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Transparency in Troubled Times

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Abstract. Difficult economic times are often threatening to the idea of transparency. Financially troubled governments argue that openness is a luxury, not a necessity. And the political uncertainty that is generated by economic troubles sometimes makes governments hesitant about releasing sensitive information. But the reluctance to maintain transparency can have serious consequences. Secretiveness can undermine the legitimacy of governmental action and contribute to political instability. Indeed, the crisis itself can be regarded as the result of multiple failures of transparency in the private and public sectors. The temptation to view openness as a luxury must be resisted. It is precisely at the moment of economic crisis that the idea of transparency is most important.

TRANSPARENCY IN TROUBLED TIMES

I. HARD CHOICES

Let me begin with a brief explanation of my own introduction to the topic of freedom of information, or FOI. I have been using FOI laws since the 1980s, but I began studying them seriously in the Fall of 1997. The Canadian Newspaper Association asked me to examine how well the country's twelve FOI laws (one federal, nine provincial, and two territorial) were working. My report was published in April 1998.[1] The findings were mixed. The good news was how quickly the innovation of an FOI law had spread across the country in the preceding fifteen years. Canadians were beginning to see the right to information as a necessity. The bad news was that in the few years preceding my report, several governments had taken steps that undermined the principle of transparency.

It was a difficult time in Canada. Foreign investors became wary of Canadian government debt in the early 1990s after it was downgraded by major bond rating agencies. In January 1995, the *Wall Street Journal*'s editors warned that Canada had "become an honorary member of the Third World in the unmanageability of its debt problem."[2] Under pressure to reassure global financial markets, federal and provincial finance ministers took strong measures to restrain government spending.

In many ways, this austerity drive compromised the operation of FOI laws. The province of Newfoundland eliminated the office of its Ombudsman, which handled FOI appeals, as part of a drive to "eliminate spending that is no longer serving a useful purpose."[3] The province of Ontario increased fees for making FOI requests or filing appeals about FOI denials. Several governments transferred work to contractors who were not covered by their FOI law. Within the federal government, budgets for FOI

offices were cut severely, and the Information Commissioner complained that slowness in responding to information requests was "a festering, silent scandal."[4] The Commissioner's own office, also caught by the austerity exercise, struggled to manage a deluge of complaints about delay in federal departments.

The politicians and bureaucrats who organized this assault on FOI were driven by mixed motives. Some regarded the austerity drive as an opportunity to limit FOI laws which they had always viewed as "costly and disruptive." Others insisted that priority had to be given to "core" or "essential" programs, and that FOI simply did not fall within this protected circle.[5] To use the phrase that was popular within finance ministries at the time, hard choices had to be made. No-one in government gave much weight to the complaint that, by gutting FOI, it became more difficult for the public to see how those choices were being made, or trust that they were being made in the right way. In a crisis, transparency was regarded as a luxury.

II. AUSTERITY, AGAIN

I mention this story because there is a certain parallel between Canada's predicament in the mid-1990s and the world's predicament today. Without a doubt, the movement for transparency has enjoyed tremendous success around the world over these last fifteen years. The number of countries with FOI laws has quadrupled, to more than ninety. The ideal of openness has also been pursued in many other ways, through policies targeted at government budgeting processes, election financing, development aid flows, revenue from natural resources extraction, public works expenditure, and the performance of schools, hospitals and other essential services. Over fifty national governments have subscribed to the global Open Government Partnership, which hopes to use transparency as a tool to empower citizens and fight corruption. In the last two

decades we have also witnessed the emergence of a vibrant global network of civil society activists who are committed to transparency. Some jurists have even recognized the right to information as one of the fundamental human rights.

Over its short life, the global movement for transparency has had the advantage of favorable economic conditions. Of course, this was not equally true at all times and in all places. For example, some of the recent adopters of FOI laws are much poorer than the countries -- mainly wealthy OECD states -- that first adopted such laws. And some countries that adopted FOI laws and other transparency measures did experience periods of real hardship over the last fifteen years. Broadly, though, the world experienced robust and steady economic growth. "The world economy is in remarkably healthy shape," Anne Krueger, a senior official at the International Monetary Fund, said in March 2006. "The benign global economic environment provides countries around the world with a valuable opportunity to press on with reforms."[6] Good times made it easier to adopt transparency measures, as well as many other governance reforms.

