Giving Voice To Values on Business Ethics and Corporate Social Responsibility Collection
Mary Gentile, *Editor*

Working Ethically in Finance

Clarifying Our Vocation

Anthony Asher

BEP BUSINESS EXPERT PRESS

Working Ethically in Finance

Working Ethically in Finance

Clarifying Our Vocation

Anthony Asher

BEP BUSINESS EXPERT PRESS

Working Ethically in Finance: Clarifying Our Vocation

First published in 2015 by
Business Expert Press, LLC
222 East 46th Street, New York, NY 10017
www.businessexpertpress.com

ISBN-13: 978-1-60649-874-3 (paperback)
ISBN-13: 978-1-60649-875-0 (e-book)

Business Expert Press Giving Voice to Values on Business Ethics and Corporate Social Responsibility Collection

Collection ISSN: 2333-8814 (print)
Collection ISSN: 2333-8806 (electronic)

Cover and interior design by S4Carlisle Publishing Services Private Ltd., Chennai, India

10 9 8 7 6 5 4 3 2 1

Printed in the United States of America.

Abstract

To develop a vocation we ask: what do I want to be remembered for? It involves aspiring to personal integrity and a life well lived.

Those of us working in the financial sector fulfill our vocations by finding ways to serve its social purposes, which is to allocate resources efficiently and to provide financial security—not forgetting the needy. This means contributing to institutions, where people can flourish personally, and creating appropriate products and services. The ethics of those working on finding their vocation do not flow from rules and obligations, but from a personal commitment to seeking the really good life. This life is based on the fundamental personal virtue, which is integrity. It is concerned with building well, tying our thinking to our words and actions, our work to our motivations and to intrinsic rewards, and means to ends everywhere.

The book is written for those who aspire to the cultivation of the virtues of wisdom, self-control and courage—to develop ourselves and protect ourselves from the intrusion of others—and justice, which is the social virtue that underlies flourishing communities based on mutual respect. We need communal structures and regulations to help us, but these are better if they are less rule orientated, are forgiving, and aimed at bringing out the best in people. The current flaws in the financial system of overcharging, over-servicing, and recklessness are unjust, but can and are being addressed by those who rise to the challenge of finding their virtuous vocations.

Keywords

virtue, vocation, finance, integrity, justice

Acknowledgments

I would like to give thanks to those who have contributed to the shaping of my vocation: as actuary, Christian, husband and father, citizen and friend. It has been my privilege to have worked with many competent, committed, and compassionate people, and been able to call many of them friends. C. S. Lewis, in his *Four Loves*, writes:

> *In a good friendship, each member feels humility towards all the rest. He sees that they are splendid and counts himself lucky to be among them . . . The ancients saw it (friendship) as the happiest and most human of loves; the crown of life, and the school of virtue* (1977, 77).

In particular, I thank those who have encouraged me in various ways to write for conferences and journals. Especially valuable have been those who have given feedback that has spurred me to read more and address the process of mental accommodation necessary both for understanding and clarity of expression. If my ongoing shortcomings in these are too evident in this book, I can only plead some progress from the earlier attempts listed in the bibliography. From those who have spurred me, Rob Thomson, who supervised my PhD and commented in detail on an earlier draft of this book must be given first place, but Rob Rusconi, Mickey Lowther, and Piet de Jongh have also made particular contributions or interventions. Mary Gentile, a wise and gentle editor, and Rob Zwettler provided the encouragement of a contract to write the book.

Jane my wife, best friend, editor, and critic, those who have been part of small Christian fellowship groups, and many colleagues and fellow actuaries, have been a source of encouragement and support. Rob Thomson, Roger Donbavand, Nick Hudson, Paul Oslington, and my sons and daughters-in-law, Robert, Jess, John, Bec, Michael, and Jacqui have also commented helpfully on earlier drafts—thank you.

Contents

List of Figures and Tables

PART 1

Preliminaries

Introduction

I write this book for those working, or about to begin working, in the financial sector who are aspiring to find personal fulfillment and make a contribution to society. Finding fulfillment in work is best enjoyed in fellowship with others. I find it exhilarating to find those with fellow aspirations, and would be delighted if you found some personal encouragement by reading this book.

It is a book on ethics, but is more concerned with identifying what is good—the virtues and the opportunities—rather than avoiding the bad, even if the two cannot be easily separated and much good will involve correcting the bad! The virtues are not new concepts, but they are not always familiar to those trained in economics and finance. Some are inconsistent with widely held ideas and theories of business. I have tried to span the gap between the old concepts and modern research, because they agree more often than is appreciated. I also try to span the gap between ethical theory and personal practice. My hope is to contribute to the development of a common language to address questions of ethics in finance, and to our personal, social, and economic flourishing.

Before proceeding, let me explain a few personal quirks:

- It will be clear to you that this book is full of my opinions, so I have tried to spare you too many *I think* and *it seems*.
- As a break from my predictable prose, I have extensively quoted well-written opinions that resonate with mine, and which may suggest further reading.

- Exclamation marks indicate something that is meant to be amusing or at least ironic. My jokes are often so feeble that you may need help identifying them!

The Plan of the Book

The plan of the book is as follows. Part 1 introduces the concepts that make up the main themes of the book and looks at them in the context of structure of the financial sector.

Part 2 returns to my experiences of injustice and how they led me to uncover a traditional model of justice. In the two cases I mention, the injustices may have been overcome—although leaving many other problems. The traditional model described is then used to identify some of the particular faults of the modern practice of finance in Part 3. Developing a vocation involves seeking to contribute to the flourishing of everyone in our communities, and justice is a prerequisite.

Part 4 considers ways of developing ourselves for fulfilling these vocations. This involves working on and with heart, head, and hands—which leads to personal growth in the virtues of self-control, integrity, and wisdom as well as in our particular strengths and skills.

Vocation is personal, and I do not think a useful book could be written on vocation without the author sharing his or her own experience. Forgive me therefore when I take myself too seriously, dwell too long on some issues and seem to ignore others. Your vocation will only overlap in part, but that is a consequence of it being unique.

CHAPTER 1

Vocation and Virtues

This first chapter takes a quick tour of vocation and virtue and some other related concepts.

Vocation

The first of the concepts is vocation. Vocation means calling, and the word originates in the idea that we can feel a desire to live unique and responsible lives. We can contrast vocation to the idea of a career:

One builds a *successful career*:

- By a series of achievements
- Gained by your own efforts and genius
- Rewarded by wealth and fame

On the other hand, you discover a *fruitful vocation*:

- By identifying and developing your values and strengths
- In relationships where you give and take
- Serving the community, economically and socially

To exaggerate the differences: a career may progress, but it has no aim or meaning. There are material rewards but little satisfaction, and it is likely to be lonely. A vocation has meaning and has an intrinsic satisfaction. The vocation is focused not just on the work but also on its contribution to the wider community. Economist Mancur Olson writes about the *anarchistic fallacy (1965, 130)*, which is the illusion that mutually useful relationships and structures will spontaneously evolve. A vocation intentionally builds these useful relationships in families, businesses, and government.

Finding our vocation begins by asking the question, “What do I want to be remembered for?” Peter Drucker[1] quotes St. Augustine as saying that asking this question is the beginning of adulthood. Drucker goes on to say that if you have an answer before you are 25 years old, you have not understood the question, while if you cannot answer it by the time you are 50 you have wasted your life. His advice is:

> *Developing yourself begins by serving, by striving toward an idea outside of yourself—not by leading. Leaders are not born, nor are they made—they are self-made. To do this a person needs focus* (2012, 174).

For those in the window between 25 and 50, I hope that this book will help develop the focus he speaks about.

Virtues

The virtues, the second main concept, are the personal characteristics (strengths and attitudes) that we need to develop to fulfill our vocation. They can be thought of as the equivalent of the physical virtues (such as strength, speed, and agility) that we need to develop to be better at sport. They are inherent in that we all possess them in some measure, but need training and development to be fully developed.

The four cardinal virtues are justice, courage, self-control, and prudence (or practical wisdom). Very briefly, they can be described as follows:

1. Justice means giving other people their due, and treating them fairly.
2. Courage is what is required to protect ourselves.
3. Self-control both curbs our inclinations to excess and cultivates, by practice, the habits of a good life.
4. Practical wisdom is making good decisions in the face of uncertainty, and sometimes opposition.

---

[1]This is from Part 5, Chapter 2 of Drucker (2012). Drucker has been called the “father of management theory,” and has written widely on management development.

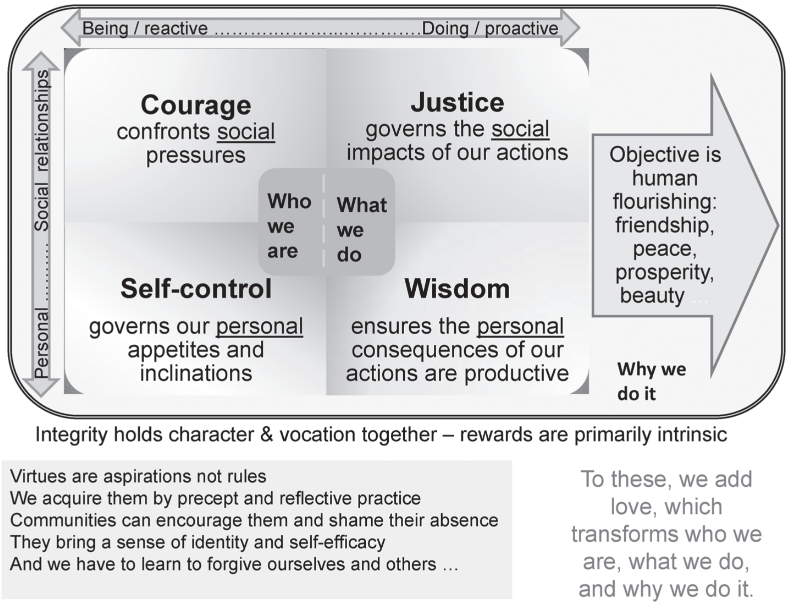

Figure 1.1 The Cardinal Virtues

We have inherited this distillation of the cardinal virtues from the ancient Greeks, Plato and Aristotle. Recent work from the field of positive psychology confirms that, while their interpretation and application varies across cultures, they are universally recognized. Katherine Dahlsgaard and her colleagues corroborate that they are found in all religious and cultural traditions, and Robert McGrath (2014) confirms it with his analysis of over a million answers from 75 countries to an online survey of values. When he uses cluster analysis on a slightly smaller sample (Table 5), he finds five clusters that can be identified with the four cardinal virtues and integrity.

Figure 1.1 represents how the virtues can help us answer the questions of who we are, what we do, and why we do it.

There is an overlap of meaning in these terms, and the words have been used in so many different contexts for so long that common agreement on definitions is impossible. The shading in the diagram recognizes this blurring of meaning. We can, however, see that the two virtues on the left (courage and self-control) are more related to influences on who we are, while those on the right (justice and prudence) relate to what we do. The top two (courage and justice) relate to relationship with others, while the bottom two (self-control and prudence) are more personal.

Illustrated by the line around the diagram, holding everything together, is integrity, the fundamental virtue. Integrity ties the four cardinal virtues together into our character (who we are), our vocation (what we do), and our motivation (why we do what we do). In particular, to work just for money falls short of integrity, in the same way as marrying or studying for money. The extrinsic motivation of money also drives out the real satisfaction of working, marrying, or studying!

The arrow on the right indicates an aspiration to building communities that encourage the development of the virtues, and allow all their members to flourish in the widest sense. The need to build community is generally recognized to be at the heart of ethical theories, and even to explain why they are necessary. The ongoing existence of the human race requires it! The idea of vocation adds the consideration that we grow ourselves as we build—so that it is not merely out of obligation that we do so.[2]

How we determine what is good is one of the main objectives of the academic discipline of philosophy, yet, for reasons I cannot explain, the virtue ethics underlying Figure 1.1 has been out of fashion in academic philosophy for a century or more. There are, however, many academics who now accept it, and I am particularly indebted to Alisdair McIntyre and David Carr's interpretation of the traditional views. Another contemporary advocate is Michael Sandel, whose book, *Justice*, introduces the topic in an accessible way. Even easier are the TED.com recordings of Sandel's Harvard lectures.[3]

The box at the bottom left of the diagram raises some other differences between virtue ethics and other theories of ethics. Virtue ethics are principles based. They are aspirational rather than a set of rules. Detailed

---

[2]MacIntyre develops these ideas in *Dependant Rational Animals.*

[3]Stan van Hooft's book gives more extensive coverage, showing also that there is a wide range of interpretations of virtue ethics. The structure shown in Figure 1.1 is my way of thinking about the virtues—and linking them to ethical behavior (deontological theories) and outcomes (teleological theories). Following what I understand of McIntyre (and Christian tradition), virtuous people want to, and often do, good things and achieve good objectives. It is not possible to determine which comes first, or to prove anything is good or virtuous from first principles. Ultimately we seek views that are reconcilable to each other.

regulations have too many exceptions, too much detail to remember, and are too prone to rationalization. They can also be used to dominate others and foster resentment and resistance. Following virtue means working at the pursuit of a fruitful vocation rather than feeling guilty for failing ethical rules. We return in Part 4 of this book to a more detailed consideration of the virtues and how to cultivate them.

Forgiveness

Of course, we often feel remorse. I am continually astounded at my failure to do the right thing. At the age I am now, I had hoped to be more in control of my actions. I know there are others over 50 who read the Drucker quote above and feel, like me, a bit of a failure! The third main concept, therefore, is the ability to forgive: the grace to continue to try after failing. It is a difficult tension: we ought not treat our faults too lightly, but have to find a way to live with them.

Epicurus, a Greek philosopher, apparently said, “Consciousness of our errors is the first step to salvation.” If he is right about the first step, the second step is to find forgiveness—from those we have wronged, if possible, from ourselves and, if we are believers, from God. Books on ethics—even by virtue theorists—often do not address this question, perhaps because the religious element makes it difficult in a pluralist society. We are being unrealistic, however, if we avoid addressing failure.

Forgiveness is seldom easy and some crimes may seem impossible to forgive. The South African Truth and Reconciliation Commission, and others like it, have, however, shown that people can forgive unspeakable crimes. Such reconciliation requires the right environment and an ability to forgive, which is a virtue beyond the cardinal four.

Empathy

There is a close link between how we treat our own faults and how we respond to faults in others. The fourth and final main concept is empathy—using your imagination to put yourself into another person’s shoes.

Empathy starts with recognizing our own feelings and prejudices, and realizing how we tend to deny them. Denying our feelings could be described as a lack of emotional integrity, causing us to miss hidden drivers of our beliefs and actions, and making it difficult to control them. Observing our own motivations, on the other hand, is a lens that helps us see and understand what others are thinking and doing. A virtuous spiral is set in motion as we strive to understand others better, and begin to understand ourselves better. Empathy leads to community, and supports tolerance and forgiveness.

Heroes and Heroics

While I would like to share some of my indignation at injustice, let me caution against heroics. Allowing anger to become all-absorbing is unhelpful and taking controversial stands can be costly—financially and physically. Philip Jos and his colleagues have catalogued some of the costs of whistle-blowing. Patience is not the same as compromise; it can give you time to discover more creative solutions to issues that concern you deeply—that may well be more effective, as well as safer.

In trying to think of examples of the heroes who have made finance their vocation, I had some difficulty thinking of anyone who had made a huge difference. So many of the well-known figures have feet of clay. But our modern world could not have been built without the bankers and investment managers who have helped mobilize capital, and many more people would have ended their lives in poverty without insurance and pension arrangements. These institutions have been built and are maintained largely by groups of people who have done good work throughout their lives. It would be an exaggeration to call them all heroes, but many are professionals who are working out their vocations—virtuously.

If you are tempted to heroics, remember that none of us has the obligation to save the world, and it is a little arrogant to think you can. Vocation is for the long haul. Jesus was 30 when he began his public activities; Moses, Mohammed, and Gandhi somewhat older before making their unique contributions. The older and more experienced you are, the more likely your stand will bear fruit. In my 20s, I was influenced by a quote from Theodore Roszak (1972, 61), "Nothing counts more heavily against the technocracy than a successful desertion, for there is no underestimating the influence of an authentically happy disaffiliate . . .". I still like the quote, even if I rather wrested it out of context and cannot really recommend the book. It suggests you have to have participated in a system to understand it, before you can really transform it.

There are those who are called to be heroes, but it is beyond me to make the call. If there are older readers of this book who are financially secure, there may well be places to be brave, and even radical. It is the responsibility of older men and women to take the uncomfortable stands—and to preserve the young from untenable pressures, such as being sent into the trenches or on suicide missions.

Chapter summary: The virtues include the self-control and courage that make us who we aspire to be; and the justice and wisdom that would direct our actions in ways that we would want as members of flourishing communities. Integrity holds the virtuous character together with a meaningful vocation. But, as we will fall short, we need to be ready to forgive ourselves and others. We do not have to be heroes.

CHAPTER 2

What is Not Covered

This book will disappoint you if you are looking for precision, academic debate, or grand theory—or solutions to difficult ethical problems.

Precision

Whether we like it or not, we live in a state of considerable ignorance about ourselves and every aspect of the world around us. We cannot therefore be dogmatic or altogether confident about anything, let alone the admittedly subjective areas of ethics. I have not even tried to be too precise or prescriptive, and have doubts as to whether it is possible.

We cannot live, however, as if we are in a state of total ignorance. We must live as if our understanding is adequate. This applies to cold facts and to theories as well as to what is best for us. It seems it is impossible to give logical proof for either of these. We accept both facts and theories when they seem to cohere. We build our view of the world as our experiences support and affirm each other. It is a bit like our granddaughter making sense of her world at 4 months. She has learnt to respond to a few words, like "Mummy" and "roll over." There is no logic, no grand narrative. Even though we have a significantly greater experience and vocabulary, it is only relative! Progress comes from extending our experience and making it fit together better.

Further precision may be unnecessary and unhelpful. Consider, for instance, the concept of gross domestic product (GDP). Many academic papers use it with great precision, rigorously exploring mathematical relationships with other precise ideas. One of the grand narratives of our time effectively holds that the GDP is the measure of all things of value. For purposes of this book, however, I use expressions such as *prosperity* or the *common good*. They are much less precise, but perfectly adequate for the meaning I want to convey. GDP is also an arbitrary concept (that depends on the definition used by the organizations collecting the data) and the appearance that it precisely measures anything of importance is misleading.

Please therefore forgive the absence of precise definitions. You will have to find them in other books. Where I skirt deep matters in a few sentences, it is because I am trying to place them in context rather than make them plain. The Internet means that you can easily search for explanations and arguments that are more rigorous.

Academic Schools

With a few exceptions, I have intentionally avoided discussion of different academic schools of thought, especially where the theories are not embodied in a community of practice. There is just too much to debate and this book is not the place. The academic literatures on education, psychology, politics, management, and economics are fragmented, with dozens of schools each with their own assumptions and vocabulary, minimal cross-referencing within their discipline, almost no relevant cross-disciplinary discussions, and sometimes no reference to practice.

I admit too that I am seldom qualified to give an expert opinion, and often have difficulty in identifying important contributions—rather than those that are merely cited often. In such cases I have relied on those who claim expertise and whose ideas resonate with the traditions and authors I find convincing.

Alisdair MacIntyre's *After Virtue* provides a more thorough justification for this type of approach, but he sets out the need to engage with alternative traditions of practice. I do therefore attempt to address, in Chapter 6, the positive economics that informs much of current practice in the financial sector.

Grand Narratives

Most thinking people are suspicious of grand narratives, whether religious or secular. Those who adopt them too enthusiastically can be dogmatic and judgmental. Nevertheless, we necessarily have a set of assumptions and explanations of what we are, and how and why we are here. MacIntyre makes the point that our thinking has to be based within some tradition of rationality and value.

The ideas in this book are compatible with a range of traditions or worldviews—religious and secular. Many religions value the cardinal virtues, while many secular worldviews also see virtues such as sustainability, democracy, and tolerance, or concepts such as human rights as being of fundamental value. My views are, however, not compatible with worldviews that elevate material progress to the greatest—and sometimes the only—value.

I should disclose my own beliefs so that you can allow for them. As to religion, I am a Christian, in the Anglican tradition, but with no strong denominational loyalty. Different religions and traditions often converge on ethical questions, and I have referred to mine because they are familiar to me. Where there is divergence, and especially from those with no religious beliefs, I need to ask for your indulgence. Please take my references to God as metaphors for the greatest good—however you conceive it. As to my politics, as with many Christians, I tend to the right on social issues including liberty, and to the left on matters of redistribution. My professional training, though, is perhaps more relevant to the subject of this book. The principles of professionalism of the International Actuarial Association set out standards of integrity and competence, and a responsibility to the public to which I aspire. In particular, this means attempting to contribute to the development of the *Regulatory Capitalism* discussed in Chapter 10, which means that I accept the overall logic of modern mixed economies.

Alternative Ethical Theories and Difficult Problems

One cannot write a book on ethics without some consideration of the different philosophical schools. You do not have to agree with everything they write to find that the well-known writers offer useful insights. These include Aristotle, Augustine, Aquinas, Smith, Hume, Marx, Kant, Rawls, and Sen. To the extent that they have followed their passions and competently addressed the issues of their time and place, they can be said to have followed their vocations—and many of the differences can thus be explained. Similarly, to the extent they have allowed their interests to reduce the scope of their vision, and to develop novel insights that are irreconcilable to traditional virtues, they are to be mistrusted. MacIntyre suggests that they fail when they attempt the impossible task of justifying why we call something good by looking for universally agreed principles that do not exist. He suggests that the traditional views justify themselves in a community of practice:

> *When . . . the tradition of the virtues is regenerated, it is always in everyday life, it is always through the engagement by plain persons in a variety of practices, including those of making and sustaining families and households, schools, clinics, and local forms of political community (2007, xv).*

While there is widespread recognition of the need for regeneration, there is also a tradition of the virtues in a number of communities of practice in modern mixed economies—especially within the professions. This book is an attempt to contribute to such regeneration within the professions and more broadly.

MacIntyre is clear that some theories are unlikely to help. These include *deontological* theories that are focused only on whether the actions themselves are right or wrong in themselves and *consequentialist* theories that are limited to whether the outcomes are right or wrong. The best known of the latter is utilitarianism, which is concerned with the benefits of the greatest number.

Many other books on ethics provide difficult ethical problems for discussion. By difficult, I mean cases where ethical considerations are in conflict with each other, and the right ethical response is not clear. Some theories of ethics and ethical education—notably those of Lawrence Kohlberg—hold that our personal ethical development requires that we think about difficult problems. Working through them, especially if real case studies are included, probably does help us understand the world better—and encourage us to make better ethical decisions. Recognizing the right thing to do, however, is, in many cases, not that difficult if we are committed to developing the virtues. This book is intended to help in identifying them and integrating them into our personal stories.

Difficult problems often have no right solutions and leave us with tensions, some of which we will discuss.

As discussed earlier, developing rules for all cases is onerous, and not necessarily helpful. This is why casuistry, which is the science of developing ethical rules for particular cases, has mainly come to mean "the use of clever but unsound reasoning, especially in relation to moral questions."[1] We also talk of the "dead letter of the law," which is what it feels to be over-regulated. We return to this question when considering risk management in Chapter 9.

Training in Virtue

Education in the virtues takes a different route, as explained by David Carr, philosopher of education. He—perhaps rather crustily—laments current failures in education:

> *. . . no really rational being could understand fully what a quality like courage, temperance, justice or compassion is and yet fail to want to possess it. From this point of view, since the virtues are not innate but entail both proper habit formation and the development of reason, it is clear that it is squarely within the responsibility of all concerned with the socialisation and education of children—parents, teachers and others—to ensure that such habituation and instruction takes place.*
>
> *There are legions of young people, who . . . continue to perceive what is admirable about virtue through the fog of lies that have been woven about her, and live lives of self-respect, decency, sobriety and genuine altruism. There are far too many others who have been blinded by the rhetoric, who have come to believe that morality is a matter of reluctantly doing one's duty where this cannot be avoided, and otherwise going to the devil* (1991, 255).

