relieved the burden but has not dealt with it properly.

It has given time to State treasuries and businesses, which over exploited financial leverage, to try and restructure their spending and their models. Indeed in the first instance extremely low interest rates help to limit the rise of financial charges in budgets. Deficit goals are therefore easier to achieve. Debt increases less than forecast.

Businesses with or without market access have unparalleled opportunities for low cost refinancing. Some have even taken advantage of this to issue cheap – so called hybrid debts which are recognised almost as equity.

Excess liquidity and the ZIRP have also had calming, if not soothing effect on other players – the politicians and the professionals. The feeling of urgency has gradually died down. Multiple interests via the lobbies now have another chance to express and exert pressure. The energy required for the quest of better organisation has dissipated.

However memories of the crisis are still there, likewise its painful effect on populations. Rising, long term unemployment, young people without jobs, business bankruptcies, foreclosures, declining consumption, stagnating salaries – all of this places politicians under constant pressure. And this is all the more true since the level of deficits no longer allows for the attenuation of the damaging effects of the crisis.

The time given is used to organise change. The path chosen is that of the consensus, mainly within the international context. Indeed a new measure, born of the 2008 crisis, the G20 is the venue, at least from a symbolic point of view, for this approach. It is supported by others like the OECD, the International Monetary Fund (IMF), the World Bank and the International Bank for Settlements (IBS) within which expertise finds expression. The new Financial Stability Board (FSB) has joined them. Launched in 1999 under the management of Mario Draghi in the shape of a forum (FSF) it earned its stripes as a Board in 2009 which was apparently less surprised by the crisis than were other institutions. Hence we can look at the developments decided upon or launched by these structures.

Moreover not only should any significant reform made to the functioning of the financial system affect its structure and the practices of those involved a priori but it should also lead to changes in the way international trade and the monetary system, with which it interacts a great deal, are organised. Or there should at least be a public analysis of the interactions between these structures.

Three structures: international trade, the international monetary system and the financial system - but few changes

In terms of the first two the description of developments will unfortunately be rapid. No issue of reform has been publicly discussed. The only things said are in a defensive mode.

In terms of world trade, in spite of some polemic or criticism the policies copy previous years and aim to extend free trade. Multilateral negotiations are in stalemate. But more limited initiatives exist. In addition to thought about zones enjoying enhanced cooperation, bilateral free-trade agreements have been introduced notably between Europe and South Korea or are under negotiation with Japan and, since February 2013, with the US.

In terms of the monetary system debate is less clear. There has been no multilateral negotiation, even though the subject is addressed formally, or informally, during the various G20 meetings. Hence in 2010 the Brazilian Finance Minister Guido Mantega spoke "*of the currency wars*" [3] and pointed to the effects of the variations in exchange rates, notably the devaluation of the dollar under the effect of the American monetary policy. Some American economists and think-tanks always criticise the impact of the Asian exchange rates on American employment. But the Treasury however maintained its diagnosis that was communicated to the Senate: there is nothing unusual in this. At the end of 2012 and at the beginning of 2013 on the occasion of the national elections Japan however turned the development of the exchange rate of its currency into a

3. In fact, some say that he did not say this. However the theme was attributed to him by the media.

real political issue. After this election and given the downturn in its trade balance, in deficit for over a year and this for the first time in 40 years, it launched the devaluation of its currency, the yen via the implementation of a monetary expansion policy. But for the time being it has corrected barely one half of the appreciation which the yen has benefited from since 2007 against the dollar and the euro.

However in spite of these developments no challenge has been made to the acknowledged and accepted capability to maintain exchange rates via the constitution of exchange reserves held in capital accounts on the balances of export countries' central banks. However this possibility, apart from the bias introduced into trade relations, is the base of structural monetary creation which has fed economies' debt capabilities [4]. These reserves have therefore continued to rise sharply since 2007. If we add the so-called sovereign funds of the very countries which are financed by these reserves to this, the amounts are colossal, totalling around 50% to 60% of the American GDP. This has not been the cause of any specific questions on the part of the public authorities.

However the financial system, as we saw in the introduction has been the focus of great effort.