Unfortunately the good times ended after the financial crisis of 2007-08. Government deficits exploded as a result of collapsing government revenues, bailouts of troubled financial institutions, and economic stimulus programs. In the United States, central government debt increased from 35 percent of GDP in 2007 to 61 percent in 2010. In the United Kingdom, central government debt increased by 43 percent of GDP in that period; in Ireland, by forty percent of GDP; in Spain, by twenty percent of GDP. Even New Zealand saw its debt increase by ten percent of GDP in just two years. Credit rating agencies became more skeptical about sovereign debt, and many countries were urged to restore confidence in international financial markets by imposing tight discipline on government spending. Because of the unprecedented scale of the 2007-08 crisis, austerity became a widespread concern.

In several countries, this new emphasis on fiscal restraint threatened to undermine FOI law, just as it had in Canada in the mid-1990s. In the Netherlands in 2011, Home Affairs Minister Piet Hein Donner called for restrictions on the Openness of Government Act because the handling of some requests was not an "efficient use of time."[7] Australia's Information Commissioner warned in February 2012 that the Finance Department's demand for an "increased efficiency dividend" -- that is, staff cuts -- would compromise his office's ability to respond to citizen complaints in a reasonable time.[8]

In the United Kingdom, government agencies actively lobbied Parliament to impose higher fees and other restrictions on FOI requests. "Consideration of the financial impact of FOIA is pertinent," the UK Ministry of Justice argued in December 2011, "at a time when all public authorities are required to do more with less."[9] An advocacy group for English hospitals complained in February 2012 that "resources are under pressure . . . [and] being diverted from the core business of caring for patients."[10] Local governments echoed the concern about the cost of FOIA administration. "Unnecessary" requests, one official said in October 2012, "are in some areas detracting from frontline services."[11] (In July 2012, though, a parliamentary committee rebuffed calls for new charges, saying that better evidence was needed about the burden imposed by the FOI law.[12]) Meanwhile, British businesses viewed the government's austerity drive "as a real opportunity for those with a vested interest in outsourcing services"[13] -- bad news for FOI advocates, given the UK law's limitations in assuring access to information held by contractors performing public functions.

Scotland's Information Commissioner sees similar tensions mounting in the operation of Scottish FOI law:

> The current economic situation is leading to an increase in FOI requests to authorities, as people naturally want to understand the reasons behind

> decisions that affect them. At the same time, authorities are finding themselves with fewer resources to respond. . . . [In addition] an ever-growing concern is the loss of rights occurring through the delivery of public services by "arms-length" organisations and third parties. FOI was introduced for a reason - to ensure that the delivery of public services and the spending of public money is transparent, open and accountable. It is simply not acceptable that citizens' rights continue to be eroded through complex changes in the delivery of services.[14]

In the United States, the non-governmental organization OMB Watch reported in January 2012 that recent federal legislation had produced "deep cuts in spending" for transparency initiatives.[15] A study by the *Sacramento Bee* found that government officials in California, one of the most fiscally troubled of the US states, were increasingly blaming "budget cuts and furloughs" for delays and denials of information requests.[16] In Canada, the federal Information Commissioner once again worried about the "impact of diminishing resources" on federal departments' compliance with the Access to Information Act.[17] And a 2012 review of New Zealand's FOI legislation also observed that "the global financial crisis has placed the spotlight on the best and most efficient use of public resources:"

> [B]oth central and local governments are forced to do more for less cost. . . . As resourcing pressures mount, there are questions about whether charging should be used more consistently as a lever to control more extreme requester behaviour, and whether the charges of a wider range of official information related tasks should be chargeable.[18]

Today, the pressure to reduce governmental spending is felt by many governments. This seems to put us on bleak, but still recognizable, terrain. Government officials make the usual argument: that FOI is not an essential service, and

that it should give way to other priorities. Advocates of FOI reply that it is precisely at moments like these, when governments are making difficult choices about where spending should be cut, that FOI is most important. Which of the two arguments wins out hinges on political considerations within a particular country. But the struggle appears at first to be a familiar one.