This book is intended to help clarify the shape of virtue and vocations, and identify those elements of the financial sector that need changing

[1]Oxford Dictionaries.

for it to fulfill its role in a flourishing society. It hopefully makes some contribution to beginning Carr's "habituation and instruction," but that role is played within a community of professionals. I would thus urge everyone to join an appropriate professional group that will encourage both technical and ethical development. Apart from the accountants, actuaries, and investment managers, there are International Associations of Business Communicators, Financial Executives, and Human Resources and more. There is also great value in Mary Gentile's book and program: *Giving Voice to Values*.[2] In it she gives useful guidance for preparing oneself and practicing to develop the voice of reason and live up to the virtues in difficult situations.

Chapter summary: There are many different theories that relate to ethics, but developing our character and vocation may not be helped by intellectual debate. Developing the virtues takes place as we aspire to develop them in communities of practice.

[2]Accessed November 24, 2014. http://www.babson.edu/Academics/teaching-research/gvv/Pages/home.aspx.

CHAPTER 3

An Overview of the Finance Sector

We now take an overview of the structure of the financial system, the function of which can be described as the management of savings and capital and the provision of financial security. First, there is a quick outline of the structure, then some discussion of what shapes it and the challenges this creates. The final section considers the wider question of change in the industry.

The Structure

Figure 1.2 provides a helicopter view of the modern financial sector. It consists of two rotors (of the helicopter) representing the liability and asset sides of the sector. The function of the liability side on the left consists of the provision of security of savings and income, and involves the mobilization of capital, being money that people have saved. The asset side allocates this capital to businesses for investment and to families for housing. These important social functions need to be just if people are to trust the system. This trust is required for the system to be effective, efficient, and robust to system-wide risks.

The two sides are interlinked. The generosity of the benefits depends on the yield on the assets. The control of the assets (and therefore the governance of much of the economy) and responsibility for the liabilities are intertwined. Working on one side can have unintended perverse consequences on the other—some of which we will discuss in Chapter 10.

I assume that most of my readers will be familiar with the function of insurance companies, retirement funds, and banks, so will not expand on

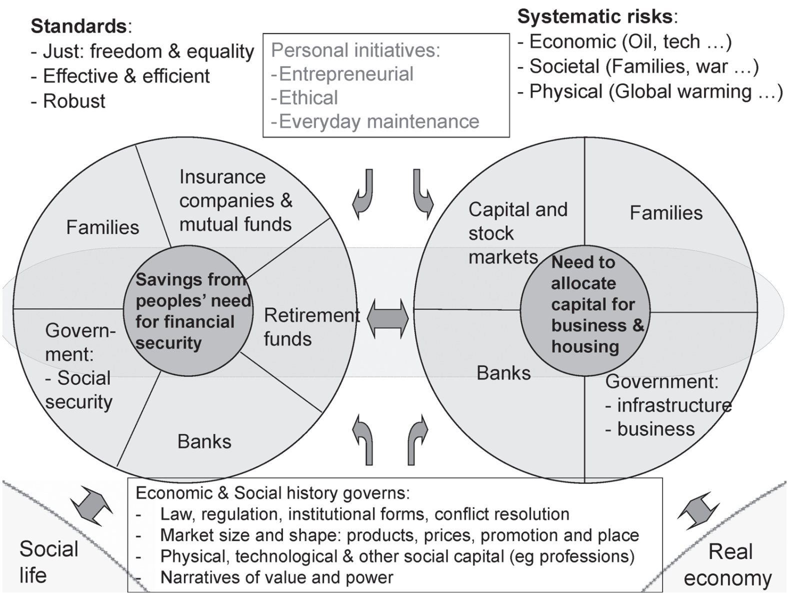

Figure 1.2 The Structure of the Financial Sector

their roles. The role of families and governments are, however, not always appreciated although their functions are in many ways interchangeable with those of the private sector institutions—and their relative size can differ significantly in different societies.

Families (often extended) appear on both rotors: they mobilize capital, provide financial security to each other, and apply the capital for housing, cars, and other consumer durables. I like to compare marriage to a whole life insurance policy: it requires a proposal, has an entry date, it includes economic and disability benefits ("for richer, for poorer, in sickness, and in health") and it is "until death do us part." Like an insurance policy, it also requires regular payments, and you lose enormously when you surrender it! Agriculturally based families are more likely not to move around, and so to stick together. They are therefore more likely to provide financial support to poorer relatives especially in old age.[1] Large families can obviously provide better financial services than smaller ones. The financial role of the family may grow when populations are growing and there are many living relatives. Today, with smaller families, often distant

[1]See Steven Ruggles's research on extended family living arrangements.

from other generations, the financial role of the family must be smaller than it was in earlier times. This provides new challenges for retirement and health systems.

What Shapes It

The social and economic forces and institutions that shape the system are mentioned in the box at the bottom of Figure 1.2. They are governed largely by history, as can be seen by the variety that exists around the world. They are not, however, accidental to the extent that they have been shaped by different people's initiatives over the years, and they can be changed in the future. Our personal vocations can lead to each of us playing a role in shaping them. Our personal initiatives therefore have a special box at the top. We can all make a difference even if we are *only* involved in the everyday maintenance of the system. It is in the nature of the system to deteriorate: the physical and legal infrastructure may not change, but the people must do so—at least because of the process of aging. At very least, newcomers need educating!

Formal Systems

Even if you are a new worker, you can observe systems at the lowest level: documentation and the following of formal procedures. There is always the temptation not to document the work fully, for new consultants not to record their hours (and minutes) appropriately, and not to follow procedures. I am not suggesting that all formal procedures are necessarily efficient—far from it—but that they provide material for learning and a base for improvement.

Some readers may be inclined to dismiss formal structures. My experience in South Africa convinced me otherwise. Without formal structures, efficiency is low because the division of labor and economies of scale are minimal, and because delegation and contracts are verbal and difficult to enforce. The absence of records limits access to credit and insurance. Without formal dispute resolution mechanisms, people can resort to violence to defend their interests. Literacy, numeracy, and schooling are less valued—and skills less likely to be passed on. The smaller tax base is a further problem.

Without going into details, it is perhaps worth mentioning *Institutional Economics* as a branch of academic study that investigates these issues, and a branch of sociology, *Structuration Theory*, that considers the impact of individuals on the structure of organizations. By structures, I include legal contracts and also the products and services that are sold. Structures do not spontaneously evolve. People change them—sometimes motivated selfishly, sometimes for the *common good*, and most often with a combination of both. Of course the structures we create as part of our vocation may not last long, but it is like farming or gardening: none of the plants are permanent, but good planting and pruning can produce much pleasure!

The Common Good

The *common good* of course includes the interests of the entire planet, but I use it here in a more limited sense as it justifies and explains the functions of institutions. The institution of property rights is one example that addresses the *tragedy of the commons.* The *tragedy* describes a perverse, often informal, institution that involves the destruction of common assets because of the free rider problem. If every fishing company attempts to maximize its take, they will soon exhaust the fishing grounds. If, however, they are given property rights (limited quotas), then it is possible to manage the catch to ensure its sustainability.

It is not that easy to create suitable institutions. Vincent and Elinor Ostrom are renowned for their work on managing the commons—Elinor being the first woman to win the Nobel economics prize for 50 years of careful observation and analysis of institutions that work, and those that do not. I like Vincent's summary of the alternative forms of institution in his book on democracy:

1) Autocracies . . . are not appropriate systems of government for the future of . . . civilization.
2) Bureaucratic reliance on a unified system of command . . . cannot be used to achieve lawful, trustworthy, and mutually productive relationships.
3) A single, comprehensive . . . code of law . . . is an impossibility.

4) The enduring and creative potentials of human civilizations are associated with self-organizing and self-governing patterns of relationships that are crafted with shared communities . . . that are built on standards of rightness, justice, reciprocity and mutual trust (1997, 264).

This argument for democracy is not because it is more effective or efficient. Autocracies may well be more effective in times of crisis. The earliest democracies appointed tyrants to command them in war. Autocratic states can also produce huge economic gains—as has been the case in China over the past 25 years. The argument is rather one of the values of personal autonomy, mutual respect, and a community of relationships. It assumes that everyone has a contribution to make—and a vocation to develop.

Elinor Ostrom sets out eight principles for the creation of a system, and sets out ways of addressing the free rider issue. They can be summarized as follows:

1) Define clear group boundaries.
2) Match rules governing use of common goods to local needs and conditions.
3) Ensure that those affected by the rules can participate in modifying the rules.
4) Make sure the rule-making rights of community members are respected by outside authorities.
5) Develop a system, carried out by community members, for monitoring members' behavior.
6) Use graduated sanctions for rule violators.
7) Provide accessible, low-cost means for dispute resolution.
8) Build responsibility for governing the common resource in nested tiers from the lowest level up to the entire interconnected system.[2]

They incorporate principles of democracy (3, 5, and 8) and ways of dealing with free riders (6 and 7) in ways compatible with the *restorative*

[2]Accessed August 30, 2014. http://onthecommons.org/magazine/elinor-ostroms-8-principles-managing-commmons.

justice that we will discuss later. They deal with non-economic goods such as protection against crime and the provision of public health and education. They also provide a template for developing our vocation—particularly where it contributes to the *common good*. These principles underline the importance of institutions, and why they should be designed to bring out the best in people.

This model provides a potential solution to the conundrum of power set out by Lord Acton's, "all power tends to corrupt but absolute power corrupts absolutely." John Braithwaite's (1998) paper on institutionalizing distrust points out that we cannot rely on some supreme authority to take responsibility for *common goods*, so there is a role for all. As he says elsewhere:

> *Guardians such as auditors are recruited to catch abuse of trust. But what if the guardians are untrustworthy? The only answer can be another layer of guardians above them . . . But if the n+1th (ultimate) order guardian is corrupt, the whole edifice of assurance can collapse. . . . (There is. . .) a simple solution to the puzzle. Arrange guardians in a circle and there is no infinite regress. The logical structure is that everyone becomes a guardian of everyone else* (1999, 92).

There are self-interested reasons for participating in this mutual accountability that includes democratic process, Drucker—who lived in Germany during the rise of Hitler—warns, "If the decent and idealistic toss power in the gutter, the guttersnipes pick it up" (1992, 244).

There are many institutions in the financial sector that serve the *common good.* Apart from the law and the courts, there are the professions and industry bodies, a range of government regulators and ombuds, as well as universities and research initiatives. We contribute to our vocation in the development of any one of them.

Rules of the Game

For the last line in the bottom box of Fig 1.2, *narratives of value and power*, I was persuaded by William Baumol's exploration of what he calls the *rules of the game*, which go beyond the legal environment:

> *If entrepreneurs are defined, simply, to be persons who are ingenious and creative in finding ways to add to their wealth, power, and prestige, then it is to be expected that not all of them will be overly concerned with whether an activity that achieves these goals adds much or little to the social product or, for that matter, even whether it is an actual impediment to production* (1990, 897).

He goes on to point out that the rules of the game have differed significantly over time and place. Many societies have valued wealth from land rather than business. Relevant to us is the high income and status that workers in finance have enjoyed in the last 30 years or so. The question raised is whether the positive social and economic benefits of the financial sector justify its size and profitability. He goes on to suggest:

> *The allocation of entrepreneurship between productive and unproductive activities, though by no means the only pertinent influence, can have a profound effect on the innovativeness of the economy and the degree of dissemination of its technological discoveries* (1990, 898).

Unproductive activities include the pursuit of monopoly rents and participation in vice industries: tobacco, drugs, and pornography. We will return to these in Chapter 6 when we discuss overcharging, in Chapter 7 when we discuss socially responsible investment, and again in Chapter 11, when we look at what we can do for the poor.

There are those who would like to see radical changes to the financial system, often with considerably more government intervention and control of capital. Dan O'Neill and colleagues are particularly concerned with resource limitations and a one eyed focus on growth. I share their views on ensuring we preserve the environment for future generations, but am less enthusiastic about centralized control.

If you agree with the values set out in this book, it follows that we all have a role in changing the *rules of the game* so that they value creativity and human flourishing—rather than the extraction of rents by overcharging and over-servicing, self-interested lobbying, the avoidance of taxes and environmental destruction. These values have to be taught in school and university, incorporated into news, film, book, and other media, and espoused by politicians. We can all espouse such rules at dinner table conversations and family gatherings—although take care your spouse is not too tired of your limited repertoire! Part of this process will need to be lobbying against the common interests of management—identifying self-interest for what it is, and making it easier for politicians, in Adam Smith's words, to face the "insolent outrage of furious and disappointed monopolists."[3]

Where the Sector Needs Changing

There are many who are uncomfortable with the industry's claims to expertise given its huge losses recently, and its apparently disproportional power. Alain Cohn and colleagues have even found some evidence for this in their recent research.

Puffery

John Braithwaite, who has experience of a wide range of industries, is one who is particularly critical:

> *New York and London created capitalism's badlands by promoting the idea that risks were things smart people shifted rather than controlled and accepted responsibility for. . . . New York and London have the most sophisticated business oligarchy in the world. It does not rule mainly by stuffing dollars into the pockets of politicians, though it does do that. It rules mainly by bluff and hegemony, by persuading political elites that it knows what it is doing. Politicians did not understand the bankers' risk management models, but they believed their incredible sophistication was helping to extend the boom and cushion the busts of previous business cycles. The financial oligarchs did not understand them either; the models were just a good story that they bought from economists who were happy to be well rewarded for not talking too loudly about their shaky assumptions and the gaps in what they were able to quantify* (2009, 440).

[3]The context of this quote can be found in the quotes from Adam Smith in Chapter 6.

This is a generalization, but nevertheless helpful in identifying the bluff.

Structural Reforms

There would also be advantages in structural changes to the industry, some of which are explored below. The centralization of power in the financial sector does not seem healthy, and there are many calling for the breakup of institutions that are too big to fail. One does not have to wait, however, to begin working on demergers or setting up independent competitors to the giants. Some of the organizations mentioned on the following pages are more radical than others, but many will be fun and productive places to join. Professional and community groups can also be helped to make an independent contribution.

Chapter summary: The financial sector exists to provide financial security to people and to allocate capital efficiently. Developing formal institutional structures can create c*ommon goods* that benefit a wider community. The financial sector also follows informal *rules of the game* that also can be changed.

PART 2

Clarifying Justice

If justice is the virtue that should form our treatment of others, how does one go about developing and applying a model of justice that can identify injustices in the financial sector? Part 2 speaks from my experience of community, working with people against injustices. It relates both to the need to respect others and to the creation of a flourishing community: both what we do and why we do it in terms of the structure in Figure 1.1. I start with the problems of apartheid with which we grappled in South Africa as they provide concrete examples of the principles, and it is the best way I know to explain them and their importance. Moreover, few countries do not have a growing underclass of ill-educated and marginalized groups, whom we consider in different places in the book, and to whom we return in more detail in Chapter 11.

CHAPTER 4

My Personal Experience

I am, originally, a white South African, who has worked in finance all my life. On either score, this would be enough—in the eyes of some—to be fatally compromised and incompetent to write about ethics! I cannot even claim to have really appreciated ethical issues until my early 20s, nor to have been particularly effective in addressing them since. Worse, I have retreated from both: living now in Australia and working in academia. All I can claim is that there is evidence that I have some reputation—at least within the actuarial profession—for my enthusiasm for ethics, and appear to have encouraged some of my students and colleagues in their ethical walks.

Apartheid

My experience of apartheid and its demise not only explains much of my own worldview. It is also relevant in many ways everywhere we face compromise.

I should have been sensitized earlier to the injustices of apartheid. My grandmother was one of only 5,000 members of the Alan Paton's Liberal Party[1] that took the strongest stand (among whites) against apartheid in the 50s. Home, school, and church taught it was wrong, but it was only as a university student at an Anglican Student Federation (ASF) conference that I began to feel the injustice. The ASF was at the time the only student organization in South Africa that had not split on racial lines, and its 10-day annual conferences were as emotionally intense as you can

[1]Alan Paton was also internationally known for his book: *Cry the Beloved Country.* The Liberal Party was the only registered party that had a multi-racial membership.

imagine. I have memories of frequent tears (from white and black) and enormous warmth, especially from black people who had forgiven whites for their mistreatment.

But as they would have said, tears were all very well, but what will you do? One obvious action for your academically minded author was to become better informed. I read the reports of the Study Project on Christianity in an Apartheid Society (SPROCAS). These were a careful analysis of racial oppression in South Africa and the possibilities for reform, written by some 150 intellectuals—largely white and Christian. Perhaps because SPROCAS had no influence over the government, or because of the growing influence of Steve Biko and the black–consciousness movement,[2] the main conclusion was that blacks would win their own liberation.

But individuals did seek to find ways of confronting injustice. Some of my friends became conscientious objectors against compulsory military service. One of them, Peter Moll and I debated the issue in *South African Outlook*[3], a magazine edited by Francis Wilson, one of the SPROCAS academics. Peter felt it was unacceptable to participate in an institution that enforced apartheid laws; I felt that a conscripted army was more likely to prevent South Africa falling into greater anarchy. He spent a winter in his underpants in a military prison, while I enjoyed four course meals in the officers' mess. I may have been right, but his courage and sacrificial stand inspired a number of people to follow his example, and undermined the confidence of the apartheid regime, probably contributing to its ultimate surrender. In retrospect, I think that they were too young to have been making these sacrifices, but I salute them for doing so.

Other friends joined churches or worked in legal, medical, or other organizations serving the poor in various ways. (The term poor is particularly imprecise, but carries enough meaning for my purposes.) Some, particularly those who worked with the trade unions, were Communist rather than Christian. Many of my contemporaries who pursued conventional careers also devoted significant time or resources to service. Others

[2]Steve Biko held that black people had to assert their own identity and freedom; it could not be done for them.

[3]South African Outlook October, 1979, pp. 153–155.

worked hard at exposing apartheid supporters in the government to the pain that their policy was causing. We felt we were not as effective in our service or opposition to apartheid as we might have been, but I am not sure what we might have done otherwise.

It is difficult to question the society and structures in which we have grown up—more so without peer support. I have a vivid memory of the physical shock shown by an Afrikaans woman, with whom I was dancing in the officers' mess, when I cracked a feeble joke about supporting the official opposition party. We had met at a bible study and, university graduate though she was, it was inconceivable to her that a Christian would not support the apartheid government.

The wonder of the South African experience is that change happened. Most important of the causes was probably the fall of Communism in Europe. This meant that the apartheid government could not rely on Western support to the extent previously, or the communist bogeyman to rally internal support. There was also significant internal opposition, not least the silent witness of Nelson Mandela. In my mind, however, Desmond Tutu personified the active opposition. I saw him close up as I sat on the Anglican Church investment committee that he occasionally chaired, and helped with a conference on sanctions/boycotts that he sponsored. He exemplifies many of the virtues to which we can aspire:

- He foresaw and had announced the demise of apartheid at least 10 years before it happened. It was perhaps foolhardy to make predictions, but it unsettled many to good effect.
- He used his personal confidence to challenge and charm. One of his favorites was laughing about how he had won over apartheid supporters by asking, "So, has a kaffir[4] ever talked to you like this before?"
- He used his profile in the United States to raise awareness of the anti-apartheid struggle and raised large amounts of money, which he used to fund a large share of the church's budget in Johannesburg when he was bishop there.

[4]A term often intended to be insulting, like nigger in the United States.

- He worked enormously hard at relationships. I was told that he might have 150 postcards ready for posting before breakfast.
- He was prepared to confront at all levels where necessary: from governments across the world to priests neglectful of their duties.
- His strategy of attacking the government's moral foundations with the statement that "apartheid is a heresy," and the promotion of economic and sporting boycotts were more effective in weakening the government's resolve than the ANC's external armed struggle—and the internal school boycotts which were self-harming.
- He then chaired the Truth and Reconciliation Commission, showing amazing compassion to many who would have previously vilified him.

He shows integrity, justice, courage, wisdom, and love.

Unfair Pension Fund Withdrawal Benefits

My personal response to injustice was work toward institutional reform in the pension industry, where I made my stated—though outrageous—aim try to make every South African as secure as the Swedes in their old age!

In 1987, the premium paid in a takeover of my employer put my share options well into the money, and allowed me to go on a few days retreat and think. What did I really want to be remembered for? One result was that I became an occasional actuarial advisor on retirement issues to black trade unions. (Apartheid split trade unions on racial lines.) They were in the process of negotiating their exit from defined benefit pension schemes, which were then in surplus (except for a short period after the October 1987 crash in the stock market). I felt that the unions were being exploited by their financial service providers (and other actuaries), who were serving the employers rather than the trustees and members of the fund. In particular, they were creating surpluses for the benefit of the companies and largely white managers. I offered to help the unions protect their financial interests, and to use the opportunity to address the question of unfair benefits—one of the items identified on my retreat.

I was already angry about unfair early withdrawals from pension funds. I saw the funds as compulsory savings vehicles, and thought that benefits ought to bear some reasonable relationship to the contributions. I later discovered that economists call this relationship *actuarial equity*. South African defined benefit funds of the time calculated withdrawal benefits by accumulating the employee's contributions at an interest rate of 2½ percent p.a. when investment returns were over 15 percent. The longer you had been a member, the more you lost, with the losses compounding. The ratio between your savings accumulated at 15 percent and what you actually received on withdrawal would be 1.8 after 10 years, 4 after 20 years, and 10 after 30 years. Any employers' contributions were also lost on withdrawal, which meant that you might lose 95 percent of your expected benefit it you withdrew after 30 years.

Many of the funds were employer based, so one was forced to take the withdrawal benefit when changing jobs. Few people could afford to do so if they had accumulated 20 years of service. Social security pensions were set at less than 10 percent of average wages in the formal sector, so a number of older people I knew were locked into service with their employer. I would like to say that it was their predicament that made me angry, but I am afraid a lot of it was indignation that I was being forced to contribute for minimal value—as I did not expect to stay at one employer for my entire career.

Senior actuaries responsible for the management of these schemes told me that:

- Members who withdrew were free to make their own decisions.
- They had never been promised anything else.
- The trustees were bound by the rules of the fund and these depended on the employer.
- Members would not save otherwise, so a little savings with poor returns were better than no savings at all.

They did not intend the last explanation to be facetious. Many who work in pensions funds think paternalistically. Many academics and policymakers believe that people are myopic—and regulations should compel, or at least strongly persuade, them into saving more. They may have a point, and surveys show compulsory contributions are politically popular. There are those in the industry, however, who persuade themselves that they are doing good things for the members, and seem to have accepted the *status quo* uncritically and unconsciously. It is difficult to suggest changes that your clients or employers find objectionable. I have felt at times that they do not even hear criticisms of their actions, unless forced to by circumstance. But, we are all capable of this type of blindness.

Others in the industry were not happy with the rules I have described—even if they did not express the problem as one of justice or fairness. My first pension fund paid me a reasonable withdrawal benefit as early as 1982. Some people had spoken up and made changes; but there were people who knew better and did not take a stand.

The work for the trade unions proved not to be full time, so I also became an academic. This allowed me the time to research the topic of justice, finding academic work that resonated with mine, refining my thoughts and better managing my feelings of indignation. I also became involved with retirement-related policy matters through the Actuarial Society of South Africa. I worked my way up from the profession's Pension Fund Committee to the government Advisory Committee on Pension Funds. In the early 1990s, employer groups approached both these committees asking them to support legislative changes allowing the refund to employers of pension fund with surpluses. The surpluses had emerged from investment returns as well as the unfairly low withdrawal benefits.

This request provided me with the opportunity to persuade fellow committee members that refunds of surplus to employers would be acceptable—if companies were prevented from manufacturing surpluses by encouraging or forcing withdrawals from the funds. Those uncomfortable with the unfair withdrawal benefits saw it as opportunity to correct the unfairness. The committees' advice provided the seed that led to reforms in 2001 which imposed minimum withdrawal benefits on all retirement funds. When this advice eventually got to parliament to become legislation in the post-apartheid government, the power of the business lobby had reduced significantly. The new legislation provided for the refund of surpluses to all those who had previously been disadvantaged by poor withdrawal benefits going back 20 years. I understand therefore that members have received most of the R50 billion in surpluses that has been repaid.

I had the satisfaction of reading that one of the *ad hoc* tribunals appointed to oversee disputes about surplus wrote, "It is apparent that much of Asher's thinking was incorporated into the legislation."[5] I must say I do not know how. I had written papers and argued for the principles at every possible occasion for over a decade so my views were well known. It was, however, other people, some unknown to me, who drafted the legislation and steered it through parliament. I salute them.