But given the quest for consensus, even though the various countries do not implement the measures decided, all take part in the drafting process. Everything is very slow as a result. And it is all the slower since the delegations sent in the previous years to structures in the name of their supposed technical expertise, like the Basel Committee [5] for banks, the *IAS Board* [6] and the *FASB* [7] for accounting, further complicate decision making [8]. There are impediments at this level because, beyond the difficulty in amending complicated texts, it is possible that these organisations' have grounds for battle, other than the improvement of mechanisms. For example they may also defend themselves against policies, their administrations, and even business demand, to protect their prerogatives or those of groups which have promoted their rules over the past twenty years. [9]

The plethora of players who want to add their stone to the edifice and who all try to hook up to a decision pertaining to their particular case, might also explain the cumbersome nature of the texts that result from these negotiations.

But this, in our point of view, is not the real reason. Indeed often pertinent responses are provided by this work but they do not aim to dig deep into the spinal column of the financial system. And so in the absence of any challenge to the base, in other words, the calculation engines, it is logical that the discord between the measure calculated and reality is attributed firstly to a deliberate error or not by the person who used the model, then to a lack of or inadequate information which has disrupted the calculation process or even to the lack of a risk module.

This approach is similar to the one which is naturally our own when we look for the cause of car accidents. We first look to the driver and successively mention a lack of capacity (drunkenness = ethic behaviour), a steering error (lack of competence or a poorly controlled manoeuvre), poor judgement (due to fog = false information). We then suggest a punishment, driving lessons (training, driving licence), the introduction of an extra mirror, speed limits … The last diligence generally focuses on the vehicle and the functioning of its various appliances.

With this example the professional will easily recognise the approach that has been followed over the last five years by the various authorities – the validation of competences, the identification of processes, all types of options and a focus on the exhaustive nature and quality of the data. We have therefore taken steps that are mainly preventive regarding players and structures. But we still have not looked at the vehicle itself – and its engine even less so.

In spite of the extent of the 2007/2008 crisis and its continuation until now – no fundamental questions have been raised. But if, as Jean-Baptiste Say suggests: "*In administration major problems do not come from the exceptions we have to make to the rules. They come from the false ideas we have of the nature of things and the false rules that we maks as a consequence* [10]", it is probable that one day or another we shall have to address the principles of how our financial systems are organised. The measures that are being taken at the moment have little chance of really being effective.

4. On this point cf. the reference in note 1

5. International Forum for Banking Supervision, formerly the Cooke Committee, created in 1974. It is hosted by the Bank for International Settlements, the BIS

6. IAS Board, the decision making body of the IAS, the internatioanl association which Europe granted the mission of drafting accounting standards in 2002.

7. FASB, or FAS Board the American FAS's decision making body, which is almost State run with the responsibility of harmonisation of American accounting standards since 1973.

8. Note that IASB and the FASB are linked by convergence goals as part of the EU/US Transatlantic Partnership.

9. Cf. site ifrs.org : we highlight the surprising debate over the IAS Board's conceptual framework, the charter of goals and founding principles of the IFRS standards. Clearly a problem the Board accepted debate abou this and this is still ongoing. It indicated however that if changes were made these should not affect standards that have already been set. Where is the coherence in what stands as a hub of expertise?

10. Jean Baptiste SAY in Traité d'économie politique, Livre 1er, ch. XVII

SOME ISSUES ARE MOVING FORWARD HOWEVER

However we should not forget that these reforms often reflect a re-balancing of economic powers between professionals, politicians and civil servants. These developments are also part of a more general change in terms balances of power between old, emerging and new economic zones. By new ones we might think in particular of the emergence of a new player -the Euro Zone. Not only has the crisis enabled its political establishment within Europe and in the international community it has also enabled the strengthening or the constitution of specific means deemed to be pertinent which bind this new zone together via interests and projects. Although the path has been and will be chaotic, questionable and even difficult to achieve the present results, it remains that it is a reality with which we shall now have to reckon. The UK has seen this. We should also note the renewed emphasis on nation-states. They have had to suffer and deal with the banking shock. But far from benefiting from the globalisation that has been boasted about over the last ten years, we have witnessed a certain kind of rescaling, firstly of economic problems, before we were forced to pool aid mechanisms.

These major changes contribute, rightly or wrongly, to the development, not only of laws but also to significant developments in the mechanism as a whole. We might quote three in this case, from the general to the more specific: the acceptance of self-regulation, the universal bank, the remuneration of executives.

Firstly we should note that the legitimacy of the self-regulation of financial activities by professionals as advocated and defended by the governor of the FED, Alan Greenspan is no longer relevant. It did not survive the calls for help on the part of banks to the treasuries of their countries. In spite of the emphasis placed on the much broadcast issue in the US "Five years on the State has won", the voter-tax-payer, still traumatised by problems, expressed a strong political request for public authorities to control the financial world.