III. A DIFFERENT KIND OF CRISIS

Unfortunately this is a misconception of the character of the crisis that confronts FOI advocates today. The situation is worse that it first appears. In previous fiscal crises, there was usually little doubt within policy elites about the nature of the problem that governments needed to resolve, and how they should resolve it. The overarching principles that should guide economic policy were generally accepted. (This free-market orthodoxy was sometimes called the "Washington consensus."[19]) Governments that deviated from one of these principles, that of strict fiscal discipline, were compelled to make painful adjustments. But they did this with a strong faith in the wisdom of the overall paradigm. They believed that a program of austerity would allow them to regain admission to the large club of countries that continued to enjoy robust economic growth.

Conditions today are very different. The crisis is so broad and deep that it has shaken faith in the free-market orthodoxy itself. Even among technocrats who previously accepted the prevailing paradigm, there are questions about the soundness of its essential elements -- such as "light-touch" regulation of the financial sector, liberalized capital accounts, autonomized central banking, restrictions on state intervention in key industries, flattening of tax rates, and even austerity programs themselves. Technocrats are not alone in questioning the established way of doing

business. There is a widespread collapse in public faith in the wisdom of technocratic decisionmaking: a broad crisis of legitimacy that has resulted in political instability and street protests in many countries. We are at one of those rare and difficult moments in history when governments and electorates confront massive uncertainty about the future, and in which the basic ideas that guide government policy are in dispute.

This is a different kind of crisis than those which affected individual countries in earlier years. And consequently the debate about governmental openness is also different.

Within governments, there are much stronger pressures to maintain secrecy. The problem that most governments confront today is not simply one of deciding which domestic constituencies should bear losses because of budget cutbacks. Rather, governments are making decisions that could affect the stability of the national economy as a whole. In Europe, the stakes are even higher than this. The survival of key institutions of continental integration is in doubt. (In October 2011, the head of the European Central Bank described the continent's troubles as "a historical event of the first magnitude, the worst crisis since the Second World War."[20] There was "complete uncertainty," the Bank of England's governor agreed in June 2012, affecting "not only the euro area . . . [but] the world economy as a whole."[21]) Under such high-pressure circumstances there are strong incentives for policymakers to close ranks.[22] Economic policy has become a matter of high diplomacy, and is shaded by the "ethic of confidentiality" that has always been a hallmark of intergovernmental negotiations.[23]

But if the tendencies toward secretiveness are unusually strong, so too are the arguments for transparency. It is precisely because we are at a rare turning point in history that the information rights of stakeholders outside government -- advocacy groups, journalists, legislators -- should be robustly protected. In a few years, a new consensus about the broad direction of national policy will have formed, and will be

almost unshakeable until the advent of another major crisis. At that point, transparency will do little but illuminate a largely unchangeable status quo. If our commitment to openness is rooted in the ambition to promote full exercise of political participation rights, then it is precisely at this moment of flux -- when choices with large and enduring consequences must be made -- that access rights should be robustly protected.

The case for transparency at this moment does not depend only on the right to participate fully in decisionmaking on national priorities. Openness is also an important part of the response to the crisis of legitimacy confronting national institutions in many countries. Eurobarometer data shows a sharp decline in trust in national and European political institutions since the advent of the financial crisis.[24] The Gallup Poll reported in September 2011 that four out of five Americans -- a "record-high" proportion -- were dissatisfied with the way their country is being governed.[25] Indeed, "dissatisfaction" is hardly the word to describe the foul temper of electorates in many countries affected by the financial crisis. Many citizens feel betrayed by their national leaders. There is a widespread sense that democratic states have degraded into "financial oligarchies."[26] Secretiveness about government policy toward the financial sector, and especially about the the terms on which it is extending aid to financial institutions, only fuels voters' anxiety about their loss of control over public institutions.