Apart from forcing me to clarify what I meant by justice, the learning from this experience was that perseverance and imagination can overcome many apparently immovable injustices. It provided confirmation Olson's *anarchistic fallacy*: far from evolving spontaneously, social institutions and regulations may require considerable effort to change.

Living with Tensions

So what of the tensions through which we have to learn to persevere? We used to say that South Africa was a microcosm of the world. We meant that third-world poverty was on our doorstep. I still agonize at the young man who had done a small paint job in our home and who I sent away after he asked to live in our garden tool cupboard. A baby's cot would not have fitted in it. Although I had no idea how to help him, I felt so guilty that I went looking for him 5 minutes later, but he had gone. Our youngest son once asked why we did not give to all who begged. My wife and he then counted 170 beggars on a half-hour trip across Johannesburg. I could go on.

We did give money to organizations, employed as many people as we could (jobs being better and more appreciated than handouts), but still lived a comfortable lifestyle. We justified the lifestyle to ourselves with the argument that we had an obligation to give our sons the education that we had enjoyed, and that I would not have been able to keep my job if

[5]Ad Hoc Tribunal consisting of J. F. Myburgh, M. W. Lowther, and E. W. Fagan—appointed to rule on the apportionment of surplus of various Shell pension funds. pp. 98–101

our lives had been disrupted by being open to all who had needs. But the money that we did give seemed so often to have limited effect. Perhaps, it was something in our attitude, or it arose from the distorted relationship that can develop between those who give money and those who receive, but our giving was often not fruitful. In summary, we regularly felt guilty and helpless in a sea of poverty.

One ought not to wallow in such emotions. While we need to feel the real pain of those around us—and those further off—there are also times for celebration. I learnt this poignantly in Cape Town in the early 80s. At that stage, apartheid attempted to prevent black people from the rest of the country coming to live or work in the Cape. The few who managed to get in were deported back to their homelands, where population growth had made subsistence farming increasingly unviable. A group of us from the church were asked to observe a situation outside the city. A group of Xhosa women had set up a makeshift camp, and the police had arrived with a view to demolishing their camp and deporting them. It was felt that the presence of white church people might prevent the deportation, or at least ensure the use of minimal force.

The scene was dramatic. Twenty or so women had created simple frames with plastic covers to keep themselves from the wet Cape winter. They were warming themselves around an open fire. Three police vans were parked at a distance, with a group of police standing near them. The sky reflected the polarity: the black cloud of a cold front coming up from the Southern Ocean covered the one-half; the other half the deep blue of the late afternoon. The women, however, were singing and dancing round the fire, not sullenly nor fearfully, but apparently delighted in each other's presence (and perhaps grateful for ours), and with all the gusto in which their culture excels. I cannot remember what happened afterward, but what I gained from them was permission to celebrate in the face of adversity.

Life contains a number of these tensions with disappointment, failure, pain, and death. In one way, we have to deny them—at least for a time. Popular psychology recognizes denial as one of the stages of grieving. When the father of a good friend died, we spent the evening talking. He spoke mainly of his father—in the present tense. There was no question about the death, but there were levels in my friend's subconscious not yet ready to acknowledge it. Denial gives us a chance to come to terms with reality bit by bit. There are unfortunately, people who cannot face new reality after loss and live in a make believe world. We all, however, probably have to protect ourselves by denying much of the pain and suffering around us. As children, we mercifully do not have the capacity to see a good deal of the pain and injustice around us. A good education will gradually introduce us to it—sympathetically. In due course, we need to acknowledge the full weight of it, but without being crushed.

Anger, also described as a stage of grief, is not a helpful response. Anger seems to have been given to us (or if you prefer has evolved in us) to provide the energy to pick ourselves up when we have been knocked down. It can, however, possess us. In our last years in South Africa, I had begun to see my life as a series of angry battles. The fights were all good causes, although the attitude was personally destructive. It is right to get indignant and angry at injustice but as one friend pointed out to me when I was much younger, "The anger of man does not work the justice of God."[6] Part of the trouble is that we can enjoy the feeling of anger. We have to learn to put the feeling away. Exercise is one of the techniques to use. I once initiated a court case against what I thought was an unjust transfer of money from life insurance policyholders to shareholders. It was evident that I was likely to lose, and I worked off some of my anger each morning hitting tennis balls as hard as I could against the wall—panting as I did so, "Fret not yourself because of the wicked."[7] If you have the same problem, find a tennis court wall!

This is another way of saying Reinhold Niebuhr's prayer as used by Alcoholics Anonymous:

God, grant me the serenity to accept the things I cannot change,
The courage to change the things I can,
And wisdom to know the difference.

I am not sure, however, that this is the whole story. There is a view that we should learn not to become too attached to anything in this

---

[6]James 1:20 (Revised Standard Version).
[7]Psalm 37:1 (Revised Standard Version).

world—whether involving success in any field, possessions or relationships. Buddhists, ancient Greek Stoic philosophers, and some others share this view. I do not. It is right to feel the pain when we fail in a good cause, or lose someone or something good. It is also right to feel anger when people are wronged. It is however also right to feel joy at experiences of real life, at success, fellowship, and beauty. The feelings are sometimes uncomfortable and in tension. I am grateful to Chris Hingley, headmaster of a school in Zimbabwe, for pointing out that holding our feelings of pain and joy in tension requires the virtue of hope. It was another poignant moment as he was talking about the pain of another rigged election victory for Mugabe—dashing again the possibility of a return to normal life in their troubled country. Chris took special comfort from the works of Viktor Frankl, who had been in Nazi concentration camps. Frankl observed that those who were able hold onto experiences of joy and meaning were able to endure the camps.

In most worthwhile activities, there is no guarantee of a successful outcome—especially institutional change which is so dependent on shifting political power. We may have to live in situations that involve compromise and difficult tensions. Fulfilling our vocation can, however, occur without outward success. Being a member of a serving community and aiming at the best is within our powers, and enough.

We will return to motivation in greater detail in Chapter 12.

Chapter summary: Apparently overwhelming systematic injustices can be changed. Contributing to such changes, even in small ways, can be an important element of our vocation—giving meaning and motivation.

CHAPTER 5

A Model of Justice

What, then, is justice, why do we get angry about injustice, and what is it that makes a social or economic arrangement unfair?

Uncovering a Traditional Model

In 1987, after presenting my first paper on fair withdrawal benefits from pension funds, I proposed a motion at the annual meeting of the Actuarial Society of South Africa that it set up a committee to define fair withdrawal benefits. I found a seconder for my motion before the meeting, but was surprised to get no other support. I was told that it was not possible to define what was fair.

Some profound changes had apparently occurred since the Actuarial Society had been founded in 1948 with the motto *Aequitas* (Latin for justice or fairness), which was in 1987 still prominent on its crest. Forty years earlier, at least some of the founders of the organization had believed that fairness was important. I cannot but refer to the "disquieting suggestion" made by philosopher Alasdair MacIntyre. He imagines a world where scientists have all been murdered and their laboratories and resources largely destroyed, but then people try to revive science. They know the words, but do not really understand the meaning. His suggestion is that the language of morality is currently a bit like this. Some of my actuarial colleagues had come to believe that fairness (or justice or equity) had no real meaning.

I was going to write that no one murders philosophers or lawyers like MacIntyre's imaginary scientists, but this is not true. In particular, prophets or activists (depending on your perspective) who speak out against injustices are often silenced, ridiculed, or ignored. Many of those murdered by dictatorial regimes would surely fall into this category. Western democracies are not immune, as witnessed by Italian magistrates murdered by the Mafia. Working in finance does not usually make us vulnerable to physical risks, but we should not be surprised to face opposition when raising moral questions.

When I made my proposal to the Actuarial Society, I did not appreciate the extent to which the standard education of business professionals in the English-speaking world omitted consideration of economic justice. My own view of justice, formed by my Christian experience that emphasized the importance of the poor, was relatively unusual. I had thought everyone would have the same sense of the desirability of fairness.

It took me some while to get to a satisfactory definition of fairness that could apply to withdrawal benefits. I had the notion from my earlier reading of C. S. Lewis and G. K. Chesterton (both popular Christian writers) that there could be no innovative values. Values had to be both old-fashioned and universal because they identify personal and social flourishing irrespective of time and place. We will come back to this question later, but there is obviously no point in developing new theory when there might be a perfectly adequate one already. In fact, a lot of what I was looking for can be found in a good law course in Jurisprudence, and in the western philosophical tradition that goes back to Aristotle, but I had not been exposed to either. I blame this lack on having chosen a business degree, which left me ignorant of a great deal of useful and clear thinking on these subjects.

My philosopher friend, Graeme McLean, directed me to a book by J. R. Lucas, who provided the following encouragement to my quest:

> *Justice is the bond of society . . . We have . . . neglected the cardinal political virtue of justice, which, together with liberty, is the condition under which I can identify with society, feel at one with it, and accept its rulings as my own* (1980, 18).

Lucas also points out that our feelings of indignation at injustice give the energy to do something about it, and help us identify what is at stake. Empirical surveys by sociologists confirm that this is not just philosophical speculation. (Although I can hear my classically trained friends retorting that recent research has only just brought the social sciences to insights that have been obvious for at least as long as humans have been writing!) Tyler and Smith put it:

> *People's actual behavior is also strongly linked to views about justice and injustice. A wide variety of studies link justice judgments to positive behaviors such as willingness to accept third-party decisions; willingness to help the group; and willingness to empower group authorities. Conversely, other studies link the lack of justice to sabotage, theft, and on a collective level, to the willingness to rebel or protest. In other words, how people feel and behave in social settings is strongly shaped by judgments about justice and injustice* (1998, 595).

Justice is the standard against which we measure the exercise of power by individuals, as well as the agreements and laws that exercise power over our lives. We use it also to measure the effect of our own actions on others, and to evaluate all elements of government action. It is consequently concerned with protecting the powerless against the powerful, or as Desmond Tutu has put it in his speeches: "concern for the poor, the hungry, the oppressed and the voiceless."

The ancient consensus defines justice as giving to each his or her due. What is due to people subjected to the power of others? For a start, we owe others a measure of respect that arises from their essential dignity: to their ubuntu (an African word meaning humanness), flowing, if you are a believer, from our resemblance to the Creator.[1] One can also argue from reciprocity: we need to be prepared to give others their due if we hope to receive what is due to us. The decision maker must hear all the parties and act reasonably, not capriciously (arbitrarily).

Acting reasonably requires a set of criteria against which to make judgments. The major criteria can be seen as aspirations, and are set out below. They may need to be traded off against each other, and trade-offs may vary. It is counter-productive to try to define them too tightly; there is no universal agreement as to definitions or relevance. Jesse Graham and his colleagues have usefully summarized psychological and sociological

---

[1]Philosopher and Theologian Nicholas Wolterstorff makes this argument.

research showing the differences between people's acceptance of these criteria and the links to personality traits, other beliefs, and culture. Most importantly, they report that most people do not take extreme views, and that views can change. I suggest that we should all see value in each of them. They are as follows:

- *Liberty.* Justice aspires that everyone be free of interference by others, including governments. Liberals (and libertarians) place a particular value on liberty and they are right in doing so. If we feel we need, for good reasons, to intervene in the lives of others, we should be especially conscious of our tendencies to arrogance, and scrupulously consider whether it is a cloak for furthering our own interests.
- *Physical and social needs.* If people cannot look after themselves, there are universal aspirations—set out in international agreements and, sometimes, in constitutions—that governments should seek to ensure basic needs are provided. The logical necessity is especially obvious for young children and the severely disabled. Obviously, there are differences of opinion about the level of basic needs, the extent to which some people cannot provide for themselves, and sometimes whether to protect people against themselves.
- *Equality.* Justice aspires to treat people equally unless there are good reasons for differential treatment. This is horizontal equity. Equality recognizes and even maximizes each person's dignity. Democracy recognizes equality in that everyone has an equal vote, and almost everyone recognizes equality of opportunity as desirable. Vertical equity means that any difference in treatment ought to be proportionate to differences in the characteristics of the people concerned. It is inconsistent for the tax on income, for instance, to double when someone earns an extra 1 percent income. Differences arise over whether the reasons for the unequal treatment are valid or not. Equality of outcome, which requires differential treatment, is a fundamental value of those who would incline to the political left. There are, however, those on the right who seem

at times not to recognize the desirability of equal economic and social outcomes. If you are in this camp (as many finance professionals and managers seem to be), let me ask you to take time out for reflection. Read the next paragraph, but then ask yourself what has led to your enjoying a higher income than those on whom you would look down?

- *Just deserts.*[2] Justice desires that all people get what they deserve. This criterion covers both the rewards that follow our own efforts or sacrifices, and the penalties that follow destructive or malicious act, or making good the harms suffered by others. Ensuring the latter is the function of the courts in most societies. It does however go further. If I recognize the true dignity of every person, I must also recognize their right to choose and take their actions seriously. If they make a meal, it should be theirs to eat or share. If they break a window, they ought to fix it. *Restorative justice* and forgiveness, which requires an acknowledgment of desert on the side of perpetrator and the victim is discussed further in Chapter 10. For those on the left politically, perhaps you could consider how to fully deal with irresponsible decisions by people who are poorer—partly as a consequence of their decisions. In thinking about desert as a principle, we also need to recognize the tendency to see our own successes as entirely deserved (rather than incorporating at least an element of luck), and our failures as occurring when we are victims of external circumstances.[3]
- *Efficiency.* Efficiency includes lower costs and higher productivity, and recognizes materiality and avoidance of waste. Justice is often contrasted with efficiency, but I suggest that it is helpful to consider efficiency explicitly when evaluating alternatives. It seems fair to suggest that people might be prepared to make some sacrifices of the other criteria for greater output.

[2]This criterion can be defined as being identical to justice or equity, and can be contrasted with equality—as in Graham et al.

[3]If you need convincing, read Daniel Kahneman's *Thinking, Fast and Slow*.

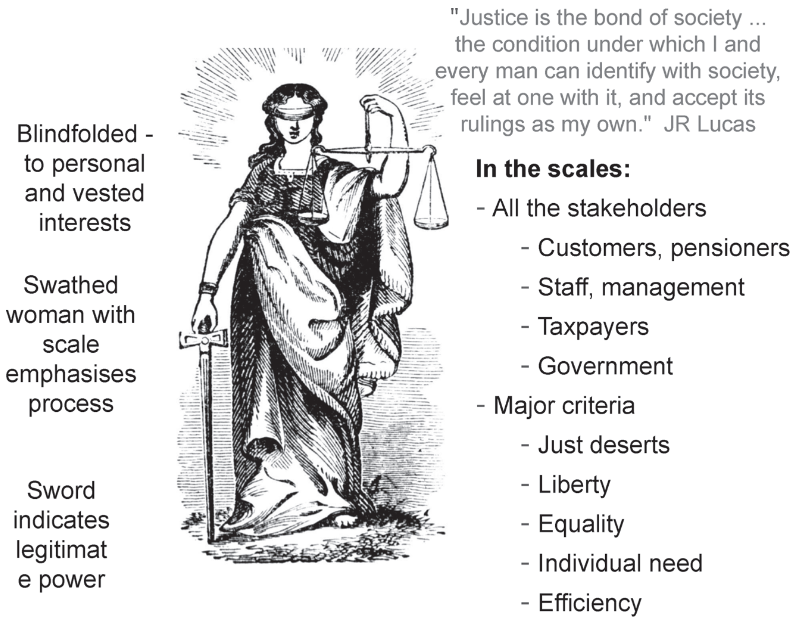

Figure 2.1 A Traditional Model of Justice

My understanding is that these criteria have absolute value: absolute because the virtuous person always aspires to meet them. Of course, compromise of some sort is often necessary. Justice is process-based; the just judge aspires to, carefully and reasonably, understand and address the rights, interests, and needs of every party.

Figure 2.1 shows the criteria with the *Lady Justice*, the image that for centuries has been placed outside law courts to personify the objective of justice, which illustrates the model being described here.

To illustrate the model, we can use it to consider the design of pension benefits. Justice may be irrelevant if the power of employers and employees are equal, but it is often the case that one group is able to exercise some collateral power over the others. To be fair, each of the criteria needs to be given weight:

- *Liberty.* Employees are free if they can resign whenever they want, and employers are free when they can hire and fire at will. If employees lose pension benefits when they resign, they are not fully free.
- *Need.* The benefits should match people's needs, so it makes sense to include insurance for early death and disability.

- *Equality.* Equal pay for equal work and equal pensions for equal service. All other things equal, it would be good to given everyone equal pensions.
- *Just deserts.* From the perspective of actuarial equity, the discounted present value of the future benefits should be equal to the discounted present value of future contributions.
- *Efficiency.* Defined benefit funds, where the benefits were based on a simple formula, were more efficient than more complex defined contribution funds, where contributions had to be accumulated at the rate of return on investments.

The model allows for relatively a wide range of benefit design, as can be seen in different companies and countries. I was able to use the model of justice to satisfy myself that I was right to be indignant at the withdrawal benefits from pension funds I have described earlier. They were unfair because they offended against just deserts and vertical equity, without promoting any of the other criteria.

Comparing the Model

Graeme McLean organized for me to present my model to his colleagues in the Philosophy Department at the University of Witwatersrand, where I was then teaching. The challenge they gave me was to try to apply it widely and see if it worked. Over the years, I have applied it to benefit design and taxation questions, to considering the fairness of charging people different insurance premiums, to whether the new South African constitution was fair, and how to compensate managed fund investors for errors in their unit prices.

One interesting use arose from a submission I made to the South African Commission on the Remuneration of Representatives. The new ANC government had set up the Commission to determine the rate of pay of public representatives, including members of parliament. Press opinion was that their pay was too low, and many people were arguing that it should be significantly increased. There may have been some lobbying to this end. I felt that this opinion was unreasonable. They were already earning more than 96 percent of South Africans with jobs, let alone those unemployed. I used the model to argue—from equality, need, desert, and efficiency—that their salaries were, if anything, already too high. The Commission was sufficiently interested in the idea to pay me to fly down to Cape Town to explain my reasoning in more detail. It was gratifying that their recommendations for a relatively small increase appeared to have been influenced by my submissions to them.

The traditional model I have presented can be helpful, but how does it compare against alternatives? The best known modern academic model is that of John Rawls. The first difference is that Rawls does not accept just deserts. He wants to "distinguish between moral desert and legitimate expectations," which is fair enough. But he goes further to suggest that "conscientious effort" could be seen as arising from moral desert and then makes the extraordinary assertion that:

> *it seems clear that the effort that a person is willing to make is influenced by his natural abilities and skills and the alternatives open to him. The better endowed are more likely, other things being equal, to strive conscientiously, and there seems to be no way to discount for their greater good fortune. The idea of rewarding desert is impracticable* (1971, 312).

I find this patronizing as it implies that some poor souls cannot help themselves because they are naturally lazy.

The second difference is that Rawls uses a *maximin* criterion rather than the traditionally broader view of equality. The principle is to maximize the wealth of the poorest (those with the minimum). But *maximin* misses those in the lower middle part of the income distribution, who do not have the time or ability to speak up for themselves, and are ground down by low-paid jobs or extra family responsibilities. The many poverty traps in our often complex social security systems create difficulties for them. Poverty traps are high marginal rates of clawback of social security benefits or tax. Clawback rates in a number of countries can exceed 100 percent of earnings, so that lower income people go backward financially if they earn any money!

Academics other than Rawls have difficulties with the concept of just deserts. Some are mistakenly repelled by the idea because it is used to argue against the redistribution of wealth. Amartya Sen questions whether we can actually determine what people really deserve, and points out that the powerful people often "blame the victims" of bad luck and even of oppression. I have sympathy with this. The concept of just deserts also cannot justify the accumulation of large amounts of wealth if it impinges on the liberties of others. Nor should it be used as an argument for excessively harsh punishments for crime. Sen's focus on people's capabilities and their freedom to exercise their capabilities, presupposes, however, that they will enjoy the benefits of their capabilities. He therefore recognizes desert at some level.

On the other hand, there are those on the right who deny equality, and are reluctant to acknowledge special needs. They recognize freedom, desert, and efficiency as criteria, and they frequently see the preservation of property rights as critical to protect each of these. Ayn Rand is a favorite for some of this group. They seem reluctant to acknowledge that much of our wealth arises from good fortune, from common goods, or by the exploitation of others. Ayn Rand and her supporters argue that virtue consists in a proper concern for one's own interest, and that modern societies' apparently altruistic support for the poor undermines the development of true, generally capitalist, greatness. They may be partly right in wanting to protect property rights, but they seem to miss the logical necessity that everyone must occupy some property to live, and have some access to the economy if they are to survive—and seem to show little understanding of the difficulties faced by the poor.

Another approach to justice is the *rights-based* approach to social objectives, which uses the declaration of human rights, preferably embodied in a national constitution, as the basis for government action. This position is often taken by lawyers, especially those inclined to a more *positive* view of the law. They argue that there is no agreement on what constitutes natural justice so we should conform to current law, particularly as it is the embodiment of the opinion of the people as expressed through their elected representatives. I do not find this approach at all convincing, having first heard it from defenders of apartheid. There are times when laws are obviously unjust, and when they ought to be disobeyed. We should however do so reluctantly, not just because of the risks to ourselves, but also conscious of the possibility that we may be blind to our personal interests, and concerned not to disturb the peace of society by breaking legitimate laws.

Rawls's and Sen's criticism of the traditional model of justice do not add additional criteria, but raise questions to correct what they see as bias, which is fair enough. It is disturbing, however, that some critics of the traditional model of justice seem to be in danger of defending their personal interests. For instance:

- Academics, who tend to the left, are frequently supported by the taxes they argue for.
- Business people are most against higher tax rates in principle because they are the targets of the additional taxes in practice. They can be supported by Academics who hold value-neutral or right wing views and to whom they pay consulting fees.
- Lawyers are more inclined to raise the status of law.
- From right and left, there are those who seem not particularly concerned about freedom and are too quick to suggest intrusive regulation.

This is a call for us to examine our own motives. While I am not particularly challenged by those who would reduce the scope of the traditional model of justice, I am personally challenged as to the extent to which it falls short of the virtue of love, which Christian doctrine holds to be of more value than justice. I do want to challenge Christian readers who may tend to take the more comfortable line that the commandment to love replaces the imperative of social justice. They could also read John Howard Yoder's *The Politics of Jesus.* Love has to act, "If anyone has material possessions and sees his brother in need but has no pity on him, how can the love of God be in him?"[4] The criteria other than need are also present in the New Testament in practical terms. Paul argues that he would *deserve* a reward for preaching,[5] that he wants generosity to lead to *equality*,[6] while in his letter to Philemon he asks for the *liberty* of his slave. Other major religions are also sympathetic to this view of justice and love.

[4]1 John 3:17 (New International Version).

[5]1 Corinthians 9:4ff.

[6]2 Corinthians 8:13.

Timeless Universal Values?

This brings us to the question of whether the concept of virtue, and justice, are universal and timeless. Do the virtues and justice apply to us as well as ancient Greeks, Chinese, and modern lawyers?

Universality?

I have referred to the positive psychology research on the universality of the virtues in the introduction. C. S. Lewis makes the case for the universality of many justice-related values in his little book *The Abolition of Man.* He includes the prohibition of murder and theft, and ways of enforcing promises. These justice-related values are obvious in the principles of professionalism that the International Actuarial Association recently produced for all its members. The Association has affiliates in 92 countries and says that they agree on ethical standards of integrity, independence, trustworthiness, and the obligation to act in the public interest. While recognizing differences in emphasis,

> *There do not appear to be material or cultural differences in views on what is ethical. No such differences have emerged during discussions in the Professionalism Committee, nor has anyone challenged this assertion* . . . (2014, 7).

Other professions may not be quite as coordinated internationally as the actuaries, but we would probably be surprised if their standards were diametrically opposed to the actuarial standards.

People do place legitimately different personal and cultural weights on the elements of justice. Europeans appear to place a greater value on equality and a lower value on liberty than North Americans do. Trade union members usually place more emphasis on equality than managers do—and less on just deserts.[7] Alisdair MacIntyre identifies a number of different intellectual traditions of justice within western philosophy, and more in other cultures. But there is probably universal agreement in all societies with a developed financial sector—as to what constitutes

[7]See work by Sidney Verba and Gary Orren.

gross injustices, such as corruption, theft, and exploitation. There is also widespread agreement on the procedures required to attain justice as is evidenced by similarities in legal processes and structures.

Timeless?