This movement has been very strong especially in the UK. It helped support the challenge made to the pertinence of the universal banking model. The Volcker rule of separating activities included in the American Dodd-Franck Act was taken up again and even greater emphasis was placed on this by the Vickers Committee in the UK. European thought led by Liikanen, the governor of the Bank of Finland, is moving in the same direction. And yet this model formed the base of the reform of British finance in the 1980's which promoted what it called *supermarket banking*. This nascent u-turn in the trend is therefore a real event in terms of organisation.

Likewise there is no longer any consensus over the modality of remuneration, both in terms of level and structure. Bonuses are being challenged [11], stock-options, welcome bonuses, retirement packages – all are being reviewed. The restrictions that were applied in structures now under state control are being extended to other businesses. We should say that the difference between the remunerations of ordinary men and women becomes as difficult to bear politically as economic prospects are sombre.

In spite of these developments, it remains that the present intervention by the public authorities is still limited and fragile from a sustainable point of view because since it is the result of negotiation or an affective type of response it is not sufficiently established in a theoretical corpus to withstand the extremely high level of coherence between widely accepted financial theories and the structuress whose creation they have enabled.

UNCHANGED CONCEPTUAL ROOTS

Indeed the scientific models at the heart of this malfunction, which were challenged strongly quite rightly at the start of the crisis have almost all remained unchanged. We should recall our previous diagnoses. The sedation of the regulators' vigilance, at worst their encouragement [12] in the face of the rising debt, werewas based on scientifically proven hypotheses, which were incorrectly deemed strong. They allowed the construction of a financial system of impressive coherence from a rational point of view as they included economic models, regulations, and socially accepted images, together with accounting and prudential

11. Cf.for example the recent European decision to limit the bonuses to once the annual set wage in spite of opposition from the UK will apply across all of Europe at the beginning of 2014.

12. Cf. the presentation and justifications of the previous governor of the FED, Mr Alan Greenspan in the face of American household debt

measures. But with hindsight, in spite of an ambitious design, it revealed itself to be too fragile in the face of globalisation's clearly targeted ambitions.
At the heart of the will to control of financial activities – there is – it is generally said – a desire to gauge the risk involved. But we should explain what "gauging risk" actually means. Gauging, in this case, means having a sum that is the product of a reproducible calculation, the result of which does not depend on the operator using it. We can pinpoint quite clearly the scientific or mathematic dimension of the process. Risk means the uncertainty of what the future might bring regarding something we have, a given or received commitment which is going to link up with the means of measurement ie a quantity, possibly expressed in a financial unit.

Hence after thirty years of progressive development we now have a method of calculation in which a necessarily limited representation of reality has been set. The financial world has collectively asserted its solution and models.

However the reduction of reality is well identified and easy to see. It is carried along by a positivist vision. It only takes on board a smooth future constrained by what we can see today – i.e. the market. However this vision, which we might qualify as optimistic does not always take on board breakdown, finiteness or even the irreversibility of observable phenomenon.

And in view of the financial crisis one question seems to be legitimate: isn't the system in the position of the madman looking for his key under the streetlamp, but not in fact where he lost it? As Pierre Duhem [13] said of careless industrialists at the beginning of the 20th century, haven't the financiers given in to the temptation of using erroneous but comfortable formula instead of ones that are more balanced and more difficult to implement?
Amongst the central ideas of the present arrangement, which we might deem limited, is the efficiency of the markets. But professional observation and experience show that this is rather more fiction than observable reality. Scientific literature, which has highlighted its malfunctions, is not lacking. [14]