IV. A CRISIS CAUSED BY OPACITY

The natural temptation during any crisis is to regard transparency as a luxury. The correct view is to regard it as a necessity, not only to assure that the correct lessons are drawn from policy failures, but also to preserve faith in public institutions. And it

is also useful to remember that, in many respects, it was shortfalls in transparency that produced the financial and fiscal debacles of the last five years.

In the United States, the National Commission on the Financial Crisis has explained how opacity contributed to the growth and eventual collapse of a speculative bubble. Homeowners borrowed large amounts of money to bid up house prices, but "many borrowers did not understand the most basic aspects of their mortgage . . . [M]ore than half underestimated how high their rates could reach over the years." Many low-quality mortgages were bundled to create financial instruments that were sold to investors who, as one witness told the commission, lacked "the analytical ability . . . to assess the securities they were purchasing." In practice, investor "relied blindly" on the appraisal of those securities by major credit rating agencies. But the credit agencies relied on "flawed models" as they certified these new instruments as essentially riskless.[27]

"Lack of transparency," the Commission concluded in 2011, "put the financial system on a collision course with risk."[28] The same rating agencies that saw no danger in new financial instruments also gave the highest possible ratings to financial institutions such as Lehman Brothers and AIG when they were only days away from collapse. However, rating agencies were not alone in misgauging the dangers hidden within these institutions. Financial regulators were equally ignorant of the risks within the sector they were charged with overseeing. "I've got some heavy background in mathematics," former Federal Reserve Chairman Alan Greenspan said in 2009,

> but some of the complexities of some of the instruments [developed by financial institutions] bewilder me. I don't understand what they're doing. And if I don't understand it, and I had access to a couple of hundred PhDs, how the rest of the world is going to understand it bewilders me.[29]

Even executives within the financial sector itself lacked a good understanding of the risks that were being assumed by their firms. "Transactional complexity," as Robert Kolb calls it, got the better of them.[30] Soo, too, did familiar problems of internal bureaucracy. In some cases, executives of financial institutions did not know that their subordinates were engaging in reckless or illegal behavior. When controversy arose in April 2012 over trading losses within JPMorgan Chase, its president Jamie Dimon initially dismissed the matter as "a tempest in a teapot." "I was dead wrong when I said that," Dimon admitted four weeks later:

> I obviously didn't know, because I never would have said that. . . . [T]here was one warning signal. If you look back on it today, there were other red flags. . . . [W]e made a mistake. We got very defensive and people started justifying everything we did.[31]

The head of another major financial institution, Barclay's Bank, also pleaded ignorance after the bank was fined for manipulating a key interest rate in June 2012. Shortly after resigning as Barclay's Chief Executive, Bob Diamond told a British parliamentary committee that he was simply "not aware of any reports" about possible misconduct by his subordinates.[32]

Balance sheet manipulations also obscured dangers in the financial sector. Risky assets were transferred to "special purpose entities" (SPEs) that were ostensibly independent of the financial institutions that created them. This seemed to relieve banks of the obligation to maintain reserves against the possibility of default on loans held by those newly created entities. But the split between banks and SPEs was illusory. When SPEs encountered trouble in 2007, parent banks provided aid and eventually restored the entities' liabilities to their own balance sheets.[33] In fact, the banks had always retained an implicit responsibility for the financial health of their creations. Until the financial crisis, a study by the Bank for International Settlement

concluded in 2009, "some senior managers were unaware of the full extent of their firm's overall linkage to and obligations (explicit or implicit) toward their SPEs."[34] A financial analyst complained in 2012 that the structures of major financial institutions had become so complex that they were "unanalysable and uninvestable."[35]

By 2012, the financial crisis had mutated into a sovereign debt crisis. Greece avoided default by negotiating a settlement in which lenders took massive losses on their holdings of government bonds. The financial market's assessment of the probability of default by other Eurozone nations -- notably Italy, Spain, Portugal and Ireland -- also became more pessimistic. Even in the United States, commentators anticipated the possibility of default as legislators deadlocked in the summer of 2011 over the raising of the statutory ceiling on the total amount of debt that can be issued by the federal government.