G. K. Chesterton has the great line about timelessness of values (which he refers to as dogmas):

> *Some dogma, we are told, was credible in the twelfth century, but is not credible in the twentieth. You might as well say that a certain philosophy can be believed on Mondays, but cannot be believed on Tuesdays* (1909, 135).

I must admit that I do not see this argument as conclusive as it once was. The last century has seen huge developments in technology and society that have changed, in some ways, the nature of our relationships with one another, and perhaps even our psychology. How much communication occurs through telephone and now video, through letters, e-mails, texts, and posts on blogs and personal sites? Interestingly, Chesterton also saw this coming in a prophetic lecture he gave in 1930. As described in a biography of him by Joseph Pearce:

> *The coming peril . . . was not Bolshevism because Bolshevism had now been tried and 'the best way to destroy a Utopia is to establish it.' . . . nor was the Coming peril another world war, although the next war 'would happen when Germany tried to monkey about with the frontiers of Poland'. The coming peril was 'the intellectual, educational, psychological and artistic overproduction, which, equally with economic overproduction, threatens the wellbeing of contemporary civilisation. People are inundated, blinded, deafened, and mentally paralysed by a flood of vulgar and tasteless externals, leaving them no time for leisure, thought, or creation from within themselves.' The astounding perception of this speech, delivered three years before the Nazis came to power, nine years before the outbreak of war and many years before the final downfall of Communism' . . .* (1997, ix).

I think Chesterton was right on both counts. Values are timeless, but the "flood of externals" does mean that we face many more distractions from what is important. To go further: when the flood comes in the form of regulation it creates physical limitations on our freedom to flourish.

Evolutionary Arguments

This is perhaps the point to consider justice from an evolutionary perspective. If organisms evolve to better survive in an environment, surely societies evolve similarly. If so, there is a case that a belief in justice is necessary for people to identify and contribute willingly to society. Societies with a stronger general belief in justice may then prosper. One would expect unjust societies, where corruption, theft, and exploitation become rampant, to fail and be replaced by arrangements that are more just. This is difficult to prove because of the many variables to consider. Economic research does, nevertheless, tend to confirm that the elements of justice have a positive impact on society and the economy.[8]

That just societies are wealthier and happier does not provide a reason as to why we should, as individuals, aspire to act justly. In fact, if we were to take a narrow view of our own self-interest, we might well promote the

---

[8]Robert Barro's papers provide a widely quoted evaluation of the effects of different factors on economic growth. He finds positive effects for economic freedom and the rule of law, but no real relationships for political democracy and equality, although he does find that economic growth may contribute later to democracy. I refer to both papers for anyone interested to note that the different mathematical models can ascribe different effects to the different variables. Models of this sort look at short periods and normally explain a small percentage of such variables as economic growth or democracy. Peter Swann warns that there is often more noise than signal in economic models, and the nature of the relationships can even reverse when you add further variables. They may well be missing important factors that could completely change the relationships reported.

Even if equality does not encourage growth, it is found to improve health (Wilkinson); to contribute to the development of mutual trust and social capital so discouraging crime (Uslaner); and because it leads to greater happiness (Layard)—although Alesina *et al* suggest that this does not apply universally. Tyler and Smith refer to extensive documentation of how feelings of relative rather than absolute deprivation underlie much social unrest: inequality seems to provide the spark.

view that others must be just (honest, and preferably trusting) so that we can more easily exploit them. We have to believe that integrity, justice, and the other virtues are worth more than pure material interests, which is why this chapter makes a case for the traditional model of justice without using arguments from narrow self-interest.

Chapter summary: Justice is the virtue that governs our power over others. It consists of giving everyone their due as much as possible: liberty, basic needs, equal status and happiness, and their just deserts. Justice is universally applicable as we only grow to our full stature when we contribute to communities which are places where the virtues flourish. It is required for societies to flourish.

CHAPTER 6

Injustice in Finance and Economics

Not everyone accepts the importance of using the standard of justice to evaluate all work that impacts others. In particular, some positive economists hold that values and virtues should have no role in economics. The first section of this chapter suggests that this extreme value-free approach is too narrow. I then go on quote Adam Smith extensively, first hoping that his authority will be persuasive, and secondly as his indignation at injustice identifies many issues that still concern us. The third section looks at the economic rents that particularly caught his ire, arguing that it is right to be indignant, and identifies overcharging, over-servicing, and excessive executive remuneration as some of the injustices we currently face. The last section considers the risks of ignoring ethics in applications of economic theory.

Value-Free Science

True science is value free in the sense that it is not biased by the personal views of the scientist. Good scientists will not attempt to manipulate politicians, who should make laws that reflect the views of the people not just those of experts. But against the idea that scientists can put away their values and preferences, Michael Polanyi writes of the necessity of a passionate approach to finding truth. The abstract of his book *Personal Knowledge* reads:

> *(He) demonstrates that the scientist's personal participation in his knowledge, in both its discovery and its validation, is an indispensable part of science itself. Even in the exact sciences, 'knowing' is an*

> *art, of which the skill of the knower, guided by his personal commitment and his passionate sense of increasing contact with reality, is a logically necessary part.*[1]

I am with Polanyi. I came to a much deeper understanding of pension mathematics when driven by my indignation at the unfairness of cross-subsidies. I confess, though, that my anger might have contributed to my failing the pension exam the first time I took it!

Polanyi also explores the perverse consequences of attempting to deny the moral intuitions that we all have. Alvin Gouldner puts it this way:

> *The only choice is between an expression of one's values, as open and honest as it can be . . . and a vain ritual of moral neutrality which, because it invites men to ignore the vulnerability of reason to bias, leaves it at the mercy of irrationality* (1962, 212).

The irrationality arises because neither self-interest nor moral indignation, which often provides emotional drivers for debate, are recognized for what they are. Too much passion can distort our thinking and offend others unnecessarily, but that makes it all the more important to acknowledge the passion and ensure it does not distort our actions.

Alisdair MacIntyre also criticizes the logic of this separation of the positive (what is) from the normative (what ought to be).[2] He argues that the two are connected by the concept of purpose. This *is* a pair of scissors implies that they *ought* to be able to cut; she *is* an accountant, she *ought* to apply accounting standards. This does of course assume that scissors and accountants have good purposes. The important question is thus: what are good purposes for different people? The answer of this book is that it is found in our vocations. Positive economists might answer that their purpose is describing how the economy works, with no consideration of their own personal development or the purpose of economic activity. The response is that this is too narrow: what is the economy without purpose?

---

[1]Accessed August 30, 2014. http://press.uchicago.edu/ucp/books/book/chicago/P/bo3628989.html.

[2]In *Three Rival Versions of Moral Enquiry* particularly.

It can also be argued that debates about purpose and ethics become too heated because views are personal and there is no agreed common ground. Much better, however, to be courteous when disagreeing than not debating the subject at all. If we want to find good solutions, we have to be prepared to try to interact with reasonable people with whom we disagree. As we have seen already, there is also much common ground on which to base our discussions.

Adam Smith's Consciousness of Justice

I find it encouraging to know that Adam Smith, father of modern economic thinking, did not espouse value-free economics, and was deeply concerned with injustice. He writes particularly about just deserts:

> *In order to enforce the observation of justice, therefore, Nature has implanted in the human breast that consciousness of ill-desert . . . as the great safe-guards of the association of mankind, to protect the weak, to curb the violent, and to chastise the guilty* (1759, chapter III).

In my view the purple passages of his main work, *Wealth of Nations*, that make it a classic, are commentary on ethical issues of the day. I have quoted them extensively in this section, because they are so insightful and relevant.

He warns that business people are well equipped to manipulate our thinking, and will often, even unintentionally, exploit the public. We had better therefore treat their opinions with suspicion.

> *Merchants and master manufacturers are . . . the two classes of people who . . . by their wealth draw to themselves the greatest share of public consideration. As during their whole lives they are engaged in plans and projects, they have frequently more acuteness of understanding than the greater part of country gentlemen. As their thoughts, however, are commonly exercised rather about the interests of their own particular branch of business, than about that of society, their judgement, even when given with the greatest candour (which it has not been upon every occasion), is much more to be depended upon with regard to the former of these two objects than with regard to the latter. . . .*

The interest of the dealers, however, in any particular branch of trade or manufactures, is always in some respect different from, and even opposite to, that of the public. To widen the market and to narrow the competition is always in the interest of the dealers. To widen the market may frequently be agreeable enough to the interest of the public, but to narrow the competition must always be against it, and can only serve to enable the dealers, by raising their profits above that which they would naturally be, to levy, for their own benefit, an absurd tax upon the rest of their fellow-citizens. The proposal of any new law or regulation of commerce which comes from this order, ought always to be listened to with great precaution, and ought never to be adopted till after having been long and carefully examined, not only with the most scrupulous but the most suspicious attention. It comes from an order of men, whose interest is never exactly the same as the public, who have a general interest to deceive and even oppress the public, and who accordingly have, upon many occasions, both deceived and oppressed it (2005, 213).

He believed that the greed of business was worse than of politicians:

The capricious ambition of kings and ministers has not, during the present and preceding century, been more fatal to the repose of Europe, than the impertinent jealousy of merchant and manufacturers. The violence and injustice of the rulers of mankind is an ancient evil, for which, I am afraid, the nature of human affairs can scarce admit of a remedy. But the mean rapacity, the monopolizing spirit of merchants and manufacturers, who neither are, nor ought to be, the rulers of mankind, though it cannot perhaps be corrected, may very easily be prevented from disturbing the tranquillity of anyone but themselves (2005, 396).

Moreover, he recognizes that it can be difficult to oppose the greedy:

The member of parliament who supports every proposal for strengthening this monopoly, is sure to acquire not only the reputation for understanding trade, but great popularity and influence with an order to men whose numbers and wealth render them of great importance. If he opposes them, on the contrary, and still more if he has authority

> *enough to thwart them, neither the most acknowledged probity, nor the highest rank, nor the greatest public service, can protect him from the most infamous abuse and detraction, from personal insults, nor sometimes from real danger, arising from the insolent outrage of furious and disappointed monopolists* (2005, 377).

His opposition to barriers to trade is partly because they fall on the weakest in society. Writing about the weaving industry of his time, he says:

> . . . *It is the industry which is carried on for the benefit of the rich and powerful that is principally encouraged by our mercantile system. That which is carried out for the benefit of the poor and indigent is too often either neglected or oppressed* (2005, 524).

He sees the value of the *creative destruction* of free trade, but urges care in abolishing barriers, again to protect the poor:

> *Humanity may in this case require that the freedom of trade should be restored only by slow gradations, and with a good deal of reserve and circumspection. Were those high duties and prohibitions taken away all at once, cheaper foreign goods of the same kind might be poured so fast into the home-market as to deprive all at once many thousands of our people of their ordinary employment and means of subsistence* (2005, 374).

It is not clear how he would vote in a modern election, as he had some sympathy for workers and how they can be treated unjustly:

> *What are the common wages of labour, depends everywhere upon the contract usually made between those two parties, whose interest are by no means the same. The workmen desire to get as much, the masters to give as little as possible. The former are disposed to combine in order to raise, the latter in order to lower the wages of labour. It is not, however, difficult to foresee which of the two parties must, upon ordinary occasions, have the advantage in the dispute, and force the other to a compliance with their terms. The masters, being fewer in number,*

> *can combine more easily; and the law besides, authorises, or at least does not prohibit their combinations, while it prohibits those of the workmen. . . . We rarely hear, it has been said, of the combinations of masters, though frequently of those of workmen. But whoever imagines, upon this account that masters rarely combine, is as ignorant of the world as of the subject. Masters are always and everywhere in a sort of tacit, but constant and uniform combination, not to raise the wages of labour above their actual rate. To violate this combination is everywhere a most unpopular action and a sort of reproach to a master among his neighbours and equals* (2005, 60).

Trade unions were illegal at the time, and he probably would have been against them as much as "combinations of masters." He specifically criticizes regulations that protect select groups of workers against others.

Purpose of Government

Smith explicitly recognizes that government has functions to protect the weak and create public goods such as infrastructure and schools.

> *According to the system of natural liberty, the sovereign has only three duties to attend to; three duties of great importance, indeed, but plain and intelligible to common understanding:*
>
> *first, the duty of protecting the society from the violence and invasion of other independent societies;*
>
> *secondly the duty of protecting, as far as possible, every member of society from the injustice and oppression of every other member of it, or the duty of establishing an exact administration of justice; and*
>
> *thirdly, the duty of erecting and maintaining certain public works and certain public institutions which it can never be in for the interest of any individual, or small number of individuals, to erect and maintain; because the profit could never repay the expense to any individual or small number of individuals, though it may frequently do much more than repay it to a great society* (2005, 560).

He is also in favor of some redistribution, at least as far as public education is concerned:

> *The education of the common people requires, perhaps, in a civilised and commercial society the attention of the public more than that of people of some rank and fortune* (2005, 639).

Smith's view of justice includes freedom and desert. He also writes with a concern for people's needs and the poor, although when he writes about the poor laws (the social security of this time) he appears more concerned at their impact on the free movement of labor than the extent to which they alleviate poverty. He seems to think that, in a system of "natural liberty," there would be minimal poverty and that private charity would be sufficient to address it.[3] His views are therefore compatible with the traditional theory of justice in these respects.

Given his views, however, it is an irony that supporters of business against government interference see Adam Smith as an authority for their cause. It is also sad that, with notable exceptions, few modern economists seem to follow his example in speaking out clearly against monopolists.

Economic Rents

The traditional theory of justice explains why economic or monopoly rents are unjust. Economic rent can be defined as that proportion of the payment to an input that produces no increase in output. The description *rent* derives from the rent paid for, unimproved, land because it is not being made any more. Monopolists effectively charge rent because they do not increase their output when they put up their prices. Another way of seeing it is that the monopolists create an artificial shortage.

One can apply the traditional model of justice to economic rents to show that they are unjust.

- *Freedom.* Some business people argue that government intervention to reduce monopoly power is an infringement of freedom. This is self-serving and misses important issues.

[3]Geoffrey Gilbert discusses Adam Smith's view on poverty in detail.

Some monopolies, particularly patents and copyright, require government interventions in the first place. Others arise because companies merge or otherwise combine to use their market power. One recognized role of government is to protect people's freedom against the illegitimate use of power by others to oppress them. This includes policing of conspiracies where a group of people get together to create greater power for this purpose.

- *Desert.* To the extent that monopoly rents do not come from any socially productive purpose, those who work to create them do not deserve to be rewarded. People may have paid to enjoy the rents, but this is analogous to buying stolen property—knowing its origin.
- *Efficiency.* Monopolies are inefficient unless there are economies of scale that smaller firms cannot achieve. This is often the case, and governments may operate nationalized industries or grant a monopoly to take advantages of significant economies of scale for the *common good.*
- *Equality.* To the extent that monopolists tend to be wealthier, monopoly rents frequently contribute to inequality—and may aggravate the poverty of the weakest.

Many people have made these arguments in various different ways. Raymond de Roover makes the point that the concept of a just price excludes monopoly rents, and suggests that this has been the traditional view of Christian theologians for centuries.

It may be that monopolies are practically insignificant in Western economies and that excessive rents are unlikely because competitors will soon enter any inefficient market. This is perhaps more true in the large U.S. markets than in other countries with smaller markets more easily dominated by one company. Even in the United States there are examples of monopolies. One that affects other countries is the "Mickey Mouse Protection Act" that extended copyright from 50 years beyond the death of the author, to 75 years or 95 years if created by a company. Disney was an immediate beneficiary as its protection for Mickey Mouse was about to expire. The retrospective nature of the extension cannot possibly have any general economic benefit. It is also currently beneficial to U.S. interests as the United States is a net exporter of copyrighted material, and the U.S. government has been active in forcing other countries to accept U.S. copyright laws if they want free trade agreements.

A case can be made to provide legal protection for intellectual property—for a limited period even if it does mean that inventors and creators are able to extract some monopoly rents. It provides incentives for creativity and just rewards to innovators who have contributed productively to society. The patent system provides plenty of incentives with its limitation of 20 years. It is, however, difficult to see advantages in the use of copyrights to give protection to software for longer periods, and the recent extensions to those periods.

Because economic rents are socially useless and unjust, they can and should be taxed away. A case can also be made to tax land rents away. Taxes on land (but not improvements such as fences or buildings) are the most efficient of taxes because the tax does not reduce the supply of property available. All other taxes—on income, consumption, and other assets—reduce the incentives to produce the income, consumption, or assets. A land tax is actually likely to make more land available for production because people will be less likely to leave it unutilized. As I learnt from my Samuelson Economics textbook, "Pure land rent is in the nature of a 'surplus' that can be taxed heavily *without distorting production or efficiency*" (1970, 541).

Envisage a country where land was publicly owned, and rented to the highest bidder. It would be used at its optimum level economically, and the government would have a huge tax base that would allow it to reduce many other taxes. One can argue that this would be fair, as all land was publicly owned at one point. Counter-arguments are that you cannot divide the land from the improvements and that some people have developed properties over many years and deserve to enjoy the fruits, while others have recently paid large sums to buy properties. One could, however, envisage a transitional arrangement whereby the land tax was slowly introduced to replace other taxes.

These same arguments also apply against taxing the rents earned by monopolists, but they are generally less convincing. By owning land, I am not obviously robbing my neighbors as long as they have a place to stay. By charging a monopoly price, however, I am taking money from my customer for no other reason but that I can and I want to be richer. While there are practical and political obstacles, I see no good reason why it cannot be taxed away, even if people have recently bought their shares in the monopolist.

Excessive Charging

Extracting economic rent—economists call it rent-seeking—is to make excessive charges. This covers misrepresentation, and taking advantage of ignorance or even carelessness. Deception is likely to be illegal, taking advantage stretches from the illegal to a reprehensible lack of integrity.

One area, common in finance, where stronger parties can exploit their weaker counterparts is that of *incomplete contracts*. In these, the institutions have the discretion to change the terms of the contract unilaterally to their benefit.

Yearly renewable term life insurance provides one example. The premium rates are increased with age, at the discretion of the insurer. The companies guarantee that they will renew the cover even if policyholders' health deteriorates—and that they will not discriminate on grounds of deteriorating health. They can, however, extract rents by increasing the premiums on existing cover excessively, and offering cheaper premiums on new policies to those who are in good health or who notice that their premiums are no longer competitive. Companies then make more money from policyholders who are unhealthy, or who are not actively comparing premiums—without losing revenue from the rest.

Life insurers who have locked policyholders into long-term investment contracts can also extract additional profits by increasing their investment charges (directly or surreptitiously through changes to investment mixes) or withdrawal penalties, or alternatively reducing their bonus rates.

Other ways are by making secret profits, which are illegal, confusing your clients so that they do not get the best deal on their charges, or unspoken agreements not to compete on price.

It may be objected that market discipline will prevent this. If the company wants to stay in business, it would be trying to remain competitive, and to retain its reputation. In recent times, however, the huge fines paid by banks and insurance companies in the United States, the United Kingdom, and Europe suggest that financial companies are not always concerned for their reputation.

In many jurisdictions, offended parties can actually rely on legal protection against such *unconscionable conduct*. It is worth keeping the potential for legal action in mind, whether you are working for a company and you would like it to be fairer to customers, or whether you are an aggrieved customer:

- One concept is that of *reasonable expectations* or policyholders' reasonable benefit expectations. The idea is that policyholders enter their contracts with various reasonable expectations about the benefits and costs. They form the expectations from what is in the marketing material as well as what is in the formal contract. The insurance company can therefore be compelled to meet the expectations that it has created, or expectations that policyholders may have been given by behavior of other insurance companies.
- Another possibility is that the terms of a contract give too much unfettered discretion to a stronger party, in which case it can be declared *void for vagueness*. In this case, the company may find it difficult to charge anything that it has not clearly defined.
- One party to a contract it not entitled to make money from the contract without disclosing it to the other. The courts should require such *secret profits* to be disgorged by a company that charges them.

It is expensive to argue cases like this in court. Regulators and ombuds are able to do so, and it is to their credit when they do. Pursuing cases in the face of apathy and opposition is one of the major ethical challenges for regulators. Recent innovative alternatives to regulatory action have been class actions organized by legal firms. In the United Kingdom, we have recently seen banks required to refund late-payment penalty charges to those they have overcharged. Here the objection was not so much that the contractual terms were incomplete, but that it was unconscionable to make a profit out of the penalty conditions in a contract.

One cannot totally prevent future managements from exploiting clients, but contracts can be made more complete. A business, which I have been involved with, has created a board charter, to which reference will be made in marketing material, to assure customers that premiums will not be raised unreasonably. Other companies have put such conditions in their contracts.

The opportunity to overcharge in various ways may be the greatest temptation facing the finance sector. Some academics are puzzled as to why U.S. merchant banks can charge 7 percent for raising capital; hedge funds can charge 2 percent of assets plus 20 percent of outperformance, and insurers can pay commissions that account for up to half of the benefits.[4] One reason is that much of the sector is protected from foreign competition. Even if the banks and insurers are foreign owned, they must invariably operate local branches—for as long as people need cash. It is also widely known that most people are rather indiscriminate—even apathetic—consumers, who do not understand or want to understand finance, and a growing proportion of assets are owned by older people who may be even less discriminating. The costs of financial services are also not *salient* in that people seldom pay them directly; they come out of the premium or bank account. They may also appear unimportant, as they are the smallest items that are reported. There may also be an element of implicit combination within the sector—to use Adam Smith's term. In the actuarial world for many years, profit targets seem to have been set at an arbitrary—and rewarding—15 percent, because that was the rate used in the most popular textbook!

One might object that indiscriminate consumers only have themselves to blame. This argument often goes with calls for better financial education. It is, however, not consistent with regulation in other areas of consumer behavior. We do expect people to educate themselves in food production, health care, or engineering so that they can prevent losses in these areas. Financial losses do not enjoy the same degree of regulation because they do not involve potential loss of life.

---

[4]See Abrahamson et al., Amin and Kat, and Downey, who provide examples, the last going back to 1957.

Overcharging is, however, important when it leads to distorted decisions, inequality, or an excessive concentration of power. The regulation of charges in the sector appears to go in cycles. Before the wave of financial deregulation of the last 30 years, governments everywhere put caps on interest and premium rates, and financial charges. Some of these survive—controls of motor insurance premiums are an example. Regulators are reintroducing others: fee caps for compulsory pension fund arrangements in Chile, the United Kingdom, and some Australian products. Even with deregulation, governments have striven to increase the salience of charges by forcing greater disclosure. Especially in the United Kingdom, huge fines have been imposed on companies for failing to make adequate disclosures, misselling, or overcharging for insurance products. Leading financial economist, John Campbell and his colleagues have publicly called on U.S. regulators to act against various "rip-offs."

There are entrepreneurs who have identified the overcharging and benefitted by competing on price. Apart from his writing on the subject, John Bogle has created a subindustry through the low charges of his Vanguard indexed mutual funds. I have felt it worthwhile to become involved in a couple of businesses that have reduced prices through increased competition. Other entrepreneurial examples are the mutual organizations—insurers and building societies/savings and loans institutions that dominated some parts of the financial sector until quite recently. Their selling point was that profits belonged to customers. We are lucky in Australia to have large not-for-profit financial institutions in the form of industry superannuation funds that are open to the public. As with the mutuals, they are under threat from the competitors they challenge, and will always be at risk of expropriation by management or outside parties. Their presence, however, keeps prices lower.

Many people in the finance industry are uncomfortable with gouging. A number of people have told me that they have left the life insurance industry because of their discomfort with overselling and excessive commissions. For those who stay, there is an obligation, particularly as they grow older, to make their discomfort known. There is a variety of ways of doing this. You could present some analysis at an industry or professional meeting expressing surprise at the puzzle of high profits, perhaps giving some report of penal regulatory responses in other countries or stories of individuals who have been exploited. Some companies may respond voluntarily or you might spur a regulator into action. Last year in Australia, excessive premiums on funeral policies marketed directly to pensioners came under an increasing spotlight, brought by people within the industry and interested journalists. The regulator has spoken to companies, and a number of improvements have been made. While writing this section, I read of actuaries in the United Kingdom calling publicly for pension fund trustees to ensure that their members do not accept poor annuity rates when they retire—because they had not shopped around.