However this assumed efficiency, to use one of Pierre Duhem's expressions, is a comfortable one. It facilitates the calculation of an aggregate which has been deemed representative of the risk by assuming that it really represents the amount of uncertainty we have about the future. But a wager over too secure a future had to be made for it to be true.
But the future escapes us. In spite of legitimate pretentions of controlling the consequences of financial commitments that have been made we have to understand that, to a point, the future belongs to no one, either individually or collectively within systems like the markets. Although some have tried to find in the "wisdom of crowds" [15] an effective remedy to the acknowledged mistakes of all kinds of experts, prophets, self-proclaimed wisemen and ideologists, others [16] have indicated the contrary.
Hence we have to admit the structural inefficiency of the markets and the limited nature of the information they provide. We have to say and repeat quite clearly, both mid and long term, on the scale of social time and economic systems, risk and uncertainty cannot be measured with the present scientific tools. We can define them, frame them, establish limits but we cannot provide an exact measure that will remain valid in all areas of the financial system in all areas of the world.
It is therefore likely that the approach that has been collectively taken by our economic systems will be compared in a few years time to that of the alchimists, wanting to change the lead of our ignorance into gold or more precisely into dollars.
Also, and contrary to the implicit choices made by the regulation authorities, the Basel Committee, for the banks to draft the Basel 2 and 3 rules or by the Commission for Solvency 2 applicable to the insurance sector, a safe financial sector cannot be risk based, whether they are internal (*IRB : Internal Rate Based*) or external (ratings agency).
The adjustments that were laboriously made to the economic models of banks, traditional insurance companies, like pension funds in a bid to compensate for obvious limitations or flagrant inadequacies, largely bear witness to this. We end up with ever complicated systems which are also uncontrollable and even the professional gives in to the process that is being promoted to control what mainly appears to be the result of human error.

13. Cf. Chapitre 8 in La Théorie de la Physique Pierre DUHEM, Editions Vrin

14. The hypothesis of financial market efficiency or HME was formulated in particular by Fama and others like Jensen. It was detailed in degrees, weak, semi-weak or strong. It is contested from various angles, behavioural, bias, limited rationality of economic agents. It is discussed by distinguishing operational, informational and allocative efficiency. But the things we are questioning here is the general acceptance that "the hypothesis which suggests that there is a fundamental objective value, which is unambiguously definable ex ante and whose price woud be an optimal estimator (however it) does not exist" (André ORLÉAN in La Tribune 29 March 2011)

15. La Sagesse des Foules James Surowiecki Éditions Jean-Claude Lattès, in this book the author highlights the situations in which crowds achieve better results than isolated individuals. However the necessary conditions are not those seen continually on the financial markets.

16. Psychologie des Foules, Gustave Le Bon, 1895, Alcan

ACCOUNTING STANDARDS THAT DISAPPOINT BUSINESSES AND INVESTORS

Almost ten years have passed since the cavalier promotion and adoption in Europe of the IFRS, new supposedly international accounting standards. All opposition was rapidly brushed aside. Critics of this new body of rules had a clear vision however of the limits of the measures being put forward. The events that followed during the crisis demonstrated this. Today there is still no unanimous agreement about the IFRS both amongst businesses and the analysts [17].

Although at first the adoption of identical rules might have seemed to herald real progress to facilitate greater knowledge about European businesses, in the face of diverse accounting traditions and customs in the various countries of Europe, can we say that this was due to the instrinsic quality of the standards which are based on a conceptual framework that is really more effective that the previous one?

Can we say that by valorizing as widely as possible and even systematically positions in the balance sheet to describe the business in the best possible manner we are making a qualitative leap in terms of knowledge about businesses and their activity models, either for the company itself, the analysts and all of those involved, clients, staff, suppliers etc …?

It is difficult to give a full answer given the range of the question. However two points can be developed. One being the consequence of the other.

The first point is common to previous arguments about risk control. If by also basing ourselves on the experience of the financial crisis, we maintain that to control risk the value of the market is not a powerful indicator, it seems illogical that accounting can take market prices, either on their own or substantially [18], as an expression of value.

In the specific case of accounting it seems that it is even more legitimate to wonder about the sense and pertinent nature of an approach which uses an instant, continually varying price to express a "value", ie a reality which will continue or which will not change significantly over a certain period of time in the future.

Yet precisely, this is only possible if we accept the underlying assumption of market efficiency discussed earlier. Hence once we have set aside the scientifically demonstrated nature of this assumption, we can see that what we might call a belief or a convention has been introduced into the economic and social system. We can believe or not. How exact is it? This is no longer the main question because any system is ordered around the acceptance of that belief. It is the phenomenon of "performation" as noted by sociologists. A statement creates a social reality in which individuals can act without necessarily always being aware of the role played by this statement. But once identified as the base the main question is then to decide whether this choice is pertinent or not. In the case of market efficiency all players acknowledge that this is key. How do we judge the tree other than by the fruit it produces?

