

How we can restore trust in financial institutions

By Gordon Brown

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There has always been an implicit economic and social contract between our financial institutions and the society they serve.

Over centuries the guarantee of responsible stewardship of people's money has been the foundation of the most precious asset a financial institution can ever have – trust.

Two years into the financial crisis, it is clear that the old contract has to be rethought and now made explicit for new times.

In recent years, our global financial system has achieved extraordinary successes; creating jobs, funding businesses, driving down costs and lifting people out of poverty.

But the scale of the failings in recent months cannot be disguised.

The new contract must recognise the two new characteristics of modern financial institutions – their global scope and their interconnectedness.

As we now know, a failure in one large bank anywhere can affect all banks, large and small, everywhere.

Since the potential damage to the wider economy was so great, taxpayers have had no choice but to keep the system afloat.

So while our regulatory changes are designed to reduce moral hazard, any new contract between our financial institutions and our society now needs to reflect the wider costs to the economy and society of potential failure.

At its heart, the contract must answer another issue raised by the crisis: that the distribution of risks and rewards between the banks, citizens and taxpayers is balanced fairly.

Our first response has been to reduce risks by agreeing reforms to the national and global supervisory system – in capital requirements, liquidity, leverage, governance and transparency.

When fully implemented, I believe these will represent a transformation of the sector.

But, as the [discussions of the Group of 20](#) nations this weekend reflected, these changes alone may not be sufficient to protect against future risk and to compensate for wider costs to the general public.

The world has moved on since some of the earlier ideas to address the responsibilities of the financial sector to the economy and society. There are now broader areas that have been the subject of the recent debate amongst policy makers, commentators, economists and bankers. These include insurance fees to reflect systemic risk; collective or individual resolution funds; contingent capital arrangements; and global financial levies.

In Pittsburgh and at St Andrews, leaders and finance ministers [asked the International Monetary Fund](#) to look afresh at this issue and at the range of options available.

I believe any measures we consider should be assessed against four core principles.

First, in a global economy and with a global financial sector, any such measures could work only if applied globally.

Second, any measures must not create distortions or incentivise avoidance.

Third, any measures must complement regulatory measures already being adopted or discussed.

And fourth, any costs to the financial sector must be fair and measured to enable institutions to do their job for our economy.

A new contract requires a wide public debate, one in which banks themselves should be leading participants. It will not always be a comfortable discussion, but it is in my view an essential one.

Banks cannot assume that trust will return without significant change. So it is in the interests of all banks and financial institutions to participate in this debate and I am happy to play my part in bringing banks and governments together. As this crisis has also shown, some financial institutions have managed their risks and maintained trust. And one of our tasks now is to ensure that all rise to the standards of the best

While I do not doubt there are practical and technical issues that will need to be overcome, the gravity of the recent crisis makes this discussion urgent. The restoration of trust depends on a resolution of these issues. Failure to do so will put at risk the confidence of millions of people in globalisation, setting back economic and social progress. We must all rise to the challenge.

The writer is the UK prime minister