Over-Servicing

The twin of overcharging is over-servicing. Adair Turner, then head of the UK Financial Services Authority, suggested:

> *. . . there are good reasons for believing that the financial industry, more than any other sector of the economy, has an ability to generate unnecessary demand for its own services—that more trading and more financial innovation can under some circumstances create harmful volatility against which customers have to hedge, creating more demand for trading liquidity and innovative products; that parts of the financial services industry have a unique ability to attract to themselves unnecessarily high returns and create instability which harms the rest of society* (2009).

One can also think of unnecessary credit cards, corporate restructures, and over-insurance. Carbon trading may also fall into this category, especially to the extent that it incorporates dubious offsets.[5]

A firm that is over-servicing its clients is in an institutional bind: what is good for the clients is bad for staff and shareholders, and correcting the problem will cause some pain. One response is to say that this is the responsibility of regulators and courts.

If, however, people are misleading or deceiving their customers, the loss of integrity of those working for the company may be worse than

---

[5]Larry Lohmann has written extensively on the politics and economics of carbon trading.

the financial losses of the customers. Even if regulators are inactive, it is the responsibility of senior management to recognize and correct this. Wherever you are in the organization, however, you can work to empower customers and chip away at over-servicing. One fruitful approach can be to warn of the risks of penal regulatory intervention by highlighting the size of the fines that have been issued in other jurisdictions. Another is to focus on products and services that do offer value for money.

Executive Remuneration

Excessive executive remuneration is another species of overcharging. The three standard arguments for the size of current levels of remuneration do not stand up to scrutiny. The first, the argument that they deserve it does not apply in a free and efficient market. Companies only have to pay executives enough to encourage enough competent people to offer their services. This is the logic of the market—the matching of supply and demand.

Second is the view that money is the strongest motivator. There is ample psychological and economic evidence[6] that people are better motivated by intrinsic rewards when faced with complex tasks where it is difficult to measure success. The idea that managers should have "meaningful equity stakes" to align their incentives with shareholders is not only theoretically suspect, but it has always been obvious that enormous share options, which they have been given, depend more on the overall increase in the share market than on any effect that they have on the company's results. When I have been told that managers need to focus on a single objective, I wonder if they could cook a meal without burning the vegetables!

The final explanation—that of the tournament effect, which suggests that junior people will work harder to be promoted—is more plausible. The problem, however, is that this focuses people more on winning the promotions tournament than on the job, and is more likely to create office politics than productivity. The current level cannot be justified by

---

[6]The best known is perhaps Frederick Herzberg (1968).

desert, equality, need, or liberty, and the efficiency impacts are at best debatable[7].

Although excessive remuneration is not new, extreme levels and poor economic performance in recent times have led to greater public opposition if not outrage. The ratio between the highest and the lowest wage within a company in the United States apparently rose from 20 in the 60s to to almost 400 in 2000, but was still almost 300 in 2013.[8] Drucker (1985) suggested that this ratio should normally be limited to some 25 to 1—with each company publishing the ratio, and each person earning about 40 percent more than their subordinates.

My friend, Nick Hudson, who works in venture capital, responded to the first draft of the previous paragraph with:

> *In our closely held private companies we set salaries that are much lower than your proposed ratios suggest. The executives must expose their capital to risk, and earn economic profits on it only when the firm earns long-term economic profits on its capital, which it can only sustainably do by treating all key stakeholders fairly. I consider it a sign of poor character (lack of virtue) when a CEO is unwilling to share anything of the economic outcomes created. Then you should not trust him.*

The problem exists across the economy and is perhaps worst within the finance sector. Proximate responsibility (that is the most guilt) lies with the CEOs who request and indeed argue for such pay and their board directors who vote for it. The CEOs are being greedy. The directors are failing in their duty to their shareholders and other stakeholders in the company, and displaying a lack of courage.

Courage needs forethought: it has to be appropriately armed. I used occasionally to have lunch with a director of my life insurance employer, who had worked his way up from selling policies. In semi-retirement, he was helping a management remuneration consultant sell reports to companies. He told me it was the easiest job he had ever had: in about half the cases,

[7]See Canice Prendergast for a review of the research.

[8]Accessed June 25, 2015. http://www.epi.org/publication/ceo-pay-continues-to-rise/

the report said the CEO was earning less than the average of his or her peers and the sale was guaranteed. Directors need to know that the comparative reports put before them may have been selected, and clear that some people must be paid less than average. They need to be free of the notion that the level of pay is a measure of respect for the person concerned.

As a manager and non-executive director, I have had to turn down requests for higher pay. It is relatively easy as a manager. You are normally operating with budget constraints and can refer to higher powers. At board level, there is no one to whom you can shift blame. The arguments become heated, and you have to back what is a subjective judgment. If you are being fair, you will be relatively sure that you can replace the person concerned at the package that you are offering. Only when my preparation has allowed me to get to that point, have I found the confidence to take an effective stand and say: I do not want to lose you, but the board will not be paying you what you are asking for.

The Price of Capital

There is a view that all returns to capital are economic rents. Historically, there were Jewish and Christian prohibitions on charging any interest—prohibitions which strict Muslims still follow. One argument derives from the labor theory of value. People produce goods and services by their labor. Capital is lifeless; it cannot be fruitful, and it is argued therefore that it should not have a price.

The argument may have some validity when applied to land. We have to share out the land in some way (in the right-hand rotor of Figure 1.2). No price is paid for that land which is owned and occupied by families. Much other land is owned by the state or communally, and so is beyond the market and the financial system. As discussed above, even if land is rented out, there are no efficiency losses if the rent is all paid as tax. There are, however, efficiency gains if the land not required for living is rented to the highest bidder—and there is an active market. This is, in fact, the position taken by the Old Testament[9] on land: families have a right to

[9]See Leviticus, Chapter 25.

a place to live in perpetuity, but houses and land in cities (commercial areas) can be bought and sold.

While it applies to land, charging for capital in commercial arrangements is surely more efficient. It would be much too complicated if businesses could only operate by paying people for their labor directly from their revenue. Raising capital in the form of debt or equity to pay wages at least is so much easier, and one cannot imagine being able to do so without offering some reward related to the amount supplied. The alternative of the state deciding on all capital allocations is possible, but the failure of communist states over the last century suggests that this centralization of power is corrupting, undermines personal freedom, and is ultimately unsustainable.

We return in Chapter 9 to ask whether there is not too much debt in the system. At this point, however, the payment of interest, a premium for risk, and a reward for entrepreneurial activity can be justified as follows (after removing the effects of inflation and accepting that measurement will be imprecise):

- The risk free interest rate can be justified as an incentive for people to defer their spending and acts as a rationing mechanism for those who want to borrow—where capital decisions are subject to market forces. In periods of growth (driven by population growth or new or changing technologies or economic structures), there is a need for more capital and a relatively large interest rate may be required to match the demand for capital with its supply. In periods of economic decline, and in aging societies where people are saving for their own retirement, the supply of capital may exceed demand even at a zero interest rate. Current low interest rates are perhaps the result of there being so many more aging individuals who want to save—and less need for capital as the population grows more slowly. The risk free rate is seldom high: the real rate does not really seem to have gone much over 5 percent for two centuries—and is now negative in many countries.
- The risk premium can similarly be justified as the price of risk to which the capital is subject—and again determined by the supply and demand. It may be that the risk premium will rise

with many older and more cautious individuals dominating capital markets. The risk premium obviously depends on the size of the risks.

- Entrepreneurial profit is a reward for creativity. It arises because entrepreneurs have created something not previously available, and people are prepared to pay more to enjoy it. Creation of such profits does involve some risk taking, but the rewards exceed the price of risk, and the profits will cease to be available when competitors copy the innovation. From the perspective of desert and efficiency, entrepreneurial profits belong to the entrepreneur not to capital—but the entrepreneurs have often provided the initial capital.

Applying the traditional framework of justice, we can acknowledge that those who respond to the economic incentives deserve their reward. The price of capital has an indirect and ambivalent impact on equality because while the very rich own more capital, many of those in the middle income ranges borrow a great deal for housing particularly. In the South Africa of my youth, interest rates were kept low to benefit rich whites whose home loans were ultimately subsidised from poorer blacks—who were actually saving more. There are forms of redistribution that are more efficient than reducing returns on capital. Regulating profits is an infringement of liberty. Housing apart, therefore, there is a good ethical case that capital is allocated best using a market price.

A Matter of Judgment

Setting a precise price that does not incorporate any excess charges is a matter of judgment on which people will differ. It is difficult to separately identify entrepreneurial profits from rent. There is, however, a huge body of antitrust (competition) law built up by many courts that have made determinations to prevent overcharging, or restore excessive profits to those overcharged. The size of the field suggests that many have already found a vocation in developing this area of law.

While it may need a forensic process to objectively isolate rents, there is a fundamental difference between the motivation to provide real value and one that aims to extract an unfair profit. It may be almost impossible for an outsider to identify, and we may even surprise ourselves when we think about it, but the difference is critical. The one adds value to society, the other subtracts from others. In the former, we exercise our virtues in a vocation, but with rent seeking we unjustly exploit others.

Problems with Positive Economics

Positive economics has come to dominate university teaching, and perhaps business thinking, in recent years—so much so that it is often called classical economics. It finds expression in Milton Friedman's description of positive economics, written in the 1950s. Not all economists agree, as can be seen by Paul Samuelson's (1963) reply. Philosophers, such as, Hausman and McPherson make a strong argument for including the discipline of moral philosophy in economic thinking. Legal academics, such as Jaap Winter, and philosophers, such as Joseph Heath, are prominent among the critics of positive economics.

They identify the major issue as the misuse of the assumptions made about people's motivation and rationality. As we have been taught, all other things being equal, we can assume, for some purposes, that people want to make economic decisions rationally. This will mean that they want to maximize some *utility*, which is often their personal material wellbeing. But other things are seldom equal, people frequently fail to make entirely rational decisions, and *utility* often goes beyond private material gain.

Heath shows that many economists make irrational jumps in the development of their theory, and in practical recommendations. The errors are not easily undone. He looks particularly at agency theory, which has been used to justify the granting of the excessive remuneration discussed above. The problematic assumption is that executives need material incentives to perform their jobs diligently not only flies in the face of the evidence, but:

> . . . *even a well-designed system of external incentives has the potential to undermine moral motivation, and thus to create agency costs where previously none existed* . . .

> *People may be acting cooperatively merely because they consider it the right thing to do. When they are subsequently offered an external incentive, it may have the effect of changing their perspective, so that they no longer consider the question from a moral point of view, but rather examine it from the standpoint of their self-interest. . . .*
>
> *Sophisticated practitioners of agency theory are familiar with these limitations, but a large number of enthusiasts are not. Because of this agency theory can serve as a source of considerable inadvertent mischief when treated as an accurate representation of reality* (2010, 136).

He then goes on to suggest that many managers come to accept as fact that people are only motivated by their own material interests, and:

> *. . . it would be no surprise to discover that a social environment in which the dominant assumption is that 'it's every man for himself' is one that would not only encourage unethical behavior, but could become positively criminogenic* (138).

It is not that positive economists are unethical. Milton Friedman, for instance, had what might be called a passionate commitment to the value of political and economic freedom and, when he argues that the sole responsibility of executives is to their employers, he adds "conforming to their basic rules of the society, both those embodied in law and those embodied in ethical custom" (1970, 1). Heath points to the problem of over-enthusiasm, but some economists appear to have divided their commitments to personal and social virtues from their thinking and writing almost entirely. This also applies to behavioral economics, which has dropped the assumption that people are not entirely rational, and tries to find patterns of irrationality. This can be seen in a popular recent book, *Animal Spirits,* written by two well-known economists, George Akerlof and Robert Shiller. They appear to have written the book in haste and can be criticized at a number of levels—as by Richard Posner, a U.S. judge, in a review: *Shorting Reason.*[10] It is interesting that even the legally trained

[10]http://www.newrepublic.com/article/books/shorting-reason.

judge does not comment on their description of the concept of *fairness* as irrational. People do behave irrationally when their interests are threatened—for instance, as employees when their jobs are at stake, as discussed in the book. People may also use arguments involving fairness that are not rational. The need to create a fair society, however, is entirely rational—as we have seen. The more we are confident of fair treatment, the more we are free to concentrate our efforts on mutually beneficial production.

From a personal perspective, we can see the world in one of two ways:

1. We can live in the world of the cynic who believes that all people act purely opportunistically, in the sense that they will lie and cheat on agreements if they can—if not in every aspect of their lives, then certainly in business. On this view, one's concerns in business matters are to find ways of maximizing your own income, to create complete contracts to ensure you are not cheated, or incentives to ensure that your fellow workers do not shirk. Issues of ethics and virtue are irrational, and irrelevant except if you are penalized if you do not comply.
2. Alternatively, we can live in a world where we aim at developing our personal virtues and seek a vocation to develop relationships in communities where we respect and trust each other. One's concerns in business are the productivity of the organizations in which one serves, and that everyone is fairly treated and remunerated. This does not deny that people act opportunistically, but we recognize that this is aberrant behavior. We address it, reasonably and justly, by persuasion and possibly by sanction.

I have not found it easy to debate with those who hold the positivist view. It is ultimately a matter of personal commitment. Something can, however, be said to those who take the cynical position. It goes like this: if you believe that no one can be trusted, and that all people act to advance their own interests opportunistically, this must apply to you. If so, I cannot trust what you are saying. You have warned me that you are likely to be lying and manipulative, so there is really no point in listening to you—unless you change your mind on this matter.

Taking this approach is a little aggressive, and you may not want to start the fight. I confess that I have lacked the courage to make the point as often as I might, not only because I have not wanted to offend a generous host.

We turn in Part 3 to identify the opportunities to make the financial sector more virtuous: serving its social functions with integrity. In Part 4, we will return to our personal development, in order to seize the opportunities and fulfill the responsibilities, filling in the background reasoning for some of the suggestions made in Part 3.

Chapter summary: Adam Smith's arguments were for a free market and against influential business people extracting monopoly rents at the expense of others. In today's economy, financial companies extract rents when they overcharge their customers, and senior managements take rents when they are paid excessive remuneration. Many economists have failed to follow Smith and can even justify rent seeking rather than identify injustices. It is, however, virtuous to create entrepreneurial profits that justly belong to those who have created them. A vocation means adding value, and not extracting rents.

PART 3

The Purpose of Financial Services

In this part, we look at the work to be done in different areas of the financial sector—where it exploits its customers, and where is requires development in order to fulfill its social purpose. I appreciate that I deal in a sentence with some issues that may require a lifetime of work; missing 99 percent of the subtleties and difficulties. My point in raising them is to bring them to your attention—and to indicate my solidarity if you are already working on them! Even if they do not take a virtue ethics approach, the expert authors in John Boatright's book *Finance Ethics* cover the subject in more detail if you are interested.

Value for the Customer

You will know that there is an ongoing debate as to whether the sole purpose of business is to make a profit, or whether it has a social purpose in meeting people's material needs—with profit being one measure of how well it is doing so. Milton Friedman (1970) is perhaps the best-known expression of the former view, Peter Drucker well known for the latter. This section, and the next, outline an approach to management that creates this value in a manner based on service and integrity rather than greed and opportunism. Much of what I say comes from Drucker's book, *Management*. I recommend it without reservation: my copy has sat on my desk for 30 years. I used to say it sat between the bible and the dictionary—until the Internet made the latter redundant!

If Friedman is right, there would be nothing much to say about working in the finance or any other sector—as long as you were making a living. I think, however, Drucker's critique is unanswerable. He says:

> *Profit is not the explanation, cause, or rationale of business behavior and business decisions, but rather the test of their validity. If archangels instead of businessmen sat in directors' chairs, they would still have to be concerned with profitability, despite their total lack of personal interest in making profits* (1975, 60).

I am attempting here to refute an idea for which Adam Smith is famous:

> *It is not from the benevolence of the butcher, the brewer, or the baker that we expect our dinner, but from their regard to their own interest. We address ourselves, not to their humanity but to their self-love, and never talk to them of our own necessities but of their advantages* (2005, 19).

Smith was over-pessimistic about human nature in some respects. In particular, he was convinced that corporations would always fail because of the agency problem: managers could not be prevented from looking after their own interests to the exclusion of everyone else's. In this case, we can perhaps assume that his position in the class system meant that he seldom spoke to his butcher, brewer, or baker. In my world butchers, brewers, and bakers pride themselves on delivering the best possible products. Our local butcher would be genuinely offended if told he chose his cuts to maximize his profits rather than to please his customers!

To return to Drucker's argument:

> *It is irrelevant for an understanding of business behavior, profit, and profitability, whether there is a profit motive or not. . . . We do not learn anything about the work of a heart specialist by being told that he is trying to make a livelihood, or even that he is trying to benefit humanity. The profit motive and its offspring maximisation of profits are just as irrelevant to the function of a business. . . .* (1975, 60).

I confess to have personally fallen into the error of not wanting to make enough profit. The South African government removed small loans from the ambit of the Usury Act in the early 90s. The idea was to attract legal commercial institutions into this market to compete with informal loan sharks. The hope was that credit would be cheaper and it would reduce the violence associated with the informal recovery of bad debts. The main entrants to this new formal market became very profitable, charging interest rates of around 60 percent, which was probably half that previously charged by loan sharks. I became chair of the board of a small not-for-profit that entered the market with interest rates of less than 30 percent, because we felt that anything more was unfair. In retrospect, that was a mistake. We were successful on a small scale but were always strapped for resources, and the organization was wound up a couple of years after I left. We would have been more successful if we had charged more to provide the resources to expand. My thinking was anchored in the idea that capital has to come from investors and not customers. I was also too focused on providing value for existing clients rather than thinking of the wider picture. Creating value in business does mean you have to invest with some enthusiasm, and may need to charge more to do so.

Drucker goes on to address the core strategic task of any business, which he says is to:

> *To know what a business is, we have to start with its purpose. Its purpose must lie outside of the business itself. In fact, it must lie in society since business enterprise is an organ of society. There is only one valid definition of business purpose: to create a customer* . . . (1975, 61).

He goes on to distinguish between the product and utility gained by the customer, and idea taken up by Theodore Levitt as the *marketing concept*. This defines marketing as providing for the needs of clients at a profit. We can contrast this with a product orientation, and with a sales orientation, which confuse the means (being the product or sales process) with the ends (the needs of the customer). Levitt's classic *Marketing Myopia* shows the dangers of failing to appreciate this contrast. He suggests that the American railroads lost their dominant position in the transport industry in the 19th century—by failing to see that their business was "transport" and not "the running of railways." With the marketing concept, it is more likely that companies will abandon existing product and sales methods and introduce new products as customers' needs change. It is to seek to meet your customers' real needs, which also see as an application of the golden rule, "Do unto others, as you would want them to do to you." Exploitation of your customer may generate short-term profits, but it is not the action of a virtuous person—nor likely to be profitable in the end.

The first three chapters of this part cover investment management, insurance and pensions, and banking and include some related issues. Those related to corporate governance and reporting seem to fit with investment management; issues around selling and mutual organizations with insurance and pensions, while risk management fits well with Chapter 9. Chapter 10 then covers regulation as it pervasive in all organizations, and relevant to how we encourage each other to ethical behavior. The final chapter is about financial services for the poor. Whatever your particular role, there are challenges and opportunities for you to make a difference.

CHAPTER 7

Investment Management[1]

The social purpose of investment management is then the allocation of capital to its most productive application on the right-hand rotor of Figure 1.2. As mentioned above, families and governments perform much of this function outside the market. In this chapter, I barely touch on ways of financing small business (often family owned), which is where much of the most creative work in finance takes place. If you are interested, the paper by Allen Berger and Gregory Udell gives a good idea of this process and its participants, as well as warnings about the risks. Small and medium enterprises (SMEs) are widely regarded as major contributors to job creation. In size terms, however, they are not important to insurance and retirement fund monies, and the surplus wealth of richer families and sovereign wealth funds, the management of which is the subject of this chapter. The chapter therefore covers fund managers, merchant banks, and venture capital.

The productive application of capital means maximizing its return, with due allowance for the potential harms that may arise—that is the risks to all stakeholders. The first two sections of this chapter address the mathematics of profit maximization, and the necessity of fundamental analysis—concepts the implications of which are not always appreciated, but which contribute both to private and public good. The following section looks at the need for the investment management industry to fulfill its responsibilities in corporate governance, including the development of appropriate accounting standards and that shareholder votes are exercised. This is followed by a discussion of overcharging and over-servicing and another on potential social and environmental harms. These are *common good* problems that require the exercise of wisdom and justice. The

[1]This chapter is based on Asher (1998a).

chapter ends with the ethical standards of the CFA Institute, which is worth joining if you are active in this industry.

The Maximization of Profits

While the theory of profit maximization is taught in first year economics classes, its implications often seem misunderstood. I have found this in many of my bright final year actuarial students, and in business people in responsible high positions.

Marginal Costs Equal Marginal Revenue

Profit is maximized when a business sets its prices so that marginal cost equals marginal revenue. This requires the manager to have determined which of the costs are marginal, and to have some idea of the response of demand to changes in price, what economists call elasticity. I have, however, often come across business decisions where profits have been reduced because a line of business has been closed on the specious grounds that average costs (including allocated overheads) have been above average revenue. Joel Stern, with his trademarked *Economic Value Added*, has made a career helping managers in large U.S. companies to understand the concept.

This book is obviously not the place to explain this concept in detail, but you might like to return to your microeconomic textbook to confirm its relevance. My favorite example is *the revenge of the gnomes*. My father once took over responsibility for a concrete railway sleeper manufacturer that made little concrete gnomes from bits of concrete left over from a batch. Before his arrival, head office accountants had decreed that the gnomes should go because they were unprofitable. The next few tenders for sleepers were, however, lost because the price was too high. My father discovered that the marginal cost of producing the gnomes was almost zero, because the concrete would otherwise have been discarded. Their contribution to overhead had been enough previously to ensure profitability.

Financial service companies are not immune. I understand that Australian banks closed branches across the country in the 90s because the branches produced a lower than average return on capital—but not lower than the cost of capital. The country towns that lost their branches suffered considerably. Similarly, Nedbank in South Africa closed many of their three million accounts of black customers in the closing days of apartheid, many of which would have been marginally profitable—particularly as black wages were rising fast. Again, the poor and marginalized suffered.

There may be other reasons for these unprofitable and socially harmful decisions. The Nedbank board would not be the only one to spite itself out of racial prejudice. Australian directors may have disliked travelling to rural towns. It seems to me, however, the best explanation appears to be that they do not fully understand the consequences of the mathematics.

Overstated Equity Risk Premium

Related to this misunderstanding of marginal cost is overestimating the expected equity risk premium—being the excess return expected on equities compared with government bonds. Projects will contribute to maximizing profit if they earn a return in excess of the cost of capital. The cost of capital is some weighted average of the cost of debt plus the return that shareholders want. The problem is that it is not entirely obvious what shareholders want. The one way of finding out is to see what they have earned in the past, the realized equity risk premium. This depends very much on the period over which the return is measured. A careful analysis—such as those performed by leading British actuary, David Wilkie, suggests that one could expect the equity risk premium to be between 3 percent and 5 percent pa. Elroy Dimson and his colleagues have since examined equity returns since 1900 in all countries and come up with a world average of about 4 percent pa. Until recently, however, academic economists have been using much larger numbers. As Aswath Damodaran, himself an academic, said:

> *At the risk of sounding harsh, the risk premiums in academic surveys indicate how far removed most academics are from the real world of valuation and corporate finance and how much of their own thinking is framed by the historical risk premiums they were exposed to back when they were graduate students* (2009, 305).

Overstating the cost of capital can have significant practical consequences. A British actuarial working party chaired by Chris Lewin reported:

> *We believe that the popular misrepresentation of the conclusions of financial economists has had significant practical consequences. In short, companies are currently failing to invest in projects that should be profitable for them, because they are seeking too high a target rate of return on prospective projects. They have possibly been led to this position by the abnormally good returns on shares experienced during the 1980s, and have been led into thinking it correct not to invest unless they can expect the same abnormally good returns again. . . . we conclude that an appropriate 'risk premium' for the assessment of capital projects is not as high as the 7% p.a. or more that has been quoted in a number of articles recently* (1995, 168).

Expected Present Value or Return on Capital?

The third related error is to think that maximizing profits is the same as maximizing return on capital employed. Doing this has exactly the same effect as overstating the equity risk premium: it again turns away from projects, products, or branches that increase profits by contributing to overheads.