It then becomes clear that evaluative accounting, either full or partial, the "fair value" promoted by the American FASB or the IAS Board, which depends on the acceptance of market efficiency, is not adequately justified for us to accept the painful consequences seen during the crisis: including excessive volatility and its amplification effects. It does not allow the various parties involved to have at their disposal sound, valid evaluations for each and every type of economic activity.

It adds volatility, which although not always deemed useful, can legitimately be qualified as artificial and destabilising in a world that does not need it. The equity that is calculated by these new standards is no longer a reflection of accumulated, available wealth for difficult times, like cash placed in reserve. They are only differences in more or less established values. They are not sufficiently pertinent or powerful enough to overcome crises.

The second point involves the standardisation system's ability to represent a business model. But today we see that the financial analyst is forced to seek out himself how cash is generated and used to confirm the values put forward [19]. In other words he has to look for indicators that help him assemble the figures communicated by the company and his vision of the business model.

For their part companies even tend to add more infor-

17. Cf. 62% of those interviewed think significant changes are necessary in the Price-Water-Coopers Survey Sseptember 2012 : Financial reporting priorities, A European Investor review

18. Unlike the first IAS 39 standards, in which the market value was a strict rule for financial instruments the IASBoard, is moving to an ever wider acceptance of transactions on an historical cost base. It is adopting an approach whereby the application of its principles is being attenuated without rejected them outright.. This is the same approach used by those who promote the global method in learning to read as they move over to a semi-global approach.

19. Cf. PWC survey September 2012 quoted in note 5 : 47% of those interviewed want more details about cash-flow operationals mation [20]. The terminology in force calls this non-GAAPs, to indicate a lack of standardization, which will again motivate a demand for either private or public standardisation [21].

These two points are not specific to Europeans. They have also been raised in the US by professionals. We can refer to the most recent letter to the shareholders of M&T [22], a traditional American retail bank, signed by its chairman and CEO Robert G Wildmers. He criticises the failure of the FASB. He points to the complexity, the confusion and the opaqueness introduced into the accounts by these standards and the inflation of the account presentation documents. Their content has been multiplied eight-fold in twenty years. He even believes that only the "Big Four" find any benefit since they have been able to multiply their fees two-fold over the last ten years. Unfortunately they also sit on the IAS Board.

Players on both sides of the Atlantic are caught in a never ending quest for transparency and explanation, like the Raiders of the Lost Ark, and yet the thing missing is not necessarily the reality of the enterprise but the answers to sometimes unexpected developments. Finally we note that in terms of economic information the financial world has undergone a radical change.
From the 1960's to the 1980's, data was not readily available. The challenge on the capital market was the collation of pertinent, exhaustive facts which had to be collected, retained and processed. Now the main problem is the inflow of information which is increasingly difficult to interpret and summarise. It is increasingly complicated to validate it given standardised or non-standardised processing and the means of communication which are often closer to influence or disinformation techniques than to a quest for the truth.
Now there are two temptations: synthesis to gain speed in conclusions or systematic automated processing.
The first temptation lies in promoting both synthetic, so-called integrated reports like those fostered by the IIRC (*International Integrated Reporting Committee*) but also the constant use of ratings issued by recognised agencies. Apparently the opinion of a third party is always preferred to ones own and that of ones team. Humility or the bid to reduce responsibility– each to his answer. The second temptation is encouraged by the "data" culture, which is highly present in some national traditions. Data bases, automated processing of raw data, artificial intelligence, all of these aspects are obviously promoted by the suppliers of these services which are supposed to provide increasingly accurate answers.

In the end the accounting standards fostered by the IAS Board, based on inadequate concepts may run out of steam in their complexity which will not add any additional efficiency to the documents and indicators produced.

COMPLEXITY IS ALSO THREATENING THE PRUDENTIAL STRUCTURE OF THE FINANCIAL SYSTEM

Growing complexity and the mass of information to process in terms of accounting which is subject to evaluative, fair value standards can also be seen in the present prudential systems of risk calculation.
The two regimes, prudential and accounting, based on the same assumptions are perfect illustrations of a rationality that is increasingly excessive, we might even call it crazy, as the realisation of its inadequacies in terms of an elusive reality forces it to become ever complex and uncontrollable. Let us take a few recent examples in terms of the prudential sphere, even if they are slightly technical.
The RWA (*Risk Weighted Assets*) help banks define their equity levels. And yet there was agitation in the press recently since in a report by the International Bank for Settlements [23], the authorities pointed to heterogeneous methods when so-called internal models were employed or differences in the approach adopted to calculate the various aggregates in prudential reports. This enabled the respect of minimum regulatory ratios (own-funds /RWA).
From a logical point of view these remarks are surprising because regulations based on the recognition of internal methods (*IRB*), cannot produce homogeneous models. Regarding the form it is strange to challenge *a posteriori* specific features and different know-how or