Like the financial crisis, the sovereign debt crisis was aggravated by shortfalls in transparency. This was most obviously the case in Greece, whose government admitted that it manipulated budget data to meet requirements for membership in the Eurozone. (Greece was hardly the only government to fudge the numbers. When the city of San Bernadino, California declared bankruptcy in July 2012, its attorney said that municipal finances had been falsified for years.[36]) Other countries used more subtle techniques to improve the appearance of government accounts. In the United Kingdom, for example, Treasury officials adjusted their interpretation of macroeconomic data so that it would appear that the central government was within its previously-declared limits on spending and borrowing.[37] In 2007 the International Monetary Fund questioned the adequacy of "fiscal transparency" in British budget-making and called for "broader audit . . . of key fiscal assumptions" applied by the Treasury.[38]

Many governments also adopted structural reforms that had the effect of improving their balance sheets -- just as financial institutions relied on SPEs. One

popular technique was the use of "public-private partnerships" or "private financing initiatives" to borrow for major capital projects.[39] The long-term liabilities incurred by these vehicles were usually not counted in calculations of government indebtedness. Indeed, some Eurozone countries viewed such partnerships as devices for "getting around [the] Maastricht criteria for debts and deficits."[40] Nevertheless, there was no doubt that taxpayers continued to carry the final responsibility for the servicing costs of debt assumed by these quasi-private ventures. It also became clear that government often carried liability for the additional costs incurred by unsuccessful partnerships, just as financial institutions were stuck with responsibility for their failing SPEs.

This was not the only way in which governments disguised the true extent of their liabilities. Many have been criticized for understating their long-term obligations for pensions and healthcare, through unrealistic assumptions about the capacity to control future costs or the likely rate of return on off-setting investments.[41] And of course the financial crisis itself has revealed another massive and previously unacknowledged liability: the governmental obligation to support financial institutions that are too big (or too politically powerful) to fail. The IMF estimates that the net direct cost of support to the financial sector in the first three years of the crisis was about seven percent of 2011 GDP in the advanced economies.[42] To this we could add the fiscal stimulus required in the first three years of the crisis -- equal to about another five percent of 2011 GDP for the major economies.[43] There is a temptation to write these off as extraordinary, one-time costs. But we should not do this. Banking crises -- and therefore bailouts and stimuli -- are a familiar feature of economies with liberalized financial sectors.[44]

V. THE CASE FOR TRANSPARENCY

In a nutshell, here is where we stand today. Over the last two decades, governmental and business leaders heralded the dawn of a new era of stable growth, built largely on a foundation of fiscal and financial transparency. But the promise of transparency was hollow: in fact, we knew less than we thought we did about the operations of the global economy. So, too, was the promise of stable growth. Instead, the world has plunged instead into an extraordinary economic and political crisis. And now the crisis itself is used by some policymakers as a pretext for curtailing measures that promote openness. In a crisis, transparency is regarded as a luxury.

There is an alternative way of thinking about the events of the last few years. We could recognize that in the years preceding the crisis we failed to take the idea of openness seriously. Government and business leaders talked about the virtues of transparency, but they were not adequately tested on it. As a consequence, they became complacent in what they did and said. They skirted rules, became lax in monitoring their subordinates, and imagined that they were better informed about the state of the world than they really were. If the idea of transparency had been applied more rigorously -- if leaders had been pressed to disclose more, and prove the accuracy of their disclosures -- today's economic and political crisis would have been averted.

Similarly, a rigorous application of the concept of transparency can help us through the current crisis. Transparency allows legislators and the public to learn from the mistakes that preceded the crisis so that they will be not be repeated. It breathes life into political rights, giving citizens the opportunity to participate in decisions about the role of government that will have for consequences for them for years to come. And it helps to clothe those decisions with legitimacy in the eyes of the public. Transparency, at this moment, is not a luxury. It is one of the most important tools for restoring political and economic stability.

NOTES

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