Creating Investment and Economic Activity

In perhaps his most famous passage, John Maynard Keynes suggests that:

> *Most, probably, of our decisions to do something positive . . . can only be taken as the result of animal spirits – a spontaneous urge to action rather than inaction, and not as the outcome of a weighted average of quantitative benefits multiplied by quantitative probabilities* (1936, 161).

He is explaining why a reducing interest rate does not necessarily lead to greater investment. His reasoning is that:

> *. . . human decisions affecting the future, whether personal or political or economic, cannot depend on strict mathematical expectation, since*

> *the basis for making such calculations does not exist . . . it is our innate urge to activity that makes the wheel go around . . .* (1936, 162).

The context was the Great Depression of the 30s with massive unemployment. Keynes' solution was that if businesses were not initiating economic activity—and they were not in spite of low interest rates—governments should do so. Economists then and now accept that increased economic activity requires investment, and the problem of insuring full employment requires the maximum of (productive) investment.

Investment is profitable if it yields more than the cost of capital, so from one perspective one can argue that businesses fulfill their social responsibility by increasing investment until profits are maximized. The insights of this section are therefore central to businesses fulfilling their social purpose, even when they are defined very narrowly. The mathematically correct approach to profit maximization can lead to the justification of many socially desirable projects that are otherwise apparently not profitable. In particular, it is profitable to provide services to the poor on a marginal basis if they otherwise would not be sold at all. Long-term investments, of which renewable energy is perhaps the most topical and socially productive, may well be profitable at realistic rates of discount.

Of course, we must accept Keynes' point that there is huge uncertainty when investing in new projects. Business decision makers ought to be skeptical about the assumptions underlying mathematical present value models. There is, however, no other way of making the assumptions explicit and allowing those with the greatest expertise to contribute to a joint decision. There are the opposite pitfalls of overoptimism and excess caution, but there is no need to compound these by misunderstanding the basic mathematics. Everyone who plays a role in these decisions, from the junior analyst to the Chairman, has a social responsibility to create profitable economic activity. This creates customers, which as Drucker says, is the only "valid definition of business purpose."

One can do so by ensuring that the discount rate used for projects has been updated to take into account the very low rates of interest being experienced around the world. In evaluating long-term projects, allowing for risk by a level percentage reduction in estimated cash flows, rather than an increase in the (compounded) discount rate, may well show that more projects are viable. Correctly calculating overheads may show that expanding business into new areas may cover marginal costs and so be profitable. When visiting companies and talking to management, investment managers can indicate that they are favorably disposed to profitable growth as much as cost cutting, and are not impressed by counter-productive return on capital targets.

Performance Measurement

Maximizing returns also means monitoring performance and costs. In some instances, fund managers could monitor their own performance more carefully, and those that use their services may find it pays to be diligent in ensuring that they do. My experience on investment committees is that there is too much talk about general economic activity, and too little about what has actually happened to the portfolio, especially expenses.

The approach described in Asher (1998b) can prove useful. It involves looking at every buy and sell decision made by a manager and evaluating whether it was good or not. Given that the managers are making many decisions, this can be statistically more powerful than standard measures of relative performance. For one new investment manager employed by a company of which I was a director, it showed significant results 6 months before the standard measure. For another manager, it enabled me to persuade him to reduce trading that was detracting from performance. The paper by Rick Di Mascio and colleagues is considerably more thorough than mine, and confirms that the methodology has value.

Monitoring share trading is necessary to ensure that you are getting a fair price. Especially in these days of high frequency trading (HFT) and dark pools, investors need to be sure they know the extent to which the prices they pay differ from the value weighted average price (VWAP) on a daily and weekly basis. It is quite possible for a less informed investment manager to use trading tactics that can be recognized and exploited by a computer algorithm. It is also possible for fund managers, brokers, or custodians to favor some funds at the expense of others in the allocation of trades at the end of the day. We can all be tempted to dishonesty and so it is better for all of us to know that there are many people checking on propriety. Given modern computing power, it is not expensive.

Fundamental Investing

Broadly, three approaches can be taken to investment analysis.

1. The first is technical analysis. For some this still involves the interpretation of charts—looking for *support lines* and *breakouts*. Today, however, technical analysis is more likely to involve the complex mathematical analysis of share prices, the weight, and pattern of orders in the market, and the timing of important news. Technical analysts can profit from the signals given by other market participants if they follow recognized patterns. HFT is a current fashion and can profit from any predictable trading strategy. Technical analysis may be clever, but it is mostly a zero sum game—merely taking from other investors.
2. The second approach is passive investment or indexing. It is based on the observation that the average investment manager performs in line with market averages and so wants to minimize the cost of investment management. It saves costs by assuming that other market participants have efficiently priced the assets.
3. Fundamental analysis looks rather at the future profitability of the businesses in which it invests, and makes a considered judgment as to whether the share price is relatively cheap or dear. Fundamental investors may supplement their judgment by looking at technical factors to determine the view of other investors.

Those using only the first two approaches are free riding. They do not attempt to evaluate the underlying value of the shares, but are benefiting from those who do.

I may be being a little unfair in that technical investors may contribute by reducing the impact of behavioral biases. They are, however, relying on more informed investors to bring prices back to something closer to a fair value. If some of the technical analysis fascinates you, you are not alone, but comprehensive, fundamental, analysis is necessary to ensure prices do not become unreasonable. Formulae-based approaches looking backward at historical data that ignore large amounts of information relevant to future profitability are, by definition, short-sighted.The rcent research of Jennie Bai and her colleaguesfinds some improvement in the ability of share prices to predict long-term future returns in the U.S. markets. This means that the US market, at any rate, has become a little better at allocating capital to more productive uses. The improvements are limited to some sectors, to growth stocks, and stocks that have more active options markets. This is a fascinating finding with two consequences:

1. Growth stocks are associated with momentum rather than fundamental investment—but the improved pricing benefits are only found after a period of 5 years, which is much longer than the benefits of momentum. If Jennie Bai's findings are valid, the greatest improvement in socially useful investment seems to have come from those who make a fundamental analysis of growing companies. They then join fundamental investors in value stocks such as Warren Buffett.
2. The presence of derivatives has improved the pricing efficiency, which suggests that hedge funds have contributed in this area. We discuss their challenges below, but this fact may be some encouragement for those who work in this area.

Returning to the question of free riding; if the market is efficient then fundamental research will yield no additional returns. If you follow the annual letters[2] of Warren Buffett, you will find he continually predicts that future outperformance will not be as good as the past. Fundamental investors like him have, however, continued to outperform. Much of this has been possible because they read the irrational exuberance of the tech bubble, in the years before 2000, and the banks before the 2008 financial crisis. My suspicion is both of these were aggravated by the large number of technical and passive investors who were making no real attempt at evaluating the future profits of the companies concerned.

[2]These are compulsory reading for those who work in this sector. Accessed August 30, 2014. http://www.berkshirehathaway.com/letters/letters.html.

Communicating Uncertainty

This might be thought to be a good thing for fundamental investors, who can profit at the expense of those blindly following the herd, but it is not that easy. Jeremy Grantham illustrates the problem when he finds that his sister's pension has been the most successful of the portfolios he has invested for others. As he has been confident that she will not replace him, he has been prepared to accept relatively poor returns in excessive bull markets. It is difficult to bet against irrational exuberance, and if you do not have the reputation and control over your assets that Buffett has enjoyed, you will lose your clients or your position if you sell out too early.

The problem of communicating uncertainty is common to professionals. As Daniel Kahneman puts it in the context of doctors:

> *Experts who acknowledge the full extent of their ignorance may expect to be replaced by more confident competitors, who are better able to gain the trust of clients. An unbiased appreciation of uncertainty is a cornerstone of rationality—but it is not what people and organizations want. Extreme uncertainty is paralyzing under dangerous circumstances, and the admission that one is merely guessing is especially unacceptable when the stakes are high. Acting on pretended knowledge is often the preferred solution. Clients do not like being told that outcomes cannot be predicted, and you risk losing them if you emphasise the uncertainty* (2011, 263).

Getting it right requires a commitment to integrity and an ability to communicate clearly and credibly that does increase your listeners' confidence. Good investment managers work hard at it. It is central to Buffett's annual letter. At the end of 2014, the investment manager of a unit trust in which our family invests, Simon Marais, reported[3] that he had beaten his benchmark by a superb 8.5 percent over the past year, and took the opportunity to tell investors about the mistakes he had made. All the better to do it, as the following quarter saw a complete reversal of fortunes.

The responsibility to get markets to focus on fundamentals also lies with companies. It is unhelpful to adopt the view that investors are only capable

[3]Accessed December 18, 2014. https://www.allangray.com.au/documents/Allan-Gray-Australia-Quarterly-Report-Sep-2014.pdf.

of short-term simplistic analysis. In a recent Harvard Business Review interview, retired IBM CEO, Sam Palmisano, suggests that the problem of short-termism lies not with investors that cannot understand but rather with "the maturity of management. You can come up with a long-term orientation that the investor can measure" (2014, 83). The lack of maturity is presumably referring to a lack of confidence, or a short-term perspective of their own.

A Role in Corporate Governance

Fundamental investors are interested in true underlying performance and will be interested in ensuring the appropriate corporate governance: in the election of management, and in proper accountings and auditing.

Voting for The Board

Investment managers will normally have the right to exercise the vote at shareholders' meetings. This gives them a crucial role in the governance of companies.

During the Great Depression, Adolf Berle and Gardiner Means produced the classic analysis of modern corporate governance. They suggested that passive shareholders have effectively forfeited the right to see the corporation as their private property, and that directors and senior managers (management) enjoy relatively unfettered power. They ask:

> *have we any justification for the assumption that those in control of a modern corporation will choose to operate it in the interests of the owners? The answer to this question will depend on the degree to which the self-interest of those in control may run parallel to the interests of ownership and, insofar as they differ, on the checks on the use of power which may be established by political, economic, or social conditions* (1933, 113).

Even at that time, they point out that some companies had more power than governments:

> *The rise of the modern corporation has brought a concentration of economic power which can compete on equal terms with the modern*

> *state – economic power versus political power, each strong in its own field. The state seeks in some aspects to regulate the corporation, while the corporation, steadily becoming more powerful, makes every effort to avoid such regulation . . . The future may see the economic organism, now typified by the corporation, not only on an equal plane with the state, but possibly even superseding it as the dominant form of social organization. The law of corporations, accordingly, might well be considered as a potential constitutional law for the new economic state, while business practice is increasingly assuming the aspect of economic statesmanship* (1933, 313).

Since they wrote, investors have become even more removed from control as the assets are held through pension funds, companies have become larger, and managers have become more powerful. Control has also become more concentrated. Stefania Vitali and her colleagues have used sophisticated mathematics to map control of the largest companies in the world. They find:

> *In detail, nearly 4/10ths of the control over the economic value of TNCs (Trans National Corporations) in the world is held, via a complicated web of ownership relations, by a group of 147 TNCs in the core, which has almost full control over itself. The top holders within the core can thus be thought of as an economic "super-entity" in the global network of corporations. A relevant additional fact at this point is that 3/4ths of the core are financial intermediaries* (2011, 6).

To some extent, the financial intermediaries (banks and insurers) they identify are neither ultimate owners nor ultimately in control because the intermediaries are acting as trustees for a significant proportion of their assets. But they also make the point that the level of concentration is understated to the extent that the management of the 147 core TNCs are trained to think along the same lines. In such circumstances, *groupthink*, which is unable to evaluate its own weaknesses critically, may proliferate.

Someone must monitor management, and shareholders are meant to fulfill the role. The trouble is a classic *common good* one: the management is a small well-organized group, the shareholders dispersed, unorganized, and operating through financial intermediaries with strong links to management. Managements limit shareholder power by moving their companies to jurisdictions that allow them to entrench the board; taking golden parachutes; and keeping shareholders in the dark—by manipulating accounts and not disclosing relevant information. The marketing division may appear to have more power over the content of annual reports than the accountants. Managements also use their lobbying power and make it difficult for shareholders to organize and exercise their authority. In some jurisdictions, investment managers can be told (by regulators in some cases) that they can only fulfill their rights to exercise votes if they can demonstrate that the benefits exceed the costs to their clients. Similarly, groups of shareholders are prevented from collaborating in applying pressure on management without potentially being required to make an offer for the whole company. Their power to vote on the remuneration of executives is often curtailed.

Competent investment managers can intervene positively in the affairs of the companies in which they have invested on behalf of others. Warren Buffett makes a virtue out of it: at one point becoming Chairman of Salomon Brothers when it seemed expedient. In his annual letters, he stresses that operational decisions are left to management, but it is also clear that he knows what they are doing and that they are accountable to him. Simon Marais also intervened at times.[4] Calpers, the Californian public sector retirement fund, partly because it is so large, has taken a passive investment management strategy, but has an active governance approach:

> *We seek corporate reform to protect our investments. The global governance team challenges companies and the status quo—we vote our proxies, we work closely with regulatory agencies to strengthen our financial markets, and we invest with partners that use governance strategies to earn value for our fund by turning around ailing companies.*[5]

To the extent to which it is a *common good* problem, it cannot be fully addressed by individual competence and ethical standards. It requires the construction of institutional arrangements that constrain management, and

---

[4]One incident is reported in the same report referred to in note 4 above.

[5]Accessed November 24, 2014. http://www.calpers-governance.org/.

direct its activity into profitable and productive areas. These arrangements could also include structures in which shareholders can discuss the performance of different managements. There will need to be accountability to prevent frivolous and vexatious accusations. The idea of incorporating other stakeholders in such arrangements has attractions. The European corporate governance model gives workers half the seats on supervisory boards of directors. This seems a sensible manner of recognizing their participation in the company and ensuring that managements are better monitored.

Accounting and Earnings Management

A classic joke on company reporting goes:

> *A company is going through the interview process in order to hire a chief financial officer. In the last interview session, each of three finalists is given the company's financial data and asked, 'What are the net earnings?' Two applicants diligently compute the net earnings. Neither of them gets the job. The candidate who lands the position answers the question by replying, 'What do you want them to be?*[6]

I thought this was funny when I first heard it, but now I see it as the single most powerful corruptor of young accountants, actuaries, and other financial professionals—and warn my students as they go into their first jobs. Unless alerted to this possibility, they may be blissfully unaware of the underlying motivation for the instructions they are receiving, and find themselves compromised later.

In many companies, they will be asked to provide a variety of results so that the CFO and CEO can decide what the profits will be. In writing this, I can hear some acquaintances of mine objecting that this is nothing remarkable: the CEO has a duty to ensure that the reported profits are fully reflective of the business. There is a problem, however, to the extent that the concern is with impressions and not reality—attempting to give the right message to shareholders to inflate the share price. Subjecting your customers

---

[6]Accessed November 24, 2014. http://www.investopedia.com/university/accounting-earnings-quality/.

to puffery is one thing; they expect it and the law requires them to take care. Attempting to fool the shareholders, to whom you owe a fiduciary responsibility, is fundamentally dishonest. I am not so naïve to believe that reporting earnings that are more volatile will have no negative effect on the share price, but do believe—with Sam Palmisano—that the long-run impact of trustworthy reporting will be positive all round. It would reinforce the integrity of the accountants, give financial managers and analysts clearer insights, and so lead to better use of capital both in and outside of companies.

The practice of earnings management seems almost universal. Leonard Brooks covers the how and why, and reports research that a large majority of U.S. companies were guilty in the 90s. It is possible that Sarbenes-Oxley has reduced its prevalence subsequently.

One institutional structure that can limit manipulation is the actuarial analysis of surplus. This looks explicitly at all the assumptions underlying the calculation of insurance assets and liabilities, and reports on the difference between actual and expected experience, and the effect of changes in assumptions and methodology. It therefore identifies over-optimism and discourages arbitrary changes to method and assumptions. The same approach can be used for accruals, depreciation, and the impairment of assets as well as estimates of all contingent assets and liabilities.

I have included this topic under investment management, as investors, preeminently, have the responsibility to see through manipulation and to make it clear that massaging the results undermines their confidence in company managements.

Overcharging and Over-Servicing

Just as investment managers have a duty to oversee management remuneration and to develop institutional structure that facilitate this, those who appoint the investment managers have a similar duty to manage overcharging in this industry.

Perhaps the first institutional change required here is to make clear the extent of hidden charges. This means investors need to be:

- Monitoring what is being paid to merchant banks and other consultants who assist with capital raising, and being

conscious of conflicts of interest where investors are being advised by the same people who profit from capital raising.
- Requiring stockbroker fees to be fully reported and not just capitalized in the purchase price of shares.
- Obtaining information as to the relative yields they are obtaining on bank deposits and the relative prices paid for foreign currencies and future contracts.
- Avoiding investment in funds or instruments that in turn invest in other funds, which also charge fees on the same assets.

Thomas Philippon and Jennie Bai find that there has been no reduction in the charges made in financial markets since 1900 in spite of significant increases in size and turnover—and the reductions that computers have made in administration costs.

John Bogle, the founder of Vanguard, and prime advocate of indexed investing, has argued that the active investment managers are "enormous parasites with their fees and transaction costs eating into returns earned by the ultimate host: public corporations."[7] Many believe that investment management fees are too high; if so there is an entrepreneurial opportunity to introduce lower cost active management. Perhaps this is your vocation.

Derivatives

The social justification of derivatives is that they allow more participants into investment markets and so improve prices—increasing the efficiency of capital. They have been used for centuries in commodity markets to enable producers to reduce their risk. In investment markets, they allow for shorting of assets so increasing the number of potential sellers and reducing the chance of bubbles. Unfortunately, human nature appears to be unrealistically optimistic, and more people seem to use derivatives to drive prices up rather than down. This may not, however, provide reason to disallow them—or even disapprove of them.

There are reasons nevertheless why they should have a smaller role in financial markets than currently. Some derivative markets seem to

[7] "Vanguard's Bogle responds to 'parasite' tag." *Financial Times* August 25, 2013.

have thrived because of opportunities for tax arbitrage, or because the markets in the underlying have been slow to adopt new technologies and have thus been more expensive in which to trade. Regulators and market service providers have the challenge to remove these costly distortions.

Other derivative markets have developed because they have provided an opportunity for powerful players to extract rents from their clients. Hedges that leave a considerable basis risk fall into this category. If you are likely to need catastrophe cover, or want to invest in companies that provide insurance, you would be better to deal with an insurance company that provides compensation for losses rather than a merchant bank that is offering a type of gamble. I am particularly appalled by the idea of providing index-based insurance to poor farmers as has been suggested.

Egregious examples of the powerful fooling the gullible can be found in the hedge fund industry. Of course, some insightful hedge fund operators have identified mispricing in the markets and made large profits for their clients. For many funds, however, their operating models are so opaque—and the fees so large—that it is foolish to invest in them. Given the opacity, it is not surprising that Vikas Agarwal and Narayan Naik found:

> *a large number of equity-oriented hedge fund strategies exhibit payoffs resembling a short position in a put option on the market index and therefore bear significant left-tail risk* (2004, 63).

It is known that hedge funds are large investors in catastrophe bonds—which consist in "a short position in a put option." If not disclosed to investors, this is effectively fraud: the funds are holding themselves out as superior investors, but anyone can sell out-of-the-money options to make short-term profits—by assuming large risks that occur infrequently. If you are operating a hedge fund, and think you are worth the high fees they normally charge, you could raise standards in the industry by subjecting yourself to some independent review or reporting directly to your clients (in arrear if necessary to protect intellectual capital). If you are to investing or thinking of doing so, do not expose yourself to the risk of being taken for a ride.

Socially Responsible Investment

One of my more interesting past roles was as non-executive Chairman of the Community Growth Fund, which invested union retirement moneys using social criteria. The union organizers were involved in the evaluation of potential investments against the criteria, and the organizers were often able to provide insights not available to our investment managers and researchers. Such insights typically consisted of an alternative view of the implementation of company policy, often relating to health and safety and in the South Africa of the time, to discrimination. One hotel group assured us that their facilities were all desegregated, but the union told us that only white staff were permitted to use the guest toilets!

The United Nations coordinates a number of socially responsible initiatives. Two, of note, are the UN Global Compact, which includes the principles that business has responsibilities to avoid harm to stakeholders and the environment, and the Principles for Responsible Investment as set out below:

> *As institutional investors, we have a duty to act in the best long-term interests of our beneficiaries. In this fiduciary role, we believe that environmental, social, and corporate governance (ESG) issues can affect the performance of investment portfolios (to varying degrees across companies, sectors, regions, asset classes and through time). We also recognise that applying these Principles may better align investors with broader objectives of society. Therefore, where consistent with our fiduciary responsibilities, we commit to the following:*
>
> 1) *We will incorporate ESG issues into investment analysis and decision-making processes.*
> 2) *We will be active owners and incorporate ESG issues into our ownership policies and practices.*
> 3) *We will seek appropriate disclosure on ESG issues by the entities in which we invest.*
> 4) *We will promote acceptance and implementation of the Principles within the investment industry.*

5) *We will work together to enhance our effectiveness in implementing the Principles.*
6) *We will each report on our activities and progress towards implementing the Principles.*[8]

Clearly companies have a duty, stemming from justice, to consider the impact of their operations on all their stakeholders. Not to do so places their profits and even their license to operate at risk. Governments have the responsibility to ensure that no harm is done, making it necessary that companies report potentially harmful impacts. The *triple bottom line*, coined by John Elkington, is a helpful phrase that refers to evaluating and reporting on the effects of a company's operations in financial, social, and environmental terms. Potential social and environmental risks and the consumption of social and environmental capital are clearly relevant to all stakeholders.

There are also a number of non-profit initiatives and research organizations in this space, and their development represents another opportunity to contribute. It would be good if they could adopt a more holistic approach that included fundamental investment factors as well as the social and environmental obligations.

In this context, it is normally inappropriate, and a risk to democratic government, to encourage companies to use their power for collateral purposes, even apparently good causes. I say normally, because the pressure brought to bear on the apartheid government by foreign owned companies did help bring about change—and provide an instance where the end justified the means. This was, however, a case of significant injustice. There are ongoing opportunities for similar campaigns; one can think of reprehensible behavior on the part of companies unfairly exploiting workers in poor countries or creating environmental destruction.

In spite of my involvement in the Community Growth Fund, I am reluctant to champion specialist ethical investment funds and would prefer to see the mainstream become more virtuous. Tobacco, other dangerous drugs, weapons sold to tyrannical regimes, pornography, and the sex industry are unacceptable to many if not most investors—even

[8]Accessed August 30, 2014. http://www.unpri.org/about-pri/the-six-principles/.

where they are legal. Bribery and failure to meet decent safety standards are the same. As long as their approach is sensible and disclosed to investors, I cannot see how fiduciary responsibilities to invest in the best financial interests of their clients requires managers to invest in activities they find morally reprehensible. I accept that it is a matter of conscience and the need to pick winnable battles. You may have a different list of unacceptable industries. If your conscience, however, is so robust it never blanches, then perhaps you could think more carefully about the risks and the possible harm done to others. If you find that you cannot invest in most companies, then there are more focused investment managers, such as those attached to the Global Impact Investing Network,[9] looking to ensure that their investments make an impact.

Using social criteria to screen investments can create unexpected results. If enough investors decide to shun a suspect company for non-financial reasons, its share price will decline and investment will appear unprofitable, and its cost of capital increase. If the company survives, however, it will provide higher returns from its lower base. Investors that ignore the moral stigma attached to such companies may be said to be beneficiaries of moral arbitrage. Similarly, socially responsible investors who lead a trend to social investment may outperform the market, but if the companies in which they invest thereby obtain a lower cost of capital, they will subsequently underperform! The complexity of these effects makes it difficult to judge whether social criteria add to performance or not.[10]

This does not prevent private initiatives to create businesses where all the investors are prepared to accept lower returns or take greater risks, such as in social impact investing.[11]

CFA Institute Standards

As the leading professional body in this part of the financial services industry, the CFA Institute deserves credit for its ethical standards. If you work in the area, become a member for the technical and social support they give,

[9]Accessed December 11, 2014. http://www.thegiin.org/cgi-bin/iowa/home/index.html.

[10]Asher (2005) illustrates this issue from the performance of the Community Growth Fund.