20. Cf. ibid : 93% of those interviewed deem them important

21. Cf. ibid ,and this all the more that those interviewed observe incoherence and cannot reconcile information with the IFRS financial statements communicated

22. Cf.in M&T, Annual report 2012

23. BIS for the Basel Committeee : RCAP- Analysis of risk- weighted assets for market risk Janaury 2013

the expression of independence of free companies in a globalised world.
In any event, it is likely that the underlying desire to homogenise, to improve the legibility and control of the results observed, which have already been achieved after complicated calculations, will encourage the development of new procedures, the drafting of regulations according to exposure drafts and lengthy consultations ...but the increasingly complicated result will also probably be just as uncontrollable by the regulators. Analysts will not be able to evaluate them either.

THE QUALITY OF THE PRUDENTIAL MODEL IS MEASURED IN LIMITED AND NOT ACTUAL CONDITIONS.

In the same way, why is not possible to see that in terms of controlling the banks the requests for stress tests since 2009 on the part of various authorities in all American and European banking systems, are an explicit rejection of the conceptual choices underpinning the regulatory regimes, and yet they apparently go unchallenged. They are no longer deemed capable of expressing anything acceptable in the event of hypotheses thought to be hard if not extreme.

And yet once more any scientist or engineer knows that the confirmation of a theory modelling real phenomenon, like the resistance of materials for example is tested to the limit and not in areas where nothing of what is really being tested can be seen, in other words breakdown. Why do we stop at this stage in terms of banking regulation? This is all the more true since regulating a system by adding stress tests is no longer satisfactory or in all likelihood effective, such is the scope for criticism of the set of selected hypotheses and the complexity of the calculations.
Wildmers, quoted above counted 6,190 pages or tables that were necessary for the M&T bank, an establishment which had no complicated product on its books.

As far insurers and pension funds are concerned, who still understands the pertinence of Solvency 2 which is supposed to be set as a single standard? Three more years of reporting were completed in 2012 on a reform that was approved in 2009, which ten years ago was unanimously agreed upon by the "industry". Now it will only be implemented in 2017.

Like the pension funds that were excluded from the new standard initially, it is now long term commitments and those subject to greater hazard which cannot be integrated. Intuitively this enables us, even the non-specialists, to determine that underlying theoretical models are typified by an over simplistic idea of the future which impedes the anticipation of the most significant events perceived to be more like catastrophes than the course of ordinary life.
It has taken six to eight years to implement prudential regulation – this proves that commitments and events - which structures have learnt to enter and manage since the middle of the 19th century – a period when the insurance sector was just emerging in Eurpe - cannot be integrated into the Solvency 2 model

Again we had to invent what we might call patches applied to a regime thereby hurting the pride of its designers, who aimed to base it on principles, integrating all developments in modern financial, actuarial science – whilst the numbered measures starting with 1 (Basel 1, Solvency 1) were, so it was said, typified by pragmatism, even the arbitrary and especially a lack of any scientifically established principles. In the end this burdened businesses with a surplus of minimum required equity.

AT THE END OF THE DAY

We might conclude that the conceptual inadequacies of the mechanisms set in place or which have been promoted over the last 20 years to control the financial systems have not been corrected. The reforms introduced are leading to increasing complexity, as well as uncontrollable and in all likelihood ineffective measures. They make work ever more cumbersome, generate costs and make structures rigid. This complexity is therefore the true expression of the sickness that these reforms were trying to heal however.
What can we do then?
Does it matter? More importantly can matters be

improved? Can we wager that in spite of everything there has been an improvement in comparison with the previous period? Can we not say that this complexity, whatever its origin, would firstly be the consequence of the incredible rise of globalisation? Indeed might we think that a globalised economy could be simple? Might we then maintain that we have to bear with this? Fatalism and the relinquishment of structuring reforms would then be fully justified and become the line of conduct for a certain length of time at least.

