Transparency is vital in these times

ALASDAIR ROBERTS

THESE are difficult days for people who care about openness in government.

Around the world, politicians are claiming that the urgency of the economic crisis allows no time for transparency – and that austerity requires cuts to programmes that allow access to information about government operations. Transparency, they argue, is a luxury rather than a core function of government.

In times like this, it's important to remember that it was a lack of transparency that led to the current global crisis. In many ways, people got into trouble because they did not really understand what they were doing. In the United States, for example, a housing bubble was expanded by reckless borrowing to homeowners who were ignorant – or misled – about the terms on which they were taking on debt. Borrowers, one report recently concluded, "did not understand the most basic aspects of their mortgage".

The financial institutions that extended credit were not much better informed. They created new financial instruments that were, in the words of a recent Australian court decision, "grotesquely complicated". Former US Federal Reserve chairman Alan Greenspan conceded in 2009 that he was "bewildered" by the new mechanisms that banks were using to finance their operations. "I don't understand what they're doing," Mr Greenspan said. "And if I don't understand it, how the rest of the world is going to understand it bewilders me."

As one witness told a recent inquiry, investors who bought these financial instruments often lacked "the analytical ability to assess the securities they were purchasing". Instead they relied blindly on the advice of major credit rating agencies. But the expertise of those rating agencies was illusory. They gave the highest possible ratings to financial institutions such as AIG when they were only days away from collapse.

Even financial executives were ignorant about the risks their own institutions were running. Before the financial crisis, a study by the Bank for International Settlement concluded in 2009 that senior managers in many firms were "unaware of the full extent" of their potential liabilities. A prominent financial analyst has recently observed that the structures of major financial institutions are so complex that they are "unanalysable and uninvestable".

Governments have suffered from similar problems of opacity. Many bragged about their commitment to budgetary transparency in the years before the financial crisis. After the crisis, the realities became clearer. The government of Greece admitted that it had manipulated budget data to meet requirements for membership in the eurozone.

Many governments also adopted structural reforms that had the effect of improving their balance sheets. One popular technique was the use of public-private partnerships to borrow for major capital projects. The long-term liabilities incurred by these vehicles were not counted in calculations of government indebtedness, even though taxpayers continued to carry the final responsibility for the servicing costs of debt assumed by these ventures.

This was not the only way in which governments disguised their true liabilities. Many understated their long-term obligations for pensions and healthcare, through unrealistic assumptions about the capacity to control future costs or the rate of return on off-setting investments.

And the financial crisis itself revealed another unacknowledged liability: The obligation to support financial institutions that are too big to fail.

The cost of support to the financial sector in the first three years of the crisis was about seven per cent of 2011 GDP in the advanced economies.

The years before 2007 were a veritable carnival of ignorance in the private and public sectors. We were deluded into thinking that we knew more than we did about the true state of our finances. If there had been real transparency before 2007, we might not be in the state that we are in today.

And so there is a deep irony that the crisis itself is being used as a pretext for restricting openness. We are told that in a time of austerity there is neither time nor money to maintain programmes that assure access to information about government activities. Elected officials tell us that priority must be given to core services, and that openness must be sacrificed.

This is a dangerous mistake. Real transparency is the best way to assure that the public understands the hard choices that governments are being compelled to make during this economic crisis. And it is also the best way of avoiding a reprise of the calamities of the last four years.

Opacity got us into this mess. Transparency will get us out of it.

Alasdair Roberts is the Rappaport Professor of Law and Public Policy at Boston's Suffolk University Law School. He spoke at the Tenth World Conference of the International Ombudsman Institute in Wellington last week.

Dominion Post, November 19, 2012