[11]Accessed April 16, 2015. http://www.thegiin.org/cgi-bin/iowa/home/index.html

and for the opportunity to contribute to the reforms that they advocate. I close this section by quoting their *Statement of Investor Rights*[12]:

> *When engaging the services of financial professionals and organizations, I have the right to . . .*
>
> 1) *Honest, competent, and ethical conduct that complies with applicable law;*
> 2) *Independent and objective advice and assistance based on informed analysis, prudent judgment, and diligent effort;*
> 3) *My financial interests taking precedence over those of the professional and the organization;*
> 4) *Fair treatment with respect to other clients;*
> 5) *Disclosure of any existing or potential conflicts of interest in providing products or services to me;*
> 6) *An understanding of my circumstances, so that any advice provided is suitable and based on my financial objectives and constraints;*
> 7) *Clear, accurate, complete, and timely communications that use plain language and are presented in a format that conveys the information effectively;*
> 8) *An explanation of all fees and costs charged to me, and information showing these expenses to be fair and reasonable;*
> 9) *Confidentiality of my information;*
> 10) *Appropriate and complete records to support the work done on my behalf.*

Chapter summary: Other things being equal, welfare is enhanced if investment is allocated to companies and projects that yield maximum returns—based on fundamental analysis and a realistic estimate of long-term real returns. Having shareholders' votes gives investment managers opportunities to improve corporate governance that benefits all stakeholders. Companies in which they invest should report on the triple bottom line that includes social and environmental impacts. Reducing overcharging and over-servicing is an ongoing challenge. Some derivative trading also appears to represent over-servicing.

[12]Accessed August 30, 2014. http://www.cfainstitute.org/learning/future/getinvolved/Pages/statement_of_investor_rights.aspx.

CHAPTER 8

Insurance and Pensions

This chapter covers life, property, and other insurances including lifetime pensions. I ignore social security benefits, assuming that they need to be supplemented by private benefits.

The needs are for financial security: to protect the family fortune from unexpected losses that would lead to financial hardship. The needs are perhaps not all obvious, and it can be difficult to persuade breadwinners to buy our policies. This applies not only to death cover—perhaps the only product that can only be bought as a gift—but also for disability, and some property, health and public indemnity insurance. This is why in many countries, such insurance and pension contributions are compulsory.

The chapter also covers hard selling, which is a species of over-servicing, the need for virtue in the management of moral hazards, and the role of mutual organizations.

Hard Selling

Hard selling is not purely a life insurance phenomenon, but this is perhaps where it started.

The origins of retail insurance go back at least several centuries, with—life insurance particularly—increasingly being sold by commissioned agents. Life companies may have developed the largest and most aggressive commissioned retail sales force of any industry. The hard sell leads to high lapse rates, at significant cost to those who have paid for the high commissions that typically consume most of the first 2 years' premiums. The lapses may partly come from policyholders changing their minds once no longer exposed to the hard sell; but when I once sent letters to our policyholders asking why they had stopped their premiums, the only replies were from those who apologized because they were no longer able to afford the premiums. Policy design should allow for some flexibility in premium payments when incomes fluctuate.

The strong financial incentives are, however, not sufficient to prevent many wouldbe salespeople failing. There is a great deal of emotional rhetoric, much of which is pure manipulation. Their employers are not beyond repossessing homes to recover commissions paid in advance of premiums that are never received.

Life insurance salespeople also offer financial advice, but it is difficult to ensure that they are adequately trained, while the incentive structure is often counterproductive. Misselling scandals illustrate this the best, with the UK regulators being particularly active in forcing companies to pay billions in compensation for wrongly sold policies.

I have, however, known successful salespeople who invariably go out of their way to help their clients and believe in the products they are selling. When I was actuary of the Prudential in South Africa, I often shared lunch with salespeople in our canteen. Commission rates were a common topic of conversation. Our most popular product allowed them to dial their commissions up and down—from about 15 percent to 75 percent of the first year's premium. I was often asked to remove this facility and set commissions at the maximum 75 percent, which was what our competitors were doing. Some of the branch managers put limits on the commissions that their staff could take. The Durban branch limit was as little as 30 percent—and it should be noted that the branch manager's bonus was itself directly related to the commissions earned by his staff. He was a man of real virtue!

In spite of this, the industry frequently claims that people have inadequate life cover—suggesting that the system fails, in any event, to distribute to all who need it. It is a challenge to find ways to distribute insurance more effectively. There are many who think that the sales process is too expensive and too aggressive. I know of a number of people who have left the industry for this reason. I am one; although I am presently helping to get a business going that makes use of the internet's new powers in order to reduce the costs of distribution. Much of what is currently sold on the web is even more expensive and exploitative of the gullible—as the sale of funeral policies to pensioners discussed above. It seems likely, however, that creative ways to use it will be found, and will offer good value.

If you need to address the challenge of making sales effective, and ethical, the work of Guy Oakes, and that of Donald Langevoort may be useful. They explore the emotional and ethical pressures of life insurance (and investment broker) sales from sociological and legal perspectives, respectively. They consider the extent to which individuals can deceive themselves and how company structures can facilitate this—and justify increasing levels of deception because the initial objective (benefits for widows and orphans) is socially justified. If you have been subject to, or observed, the emotional hyperbole of a life insurance sales convention, you will understand what they mean. If you have felt uncomfortable with the hyperbole, your discomfort is probably justified.

Standing against flagrant hyperbole and greed requires courage, preparation, and patience to find the right time to act. To make an impact, you will probably need the imagination and technical competence to show that:

- There is a better—more honest—way of selling.
- Acceptable levels of income can be made by the better way.
- The risks of continuing in the current direction are too great to sustain.

Over-Promising

Hard pressure sales can also lead to exaggerating potential investment returns. It is easier to resist the temptation if regulators impose maximum illustration rates. In any event, it requires courage to stand up against those who use inflated projections. Again, some creativity may be called for. One solution is to illustrate at more than one rate. This communicates the uncertainty and still allows for comparisons with competitors if they use an optimistic rate.

Intentionally underfunded defined benefits pension schemes fall into the same category. Barton Waring has described the problems and issues in the United States, but the problem happens all over the world—in schemes that cover politicians and civil servants particularly. The costs of generous benefits have been understated, which has benefitted existing members, pensioners (especially those on large pensions who often made the decisions), and future generations will be asked to pay. Waring talks of the need for *tough love*, which will fall to some future generations of politicians. For them, courage and creativity will be necessary. Care will be needed to ensure that it is not the less vocal who bear a disproportionate share of the pain.

I would like to share one small contribution that I found personally gratifying. It was related to over-promising in that the actuaries concerned were, in my opinion, overestimating investment returns in their reports. I produced a number of actuarial reports for use by individuals making claims for loss of support in South African courts—using much lower real rates of return because I could not see how the individuals concerned would be able to make the returns being used. My reports were never challenged in court, but frequently led to larger settlements. The most successful, and most interesting actually had little to do with financial assumptions. It concerned a widow who had a claim for loss of support because of her husband's wrongful death. He had worked for a farmer and been allowed to keep two cows on the farm. I had been asked to determine the present value of his income, but the question was the value of the cows' milk. At the time as I remember, he would have been lucky to get 50c per liter from other farm workers; the farmer was receiving twice this price from the wholesalers, but his widow was paying six times at the store in the local town. The difference more than doubled her claim. Using some of my financial instincts to help in this way was particularly satisfying! You never know where some ideas will take you if you are looking for an opportunity to contribute.

Benefits that Meet Needs

The focus on sales means that the industry often seems little concerned for the real needs of its clients—as would be required by the *marketing concept*. The next few pages look at the inadequacy of some of its products, and how they provide creative opportunities for product development that would meet people's needs.

One potential contribution is to work at improving the advice given by salespeople and financial planners. In particular, the calculators, proprietary or freely available on the Internet, could be made more effective in addressing people's needs, and could provide the basis for better advice. Many of them misleadingly focus on the easy risks and avoid the more difficult: inflation, investment shortfalls, and longevity particularly.[1] They also often fail to attempt to smooth consumption over the long run. There is a need to communicate the uncertainty and to steer people into appropriate products. Given the declining role of human capital (future earnings), it is agreed that lifetime consumption can be increased if investments are more aggressive when people are younger and the risk reduces with age. The aged need a *harvesting plan*[2] to manage their declining asset balances—and declining ability to manage them.

At the other end of life, coverage for orphans is by far the greatest need. Adults without children are unlikely to require life insurance cover for themselves—as they can earn their own living.

Disability Insurance

Another area for product development is the redesign of disability insurance. The standard offering is a lump sum paid on total and permanent disability only—leaving people uncovered if they suffer from temporary or partial disability. Where there is cover for these, it is often limited to 2 or 5 years. On the claims management side, the industry has been slow to recognize that physical disabilities do not prevent people from working in what is now a knowledge economy. Huge improvements in medical technology also mean that many people, who would have been disabled in the past, can get back to work. There is much work to do to bring the best of rehabilitative medicine to the management of disability claims. This not only applies to life insurance, but also in the accident insurance schemes that provide cover for workers and road accidents. Rehabilitation and training can be painful and humiliating, but it is invariably to be preferred to the isolation and meaninglessness that otherwise may accompany unemployment.

---

[1] Zvi Bodie and John Turner have written on these issues, and I have looked at a number myself in an attempt to find one I can recommend to people!

[2] This is one of the ideas about which I am personally enthusiastic, see Asher (2012).

The industry is also prepared to offer overlapping benefits: the trauma benefits, which pay significant lump sums on the diagnosis of certain critical illnesses, may be needed for rehabilitation expenses, but the medical expenses are better covered by health insurance. Recent medical advances mean that some of these policies are paying large amounts of money on the diagnosis of what have become trivial diseases since the policies were sold. While it may be difficult to persuade life insurers to drop policies that people can be persuaded to buy, there are business opportunities for health insurers to increase the cover they offer in this market.

Longer-term income payments are often not linked to inflation—or have an inflation linkage limited to a fixed percentage. These limitations are a throwback three decades to before inflation-linked bonds were widely available to provide hedges for such benefits. Inflation-linked contracts may be more of a challenge to sell, but potential customers may well appreciate genuine efforts to explain risks in a manner that clearly shows respect and care for their welfare.

Companies offer benefits that leave other gaps in cover. It is common for companies to offer cover for accidental causes only (no need to ask questions about health). If a family needs cover, it needs it regardless of the cause of death or disability. I have been told that any cover is better than none, but integrity requires us to at least disclose any inadequacies. It is surely also good for sales in the long run!

As actuary to a life insurance company in South Africa in the 80s, I found that there was opportunity to be quite flexible in designing products that were more appropriate. At one point, I was put under pressure from our marketing managers to introduce a trauma product.[3] I thought the amounts in insured were much too large for the need, and so designed a product that only paid a quarter of the sum insured for each disease diagnosed—and then also paid a benefit related to the number of days in hospital. This was a reasonable proxy for severity and many medical insurance policies would not have fully covered the hospital costs. I am pretty sure that most policyholders did not realize that the benefits were quite different to those offered by other companies, but also sure that most of

[3]These had just been invented in South Africa by Marius Barnard, brother of Chris Barnard who had performed the first heart transplant.

them would not have been able to describe the competing policy benefits either. I was satisfied that we were giving good value for money and charging people less, although never had the opportunity to investigate the extent of over-servicing. A further bonus for me, though, was that we were able to remove the accident benefits from our product range. The General Manager Administration and I were able to persuade the marketing managers that we could give them their new trauma product much faster if we used the same computer code as for accident benefits. Because one could have only one product per computer code, the accident benefits would have to go, and we distinguished between the two products by date of entry.

Deductibles and Health Insurance

The industry's obsession with easy sales, at the expense of clients, is also seen in the way that policyholders are seldom advised to increase their deductibles. There is no point in insuring for small losses: they are a waste of time and money—expensive to administer from the perspective of both policyholders and insurers. Most middle class people can afford losses of a few thousand, and should only insure for potential losses in the tens or hundreds of thousands.

I feel that this is true even in the case of medical insurance, where there is a concern that people will not go to their doctors (GPs) for preventative treatment if it is not covered by insurance. The Australian mandatory system, for instance, provides cover for visits of less than $50. Even if GP visits were subsidized, the insurance that is needed is not for a few small claims, but for situations where many claims in a short period put a strain on family finances. Modern computer technologies make this much easier to manage than previously. Incorporating this technology provides perhaps the greatest current challenge in financing medical care. Automating medical records will also allow for much better management of all medical care, and provide for huge strides in research to determine the most effective treatments. There may be some resistance by members of the medical professions who see it as a threat to their status and incomes. In this area, it may be that the financial industry has a profitable chance to be on the side of the angels.

Ageing and Dying

Population ageing is a popular topic with the baby boomers entering retirement. The financing of advanced old age becomes a larger problem with increasing longevity and smaller families, which mean fewer children to care for aged parents.

By coming slower than previously, death may be easier to deny. If the aged are to live and die with dignity, addressing their problems requires careful thought, empathy, and some courage. How will we cope ourselves? We cannot address the financing of ageing without considering death. The good life includes a good death, where we acknowledge and accept our declining powers. There are consequences for our vocation. First, there is the need to develop satisfaction or contentment within ourselves. We have to befriend ourselves—because we might outlive all our friends and family. My grandfather, who lived to 102, told me that he did not like to go to the local market anymore, "because all my friends' children are dead!" We also need reconciliation to a world where we cannot control our family or our carers.

Secondly, there is a need to make financial provision for later years when we cannot control our finances, and provision for passing on the wealth that remains. There is a period of a year or more before dementia is diagnosed where people are particularly at risk. I am doing work with Jo Earl and others that suggests that people are more gullible and therefore more susceptible to losses at this time. The need for financial advice and appropriate products is therefore much larger than previously. For those in the early stages of dementia, it may be desirable to lock financial assets away in life annuities.

There are also ways of ensuring that prevent yourself from selling your property for less than it is worth, which I have known to happen before dementia is diagnosed. Philippe Février and his colleagues describe a contract used in Europe and called *viager* in France. The seller gets a monthly payment and the right to occupy the property for life. It is probably better to pool your risks though:

> *Back in 1965, when Mrs Calment was aged 90, she sold her apartment in Arles to a 44-years old man, on contract-conditions that seemed reasonable given the value of the apartment and the life-expectancy*

> *statistics that prevailed at the time. The man turned out to be unlucky since Jeanne Calment*[4] *lived a very long life. He died in 1995, two years before Mrs Calment, after having paid about FFr900,000 (twice the market value) for an apartment he never lived in* (2004, 4).

Research

There is also a challenge to research the effects of the benefits the insurance industry pays when an insurable event has occurred—and of people who have failed to take out insurance. Can too much insurance be disruptive like winning a lottery? How much income does a widow need if she has young children? If she does not? Are widowers different? Are lump sum or income streams easier to manage? What is the best way to support people after they have suffered a disability? What happens to people who are not insured when their houses are flooded? For a multi-billion dollar industry, little is known. Writing this, I have to confess to feeling that as an academic I could have done more to initiate research into this area, but there is time to do more! In fact, there is G8 initiative[5] to make government data more readily available for research, and one can also argue for the need to collate private sector data. The development of knowledge is a necessary although not sufficient requirement for wisdom.

Moral Hazards in Insurance

Moral hazards increase the costs of insurance if policyholders behave more recklessly when they are insured. Anti-selection increases costs if some policyholders know more than the insurers about the claims they are likely to make—and they take out more insurance. Managing moral hazards and anti-selection is a challenge to those involved in the legal wording of contracts, marketing, underwriting, and claims management—as well as actuarial work.

---

[4]Who also made the Guinness book of records as the oldest person alive.

[5]G8 (2013) Open Data Charter. Accessed December 20, 2014. https://www.gov.uk/government/publications/open-data-charter/g8-open-data-charter-and-technical-annex.

Insurers do need to be cognizant of moral hazards and anti-selection. Disability income claims are, for instance, definitely higher when the replacement income is a higher proportion of what the claimant could otherwise earn. Contracts need to be designed to prevent opportunistic behavior by some policyholders at the expense of expected profits or other policyholders. The risks can however be exaggerated, partly because policyholders themselves bear the costs of recklessness. I saw this first while analyzing mortality during the Rhodesia/Zimbabwe war. The company for which I worked had increased the premium rates for term assurance—on the assumption that those most at risk in the war would take out more cover for the cheapest possible premiums. When we analyzed the experience, however, we found that term insurance mortality had in fact declined. Those prudent enough to take out term insurance were also prudent enough to stay out of trouble!

People are not all opportunistic. It would be imprudent to rely on no one taking advantage of you, but overly cynical to think everyone will. The issues can be illustrated by considering the various life insurance arrangements that offer *free cover*—that is free of evidence of health. This works very well when offered to large groups of employees of a company. Even if there are one or two in poor health, and even if those in poor health are instrumental in organizing the insurance, the size of the group may well dilute any excess premium that should be charged. If these arrangements have been successful for some time, however, pressure from salespeople can lead to smaller and smaller groups being accepted. This trend ends in losses once opportunistic salespeople create groups with which to cover people in poor health. Insurance companies can also apply a lower standard of underwriting when people are about to take out mortgages to buy a home. Buying a home normally indicates that they are in good health. Problems occur, however, if the underwriting becomes so limited that opportunists find *death bed* cases, who can take out a mortgage and then get life insurance at normal rates. Managing these hazards calls for some wisdom—and courage when your major competitors are acting recklessly. There is a great deal of merit in developing ways to offer insurance with less underwriting, but none in failing to prevent free riders creating losses.

Taking a virtue ethics approach does not mean being naïve. People can fall prey to temptation so it is prudent to design products and underwriting so that there is a cost to deception and manipulation. People are also less likely to be manipulative if they encouraged by codes of ethics as is covered later in Chapter 14. My experience is that many people respond positively to the idea that insurance contracts include the requirement of *utmost good faith*, which is that both parties to the contract will disclose all relevant information to the other.

It is not surprising that opportunism and fraud flourish where policyholders feel that they have been treated unfairly. Lack of candour in marketing material, particularly failure to highlight unexpected exclusions, can create such feelings. To find out, after the event, that your policy covers rain damage but not floods caused by an overflowing river can well create resentment. Policyholders will feel unfairly treated where the industry gives the impression that it does not want to pay claims. In the companies in which I started work, we emphasized that paying claims was our purpose. I cringe, therefore, when I read headlines, "victory for insurance industry" because some company has won a case against a claim by a policyholder.

Mutuals

Mutual societies, owned by their customers, can be successful competitors to shareholder-owned companies—in the finance sector particularly. They play a role in the market by discouraging price gouging, and may address moral hazards because they remove the conflict between shareholders and customers, making the arrangements seem fairer. In Australia, industry superannuation funds are effectively mutuals and their slogan of "all profits to members" addresses both these issues.

Some of the older mutuals were set up before corporate law was fully developed. Since then, it has been much easier to set up a company than a mutual organization. If share prices fall below book value, however, it may make sense for the policyholders or depositors to buy out the shareholders.

Having spent a decade of my life sponsored by, and then working for, a mutual insurer, I prefer their ethos. My view is that the demutualization of the past 30 years had its origins in greed rather than any inherent structural disadvantages. The senior management of the mutuals wanted the profits from the share options that could not be given to them until demutualization. Consultants and merchant banks, which made huge fees from the transactions, aided and abetted the process.

Mutuals need a different approach to capital if they are to survive. The capital providers need to benefit directly from the capital. If not, then the organizations will be vulnerable to opportunistic takeover. Those organizations that demutualized paid members significant sums for the sale of their capital, which the opportunists said had been tied up in the organizations. Frank Redington, a leading British actuary had, however, indicated the solution in his essay, *The Flock and the Sheep*. There are two alternative perspectives, both of which can be valid. The organization view, legally correct, is that all the assets of the company belong to the legal entity that is the company. The sheep analogy recognizes that the personality of the corporation is a legal construct, and that the capital, like the fat on a sheep, can potentially be taken by the capital providers when they leave the flock. Members can therefore bring capital into an organization when they become customers, and take it when they leave. There is a need to prevent too much mobility—members like sheep may need to be corralled for their own sake! Nevertheless, with some creativity, they can bring the fat in by an extra loading on their premiums or adding shares to their deposits. It was a great pity that the Equitable, the strongest advocate of the mutual model in the United Kingdom, was led to ruin by a dominant CEO who made impossible promises to policyholders.

In an idealistic youth, I was particularly attracted by the Mondragon cooperatives of Spain, and the Yugoslav model of worker ownership. The ideas of employee share-ownership schemes also had some attraction. Having more experience of business risks, I now think that it is unreasonable to give workers a significant interest in the profits of their employer. There is too much downside risk in that they may lose both job and savings in companies that make losses. There is also too much upside benefit in companies that turn out to be hugely profitable—especially if they are capital intensive and provide disproportionate rewards to their employees. Workers in unprofitable companies might well be resentful. I fear that this might even have played a role in the conflict in Yugoslavia. Lars–Erik Cederman and his colleagues have produced some convincing statistical evidence that inequality was a contributor to this conflict. If so, it emphasizes the importance of economic justice in keeping the peace.

The flourishing Mondragon cooperatives have modified some of their more idealistic initial principles. While the website of the Mondragon Corporation affirms that it puts workers before capital, they now raise capital on the market—without giving it control. It has expanded internationally and is recruiting associates—if you are interested!

Other types of mutuals provide social benefits to members in addition to their financial role. This often applies to the friendly societies that exist in a number of countries and to the burial societies that are common in Africa.[6] The development of mutual type organizations therefore provides possible outlets for creativity in a vocation.

Chapter summary: Hard selling is a form of over-servicing that exploits customers. Over-optimistic projected investment returns are misleading and can be hurtful. The challenge is to design benefits for life, disability, and retirement that leave no gaps and create no overlaps in cover. Moral hazards can be managed by careful and scrupulously fair management. The ongoing participation of mutual firms in the market creates diversity that can encourage better value for money and corporate governance.

[6]See Rob Thomson and Debbie Posel.

CHAPTER 9
Banking

We can approach commercial banking as having three main roles: making loans, facilitating payments, and taking deposits. This chapter starts with these functions, looking at the risks and how they might be addressed. It also suggests that the banking industry has spread too widely into other services and become too powerful.

Loans

Bank loans facilitate both new and existing economic activity, creating money as necessary to achieve this.[1] Doing this in a way that maximizes activity without taking too much risk is a challenging intellectual activity. Michael Manove and colleagues provide a challenge for those evaluating loans in banks by suggesting that they are lazy if they rely too much on collateral rather than on careful evaluation of the economic merits of the new projects! I have little experience in this area, but—particularly when linked to SMEs—it seems it can be both productive and exciting as a vocation.

Charging too Much

This chapter is, however, more concerned with the size and costs of loans. Making loans and taking deposits involves charging interest, which we discussed in Chapter 6 as the price of capital, and which has long been regarded with suspicion from an ethical perspective. Two elements of this distaste for interest touch modern banking practice.

---

[1]McLeay et al. (2014) of the Bank of England provide a concise summary of modern banking, and how banks create money.

First, charging high rates of interest is reprehensible if it means rich people are profiting from the distress of poorer people who have to borrow to survive. As a problem, it has probably been with us since interest was invented. We can talk about informal sector loan sharks, but there are also interest rates charged on credit cards—particularly when aggravated by penalty charges and outrageously expensive insurance. There are other forms of sub-prime loans, which are more likely to create financial stress for the borrower. It is unjust to exploit misfortune and ignorance. Lots of good work is done in this sector by those working for credit unions, micro-lenders, and various charities (non-government organizations), who help poor people avoid crippling interest. Some of their best work is in providing help with budgeting and other financial advice and assistance. It would be good to see more people in the formal banking sector being more concerned with ensuring that people's ignorance is not exploited, and that they are guided into more sensible behavior and lower credit charges.

One element of this is help to renegotiate heavy financial loads. One of the marks of a civilized society is that it has fair and efficient ways of relieving people of unbearable debt burdens. If you have read Charles Dickens's *Little Dorrit*, you will know of the debtors' prisons of 19th century England. We now have systems of bankruptcy that mean that a competent court can require a lender to forgive debts that cannot be repaid. It is important to ensure that these systems are preserved and if possible enhanced—being aware that interventions can have perverse side effects. If contracts are not fair to both borrower and lender, lenders will withdraw from the markets and poorer people may be even worse off.

Lending too Much

A second reason for being wary of interest is that debt is a poor way to finance risky ventures. Interest does have the advantage of convenience, because it can be clearly defined and the level set without difficulty if there is limited credit risk involved. Making an equity investment means that there are additional costs involved in evaluating the size and volatility of the profits. These additional costs are not much greater, however, than evaluating loans where the borrowers are over-extended—as credit failures continue to illustrate!