THE PRESENT DANGER IS THE DEGENERATION OF THE ECONOMIC MODEL

This rapid overview of financial reform has insisted on the increasing complexity of regulations and accounting in the financial system. But it also extends to the rest of the economy. It is also disrupting foreign trade and the analysis of monetary measures. In all events it is leading to extremely diverse regulations that sometimes target some surprising issues but these are always dominated by preventive measures. They have immediate effect in facilitating oligopolistic concentrations, herdlike behaviour, and especially the litigious shedding of responsibility.
Let us just take a few examples to illustrate these developments.
Oligopolistic concentration: in the USA after five years of crisis 10 establishments manage nearly 75¨% of the financial assets. The biggest have absorbed the weakest.
Herdlike behaviour and the shedding of responsibility: in all systems politicians have tried to find the origin of the errors. As we described above, since they were not found in the system's design, individual or collective errors had to be defined. These were logically of a criminal nature, or due to a "lack of control".
The first situation was quite extraordinarily and astonishingly ignored by the authorities. The second however is the base of the path towards transparency over means and ends. This was achieved by ever greater regulatory interference in business life. Companies now have to ask for all kinds of approval, about the board members, the management, about the necessary presence or not of written processes, about the company's activities. They have to draft and have increasingly detailed activity programmes approved. And as far as products which are manufactured and sold to the consumer, we can add that in a bid to protect the latter, consumer protection has been introduced and the latter even have to be defended against themselves....
All of this leads to the tight standardisation of all operations undertaken in all companies. As time goes by, the specifications become increasingly precise by strucutres which enjoy greater means and in some cases compete to justify their existence in these times of budgetary restriction.

In all it is logical to note that behaviour has tended to stultify and become the same whatever the circumstance. The focus of those in charge turns away from the result towards the implementation of regulatory requirements.

Practiced in a collective or individual manner this regulatory mimetism will facilitate extremely damaging repercussions, in other words the amplification of the most harmful trends seen during financial crises.
More importantly we should look into whether this is a sign of a deeper set phenomenon – that of a degeneration in the global economic system as it stands today.
Indeed it is tempting to draw a parallel with the Soviet economic system which experienced its brilliant [24] zenith in the 1960's but which did not survive the 1970's and finally experienced an extremely painful demise.
Historically we might say that the systematic, centralised planning used to define the allocation of resources in the Soviet economy caused the failure of its economic model. For nearly twenty years all kinds of economist were struck (and even convinced) by the apparent efficacy of this system: it had everything necessary from growth rate to output tonnage and volumes. We should re-read the 18 lessons on industrial society written at the end of the 1950's by Raymond Aron, who however, was not suspected of having any sympathy for the regime. Although the figures impressed, only the belief that the human cost was too high impeded people from adhering to it. However, year after year the mechanism seized up. The arbitration and rationality that should

24. An adjective that is limited of course only to quantitative economic results of the time,.

have been established simply collapsed.

There were two main reasons for this. Firstly the increasing complexity that emerged once the economy had completed the stage of post-Second World War reconstruction. Then the pollution of the various information circuits that were necessary for decision making - either in terms of requirements or projects. Complexity and inadequate information blocked what in the eyes of its supporters was the height of modernity: the introduction of rationality.

History then tells us of waste, losses and rigged statistics which were increasingly out of line with real achievements. This all led to an increasingly costly, complex, military/industrial slippage which collapsed with the political regime after a vain attempt to reform (*perestroïka*) and to bring transparency (*glasnost*). It is said that history does not repeat itself but with same measure of risk, is it not serving the same dishes in the once triumphant West?
What can we see today? In the West there is economic, general stagnation, the middle classes are declining, there is an increase in poor workers, however elites are being created, true *nomenklatura* [25], with an ever increasing gap between their revenues and those of their contemporaries, resource wastage, general incapacity to reform, communication means that are controlled by a one-track approach and story telling, the reduction of prospects for young people, almost general impunity in the economic sphere, weakening of the legal system, increasing complexity of rules and legislation, the relinquishment of mechanisms to re-balance the market to the benefit of interest and exchange rates set by civil servants, etc. All of these are objective signs of regression.
It is urgent for us to be aware of this. It is time to look at reform from the very start. Appropriate concepts that are adapted to modern realities have to be reintroduced. In sum: simple rules, accounting that is linked to real elements in the economic model, a return to the distinction between accounting and evaluation, the personal assumption of responsibility versus procedures. We know all of this already and it has already been described. All we need is the clear will to take action.

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25. The world superclass according to Samuel Hutington in Who Are We: The Challenges to America's National Identity (2004)25.

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