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*Capital Failure: Rebuilding Trust in Financial Services*

Edited by Nicholas Morris and David Vines

Oxford: Oxford University Press, 2014.

432 pp.

Hbk £60.00.

Trust in the financial services industry is broken. Such a categorical statement may seem harsh, but we have yet to find closure over the misdeeds and misfeasance that led to the Global Financial Crisis. A few individuals have been prosecuted and banks have paid fines. But even if more people went to jail or if the fines were significantly greater, the current chapter in financial history would still be open. The LIBOR scandal, or more recently the accusations of collusion among the world's largest currency trading banks in the foreign exchange markets, only serve to reinforce the perception that there are still fundamental flaws in behavior and conduct. Add to this the continuance of outsized wages and bonuses in an environment where real wages for many people remain flat and an environment where governments say there is no money left to pay for infrastructure and services that enabled prosperity in the first place, and it is easy to be suspicious and for some even irate. There is a concern that too many organizations and individuals in the financial services industry are working for themselves and not their clients. Hence, many have lost trust in the system.

But for Nicholas Morris and David Vines, and the contributors to their edited volume *Capital Failure*, it is possible to rebuild trust in financial services. Although much has been written about what is wrong with finance and what to do about it in the last five years, it does not mean that *Capital Failure* has arrived too late to the dialogue (see,

e.g., Engelen et al. 2011). Again, it does not appear that lessons have been learned. Nor is it clear whether the regulatory fixes that have been issued adequately address the fundamental problems in the financial system that have resulted in the collapse of trust between clients and the financial intermediaries that are supposed to serve their interests. Indeed, one of the main arguments in *Capital Failure* is that financial reforms and other institutional remedies (e.g. Codes of Conduct) insufficiently secure trustworthy behavior. And it does not accept arguments that financial markets have become so big, so extensive, and so global that reinvigorating trust in finance is impossible without returning to some small-scale pre-globalized form of finance to achieve it.

Geared towards a broad readership across the academic spectrum and the community of regulators, lawyers, and financial practitioners, with accessibly-written essays from a cast of well-known and concerned scholars, *Capital Failure* unpacks the problem of untrustworthiness in financial services and what to do about it. The five essays in the first section deal with what went wrong and why trustworthiness is so important for an effective and socially-useful financial system. In chapter 2, for example, Sue Jaffer, Nicholas Morris, Edward Sawbridge, and David Vines consider how the deregulation boom that began in the 1980s brought in a fundamental reworking of financial relationships. Put simply, deregulation resulted in the commoditization of financial services, where knowing and therefore acting in the best interests of one's clients became less important. Instead of leading to better risk management with the proliferation of new financial products and analytical tools, deregulation skewed incentives towards increased risk-taking with clients' money. And as Tom Noe and H. Peyton Young show in chapter 3, it is all too easy for selfish asset managers to

construct arrangements that yield high returns initially to the benefit of client and manager, but that impose severe risks for beneficiaries that materialize in future years.

Part II offers three essays respectively on trust and accountability that apply to not just financial services but any context. In chapter 8, for example, Onora O'Neill focuses on the role of accountability in underwriting and ensuring trustworthiness. For O'Neill, too much accountability is based on a 'tick box', or managerial, approach. Accountability has become a managerial process rather than a requirement.

Unfortunately, this system is not a replacement for relations of trust. O'Neill offers what she calls an intelligent approach to accountability where trust and accountability go hand in hand. Put simply, there needs to be an explicit set of obligations and duties that apply to the individuals and institutions that are to be trusted. Individuals and institutions are not to provide proxy indicators of performance, such as market performance, but rather are obliged to provide an account of (non-)performance of how they fulfilled their obligations for which trust was placed.

In Part III of *Capital Failure*, three essays take the discussion a step further and considers how the legal and regulatory systems can be used to restore trustworthiness. Joshua Getzler in his chapter argues that fiduciary duties in asset management are often pared back through contract, particularly in the context of so-called sophisticated investors (e.g. large pension funds), which leaves financial intermediaries too unmonitored vis-à-vis their beneficiaries. For Getzler, trustworthiness can be improved by clarifying fiduciary duties and remedies. In Justin O'Brien's chapter, there is a need to confront the norms governing the financial industry. Specifically, regulation needs to integrate normative objectives in three

distinct ways: whether products should be deemed permissible, consideration of who carries the risk of poor performance, and whether products and services are legitimate. Importantly, this regulatory framework is not left to regulators alone, but must be reinforced at the corporate and professional level as well. Such institutional level considerations are hence taken up in the essays in the final section of the volume.

In sum, *Capital Failure* is a useful addition to the ongoing dialogue on what can be done to improve the social-usefulness of finance. For social policy scholars the relevance is clear. So many people are now dependent on the performance of financial markets for their retirement income security (Dixon and Sorsa 2009). Rebuilding trust in finance is part and parcel of ensuring they get a good deal.

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