On the borrowers' side, debt exposes them to interest rate and other risks. This both restricts what they can spend and imposes economic, social, and psychological costs when they are bankrupted—even in civilized societies. Bank loans should only really finance a relatively small part of risky ventures—not just businesses, but also long-term housing loans.

Many people argue that overall debt in the economy is too high and creates credit crises—that lead to the loss of many businesses and undermine confidence. This view is often associated with Hyman Minsky, who says:

> *Whenever full employment is achieved and sustained, businessmen and bankers, heartened by success, tend to accept larger doses of debt-financing. During periods of tranquil expansion, profit seeking financial institutions invent and reinvent 'new' forms of money, substitutes for money in portfolios, and financing techniques for various types of activity: financial innovation is a characteristic of our economy in good times* (2008, 199).

The implication is that people, and governments, are living beyond their means. This is true if the debt has been used to finance consumption rather than investment (what Minsky calls Ponzi finance). Lenders can be criticized for encouraging this, and will suffer the credit losses that follow. There is, however, also the possibility that the funding instrument is inappropriate. Businesses could often have less debt, and use more equity funding, and housing could be financed by more sustainable instruments, as suggested in the next section.

Using additional equity is not controversial from a theoretical perspective. The Modigliani–Miller capital irrelevance proposition holds that, under certain conditions, capital structure will not influence the value of the firm. There has, however, been debate about what is sometimes called lazy capital, with many authors suggesting that managements will waste cash flow if they are not highly geared (borrowed to the hilt so that almost all the cash flow is required for interest payments). It seems to me that the arguments for higher gearing justify corporate restructures and share buybacks that serve the interests of the financial sector at the expense of other shareholders.[2] There are effective, more direct, ways of supervising managers other than putting them under the pressures of excessive gearing. Of course, tax can further distort gearing decisions, although does not have to do so. In Australia, our dividend imputation system has minimal distortions and we have less gearing in the corporate sector as a result.

It is also argued that bank deposits offer security and liquidity that are socially beneficial, and valued by savers who are increasingly older and retired. Bankers call their business model *maturity transformation*, and in my experience have a great deal of difficulty in even hearing the question as to whether too much liquidity could be economically undesirable. At what point do costs exceed the benefits? Is it desirable to have as much liquidity as our banking system currently offers? When one adds the sources of immediate liquidity (demand deposits, credit card limits, lines of credit and cash), one gets more than a year's GDP. Many people, ahead on their mortgages, can conceivably borrow years of salary without speaking to their bank managers! The current levels of liquidity are excessive as they cannot be sustained without a government guarantee. They are surely leading to a misallocation of savings to short—rather than long-term investments.

The high liquidity and short-term interest rate fluctuations offered by bank deposits may actually be more of a problem than a boon for elderly people.

- To the extent they want to live off the interest income, it gives them what has been one of the most volatile sources available—and currently the lowest returns in history.
- Being increasingly at risk of dementia, they have no protection against making imprudent decisions if they lose their sense of the value of money. I have heard of a number of

[2]I have been unable to find much in the way of direct criticism of this view in the large literature stemming from Jensen and Meckling (1976). A possible exception is Walter Novaes (2003) pointing out that managerial power may also explain capital structure. The huge costs of the 2008 banking crisis, however, nullify previous research showing small gains from gearing. Andrew Haldane and Vasileios Madouros (2012) show that the simple gearing ratios used by Basel 1 were good predictors of bank failure. Rather than addressing the agency problem, the encouragement of gearing seems to have caused an increase in the managerial expropriation of wealth, and huge credit losses.

cases where individuals spent money unwisely, or gave away large sums they could ill afford.
- Even if they are in possession of all their senses, they are vulnerable to their less responsible children, or smooth talking investment advisors who might recommend high-risk investments.

If this is true, then much of the debt can be converted into longer term contracts that would be less risky both for borrowers and investors.

Sharing Revenue

There are varieties of ways of sharing risks other than through company equity. Shopping center rentals are often based on the retail lessees' turnover. A related and ancient practice is crop sharing. The landowner gives over his land to a tenant in return for a portion (often half) of the crop. They both therefore share the risk of poor weather or declines in the price. It can work for long periods: visiting St Catherine's Monastery at Mount Sinai, we were told the contracts between the Monastery and the tenants had been formally written down when Napoleon conquered Egypt over 200 years ago, and had been in force long before that. The contracts seemed unfair, however, with only 30 percent of the produce going to the tenants.

The idea might be applied further in agriculture and mining. Commodity futures shift some risk from producers to investors and consumers. They are, however, incomplete insurance contracts. Farmers remain vulnerable to weather and other crop conditions. Crop sharing for cash crops entirely sold in public markets are not difficult to monitor. While not an investment, South Africa's Eskom provides electricity to Alusaf's smelter at a price related to the price of aluminum, which allows it to participate in profits at a lower risk to Alusaf.

There are probably many other such contractual arrangements. Lawyer, Tim MacDonald, for instance, has been designing contracts that allow investors to get more access to revenue, before deductions for operating expenses and taxes, for 30 years.[3]

---

[3]Accessed November 24, 2014. http://evergreeninvestors.com/author/tim-macdonald/.

Salary-Linked Housing Finance

Salary-linked housing finance is the best product idea that I have had, although I have not yet been able to persuade anyone to introduce it. At this stage, it is outlined in some papers and a couple of boxes of product specification. I remain convinced, however, that it could provide both an ideal investment for retirees, and provide financing housing with the lowest risk.

The basic instrument is simple: Homeowners contract to pay a predetermined proportion of their income for a predetermined period. This provides significant advantages:

- No interest rate or inflation risk
- A hedge against their salary increases being less than average
- A reduction in the initial repayments compared with conventional mortgages—as they will pay more later

They would be particularly attractive to pensioners, who could invest through some pooled vehicle and share in salary growth. They also obtain significant advantages:

- An investment return linked to the salary inflation of the pool of homeowners so giving them standard-of-living increases related to general prosperity.
- An investment that pays regular monthly cash flows to match their spending needs.

As a financial instrument, it would be in a different class and offer real diversification benefits. The real returns would be independent of interest rates, share prices, and property rents. For homeowners, it insures the same risks as the *livelihood insurance* suggested by Robert Schiller in *The New Financial Order*, but without any basis risk.

There are obviously obstacles to the introduction of the product, especially operational risks and moral hazards, but these are no different from collecting income tax. For those interested in a more detailed consideration, there are more details in my 2011 paper. I would be happy to collaborate with anyone who would like to try to introduce them into some market!

Payments and Money Laundering

My knowledge about the issues in payment systems comes from following my friend David Porteous's work at Bankable Frontier Associates. Their report[4] outlines the advantages of new payment mechanisms (such as debit cards and mobile phones) in facilitating economic activity in poorer countries especially. These mechanisms make possible some transactions that distance previously made impossible, and are often safer and more convenient. By bringing more transactions into the formal sector, they also make it easier to collect taxes and catch criminals using money-laundering rules.

While particularly important in poorer countries, there may still be innovative work that can be done in developed countries to develop systems that are more efficient and ensuring that pricing reflects the total costs, and does not distort incentives. I, for one, find loyalty programs and card points an intrusion. One cannot ignore them as you are asked questions about them at every checkout. Can someone please find a better way?

Money-Laundering

Payments have an integrity side other than ensuring that the right parties are paid. Organized crime needs banks, and apparently respectable banks have often proved more than willing accomplices. This issue appears to have been addressed more actively since the World Trade Centre attack when the physical risks became clear. However, there remains a great deal of work in this area to assist law enforcement agencies to identify more serious issues of crime, and for tax authorities to collect their fair share from international tax evasion. The work of the international Financial Action Task Force is worth supporting. There is much that many financial institutions could do to ensure that they support the letter and the spirit of this important activity.

---

[4]B. F. A. "The Journey Toward 'Cash Lite' Addressing Poverty, Saving Money and Increasing Transparency by Accelerating the Shift to Electronic Payment." Accessed August 30, 2014. http://www.uncdf.org/sites/default/files/Download/BetterThanCashAlliance-JourneyTowardCashLite.pdf.

Tax avoidance and evasion sits along a spectrum from the legitimate to the criminal. It is an easy slippery slope for integrity—and there are different places to draw the line. "Everybody does it" is a poor justification. The most comfortable place is where you would suffer no embarrassment if the tax authorities and your best friends knew your details. A tax problem means that you have enough: pay it!

Ancillary Banking Operations

Banks offer a wide range of financial services other than direct banking. These include custodial business, foreign exchange (FX) dealing, extensive dealing in derivatives, stockbroking, investment management, insurance, and merger and acquisition advice. The investment and insurance related services do not flow naturally from their core business, but arise partly because the banks have an unfair commercial advantage. Customers are invariably also borrowers, and who can afford to argue with their bank manager? I think the approach of the Depression era Glass–Steagall Act in the United States was correct, and should be applied everywhere. There are economies of scope in permitting a wide variety of financial services from one organization, but the distortion of competition and concentration of power is undesirable, and the systemic risks considerable.

There are also many opportunities to take secret profits and make excessive charges, as the customer may not focus their minds on the ancillary business. The misselling fines that have been imposed around the world are often the result of these ancillary offerings.

Ensuring that the banking conglomerates are broken up is essentially a task for legislators, but for as long as they are permitted, and if you are involved in buying these ancillary services for your organization, you need to exercise precautions to ensure that there are no conflicts of interest and you are getting the best deal. If you are working in banking groups, the challenge is to make your charges transparent and educate your clients in what is best for them. They are sure to appreciate it! If you can set up new businesses outside the big groups, so much the better.

Risk Management

Risk management has a high profile in the banking industry. The experts agree that it is crucially dependent on an organization's risk culture. The discussion then normally moves on to how to ensure that everyone in the organization takes responsibility at some level for the management of risk. Poor risk management can, however, be seen an offence against justice as stakeholders are not being given their due. Stakeholders include all those who are at risk of being harmed by the organization—including the environment and future generations. Culture can thus be seen as the organizational equivalent of character, and risk culture can be seen as the manifestation of virtue within the organization. A lack of prudence in risk management is linked to the injustices of the market manipulation, money laundering, and sanctions busting in which many of the large banks have been engaged. Risk culture fails when inappropriate informal behavioral norms and expectations override the virtues as suggested in Table 3.1, which maps the elements of poor risk culture in financial institutions mentioned by Michael Power and colleagues (2013) against the corresponding virtues.

Table 3.1 The Risk Management Virtues

Elements of culture from Power et al. (2013)	Corresponding virtues
"Necessary to restore trust"(12)	Integrity—being trustworthy
"Meet customer needs" (12)	Justice—giving all their due
"Deviant subcultures" (13)	Self-control
"Over-confident corporate risk-taking"	Justice—failure to avoid harm
" 'Brash' and aggressive 'tones from the top'." (13)	Wisdom or prudence
"Breaches were routinely disregarded" (13)	Integrity
"Introspection, lack of insight or sufficient self-criticism, rejection of external criticism" (14)	Wisdom
"Above all fear" (14)	Courage
"Complacency . . . There are recurring themes of missed warning signals, failure to share information." (14)	Integrity

Culture Not Compliance

If risk management should be an exercise in the cultivation of the virtues, it is unlikely that additional regulation alone will be successful. We do not learn virtue by following rules. Confucius has it: "If people be led by laws, and uniformity is sought to be given them by punishments, they will try to avoid punishments but have no sense of shame." Detailed rules must undermine personal responsibility by encouraging the tick-the-box approach.

People may think that they prefer easily followed prescriptions. The apparent certainty, however, offers a false sense of comfort and reinforces immature thinking. It also fosters uniformity and has the potential to create greater risks. Rules without understanding are not second best; they are dangerous. John Braithwaite illustrates from the Three Mile Island nuclear power incident, changes from which subsequently have led to a 90 percent reduction in automatic shutdowns:

> *When something went wrong that was not covered by a rule, operators lacked the systematic wisdom—the risk analysis intelligence—to think systematically about what needed to be done. So the nuclear regulation paradigm changed to be less about government inspectors checking compliance with rules. An important part of the new paradigm became regulatory scrutiny of risk management systems and re-integrative shaming within the nuclear professional community of companies that failed to improve those systems* (2005, 86).

From a slightly different angle, Jodi Goodman and colleagues have looked at the success of giving detailed feedback in training. They find that the "specificity of feedback is beneficial for initial performance but discourages exploration and undermines the learning needed for later, more independent performance" (2004, 248).

Dominant Personalities

If an excess of rules is one way of undermining a culture virtue, an aggressive senior management that fails to consult, let alone empower their staff, is perhaps even more effective. There are many examples. In Australia the failure of HIH, the largest insurer in the country was the subject of a Royal Commission. The commissioner, Justice Owen (2003) expressed it this way:

> *The problematic aspects of the corporate culture of HIH—which led directly to the poor decision making—can be summarised succinctly. There was blind faith in a leadership that was ill-equipped for the task. There was insufficient ability and independence of mind in and associated with the organization to see what had to be done and what had to be stopped or avoided. Risks were not properly identified and managed. Unpleasant information was hidden, filtered or sanitised. And there was a lack of sceptical questioning and analysis when and where it mattered.*[5]

Dominant personalities are a poison that has to be confronted, and courage is required to do so. It would be easier for boards to consider character, and be suspicious of signs of arrogance, when appointing members and executives. Remuneration packages could also be based less on grandiose views of the role of the leader. Limited terms can keep politicians in line and could help in business too. If you are faced by a dominant and bullying individual in your organization, you could look at the discussion of bullying in Chapter 13.

Systemic Risks

If we are concerned with flourishing communities, we will be concerned for the weaknesses and fragility of the financial systems within those communities. As banks must trade and accept payments from each other, they inevitably have exposure to each other. There is a need to ensure that payments are netted or settled as soon as possible so that all parties can easily calculate their exposure to an institution that is weak.

This appears to have been done effectively for payments in most countries, but not for exposures arising from derivatives and FX, which

---

[5]Accessed August 30, 2014. http://www.hihroyalcom.gov.au/finalreport/Front%20Matter,%20critical%20assessment%20and%20summary.HTML#_Toc37086537.

therefore present a systemic risk. The FX market particularly continues to grow and this year has apparently reached the quadrillion level. As such, it may be too big to manage, and the latest Basel findings are not surprising:

> . . . *substantial FX settlement-related risks remain due to rapid growth in FX trading activities. In addition, many banks underestimate their principal risk and other associated risks by not taking into full account the duration of exposure between trade execution and final settlement. While such risks may have a relatively low impact during normal market conditions, they may create disproportionately larger concerns during times of market stress* (2013, 3).

Andrew Haldane and Robert May have suggested a hub and spoke approach to simplify derivative markets—rather than the current "cat's-cradle" of financial network interactions. This would require trades to be settled by international clearing houses, and there are already entrants to this market.[6] It will require regulation to require standardization of contracts and to ensure that all banks participate. There is much creative work necessary to design effective institutions to provide for all derivatives and not just FX contracts.

Unmanageable chains and layers create similar systemic risks. Lloyds of London almost failed in the 90s because of a reinsurance *spiral*. Members were not aware of which risks they were insuring because the different layers of insurance were not visible to them. The 2008 financial crisis was also exacerbated by institutions unaware of the concentration of risks though multi-layered asset backed securities and credit default obligations. I have also been told of stock lending spirals where the original owners do not know who currently has possession. It is difficult to believe that such spirals are efficient, let alone necessary. The lack of transparency also suggests overcharging.

Dynamic hedging of put options and a variety of other trading systems that sell when prices drop present another systemic risk. Programmed arrangements have been blamed for the 1987 market crash, and a variety of

[6]See, for instance: http://www.cls-group.com/Pages/default.aspx. Accessed December 22, 2014.

capital requirements and trading rules have thus far prevented a system-wide recurrence. There are, however, losses every time the market drops. Life insurance companies issue guaranteed annuity contracts that they protect using dynamic hedging. Actuarial company Milliman reports that the hedging programs saved the life insurance industry $40 billion in September and October 2008, but they also lost $4 billion in those 2 months.[7] There is no comment on who suffered the $40 billion losses, but it would presumably have been some hedge funds and the banks that offered the derivative contracts. This is another Miller–Modigliani application. Spreading investment risks around the market does not necessarily add value, just frictional costs. Companies that offer investment guarantees should have capital to absorb the associated risks; otherwise the capital may not be available when it is needed.

Resolution Plans

International regulators[8] have called for the introduction of resolution plans, also known as living wills, to address systemic risk particularly. These recognize that no risk management system can prevent catastrophic losses overwhelming the institution's capital. Plans need to be in place to respond quickly so that the failure of one institution does not damage others. This is especially important for banks so that they can be recapitalized quickly and resume lending. The insurance industry, not being government supported, usually has exclusions for catastrophes including *Acts of God* and *Force Majeur* to protect themselves and so that they can continue to function.

For banks, there need to be triggers for freezing deposits and turning them into longer-term instruments to avoid bank runs, and for writing off equity when it appears that there have been credit losses. There would be an earlier point at which subordinated debt would be converted to equity (tier 2 into tier 1 in Basel terms), and further points when other

---

[7] Accessed 12/22/2014. http://www.actuaries.asn.au/Library/Standards/LifeInsuranceWealth/2012/LIWMPCVariableAnnuitiesOctober12.pdf (page 6).

[8] For details see http://www.financialstabilityboard.org/wp-content/uploads/r_121102.pdf. Accessed December 12, 2014.

creditors and depositors would have part of their value converted into equity. The points should be set at levels (obviously subjective) where there would be no point in withdrawing deposits. The share price at which conversion takes place can be predetermined at a level that effectively wipes out shareholders. New shareholders can then vote for a rapid change of board and management if they feel it appropriate. Similar approaches can be applied to insurers. It will be objected that it is not possible to value assets sufficiently quickly—and this could lead to considerable inequity if the assets were subsequently found to be much better than originally judged. There would be no objection to providing appropriately priced options to previous shareholders to recover their losses. The point is that, absent government support, failure is quite likely at the levels of gearing banks typically use—and society ought not to have to suffer the pain of waiting for banks to recover and resume normal lending, nor of compensating investors for business risks. Sebastian Schich and Byoung-Hwan Kim show that market participants still widely believe that governments offer implicit guarantees to bondholders, but report changes to these beliefs as resolution plans are implemented.

It can be seen as a matter of integrity. Institutions need to address their weaknesses and mortality. Even if regulators do not require such plans for all institutions, they can move in this direction themselves. It is again a question of communicating uncertainty and the same arguments apply as in Chapter 7. Companies that work on helping their clients understand should obtain a marketing advantage in greater customer trust, and protection against bank runs in times when panics occur.

Chapter summary: The main social function of banks is facilitating payments, which include the taking of deposits and the provision of liquidity. It is, however, risky to use bank deposits to make long-term investments, and high gearing is economically and socially destructive. Banks have become too influential in modern economies; it would be better if they were not involved in housing finance or investment management, and reduced their share of the unmanageable complexity of some derivative markets. All of these have created forms of over-servicing and failures in risk management that are linked to ethical failures of the leadership, some stemming from arrogance. Dealing with systemic risks requires banks to have resolution plans.

CHAPTER 10
Regulation

This chapter looks at the complexity of what can be called modern regulatory capitalism, and suggests that the focus on rules is counterproductive. It suggests that the idea of responsive regulation is likely to be more effective regulation in that it takes greater notice of the ethical nature of the issues it attempts to address, and will be more likely to garner positive responses.

Regulation touches the financial industry at many points. Australia, for instance, has separate agencies for prudential regulation, market conduct, competition, money laundering, human and consumer rights plus a range of public and private sector tribunals and other dispute resolution bodies. These agencies are in turn subject to international regulatory bodies such as the Bank of International Settlements (the Basel Rules), the International Accounting Standards Board, and a host of institutions that come under the United Nations and the G20 governments. David Levi-Faur and Jacint Jordana coined the term *regulatory capitalism* to describe the current international order.

> *Democratic governance is no longer about the delegation of authority to elected representative but a form of second-level indirect representative democracy—citizens elect representatives who control and supervise 'experts' who formulate and administer policies in an autonomous fashion from their regulatory bastions . . .*
>
> *Thus, it is argued that a new division of labor between state and society (e.g., privatization) is accompanied by an increase in delegation, proliferation of new technologies of regulation, formalization of inter-institutional and intra-institutional relations, and the proliferation of mechanisms of self-regulation in the shadow of the state. Regulation, though not necessarily in the old-fashioned mode of command and*

> *control and not directly exercised by the state, seems to be the wave of the future, and the current wave of regulatory reforms constitutes a new chapter in the history of regulation* (2005, 13).

John Braithwaite (2008) has developed the ideas in more detail, including ideas as to what to do to improve regulatory capitalism. His view is that much of the regulation represents a pleasing dispersion of mutually accountable power, including the view that multi-national corporations can effectively help regulate states—as they did in a small way in Apartheid South Africa. He suggests that the large companies, like large governments, have provided the investment and concentration of resources that has led much of the technological development of the last century, although he recognizes the downside:

> *But other forms of regulation also prove impossible for small business to satisfy. In many industry sectors, regulation drives small firms that cannot meet regulatory demands into bankruptcy, enabling large corporates to take over their customers . . . For this reason, large corporations often use their political clout to lobby for regulations they know they will easily satisfy but that small competitors will not be able to manage. They also lobby for ratcheting up regulation that benefits them directly (e.g. longer patent monopolies) but that are mainly a cost for small business* (2005a, 25).

He does not mention the role of the large professional consulting firms, but they have a considerable interest in complex regulation. One solution Braithwaite supports is for large companies to be required to monitor and publicly report on their interaction with all stakeholders to identify where they—perhaps inadvertently—cause harm. The widely supported International Integrated Reporting Council (IIRC) has taken up the challenge of reporting the value that they create and consume in not only financial, but also social and environmental terms.[1] Integrity aspires to more clarity and transparency.

---

[1]Details of its programmes and its Integrated Reporting Framework can be found on its website: http://www.theiirc.org, Accessed April 14,2015.

Another Braithwaite suggestion is meta-regulation, which he defines as follows:

> ***Meta-regulation*** *means the regulation by one actor of a process whereby another engages in regulation. An example is the government regulating a process of corporate self-regulation—i.e. regulated self-regulation* (2005b, iv).

He illustrates by the following suggestions as to personal responses:

> *Those of us in jobs can start in the organizations where we work; children and those with children can start in their schools. One of the pragmatic appeals of the strategy is that the first mover to improve any particular kind of access to justice can be a private organization that uses the improvement as a competitive tool or as moral leadership, a state organization that requires it as a matter of regulation, or an NGO that demands it as a matter of politics from below. Meta regulatory strategy is about ratcheting-up incrementally. The meta regulatory institutional design is to push NGO, state and corporate ratchets in series—so when one justice ratchet moves up a click there are knock-on effects on the other ratchets* (2005b, 43).

Concern over the negative effects on small business needs also to be matched with concern over the *Washington Consensus* that has used international organizations to impose the interests of western nations and transnational corporations on poorer countries. These countries also need meta-regulatory support.

Complexity

The ongoing flood of new regulation is an increasing challenge. UK academic John Kay describes it[2]:

> *. . . regulation that is at once extensive and intrusive, yet ineffective and largely captured by financial sector interests. Such capture is*

[2]Accessed August 30, 2014. http://www.johnkay.com/2012/07/22/finance-needs-stewards-not-toll-collectors.

> *sometimes crudely corrupt, as in the US where politics is in thrall to Wall Street money. The European position is better described as intellectual capture. Regulators come to see the industry through the eyes of market participants rather than the end users they exist to serve, because market participants are the only source of the detailed information and expertise this type of regulation requires. This complexity has created a financial regulation industry—an army of compliance officers, regulators, consultants and advisers—with a vested interest in the regulation industry's expansion.*

Regulatory overload is not easy to oppose. Each new regulation has some advantage that, in isolation, can be justified, particularly if it appears more sophisticated. By opposing it, you may seem reckless or not up to the new sophistication. Andrew Haldane, an Executive Director of the Bank of England, and Vasileios Madouros, have therefore done us a great service in showing that the complex regulatory models introduced in the last two decades do not work well. In particular, Basel I rules would have worked better than Basel II in the 2008 financial crash. Complex regulations are often difficult to understand, but it is almost impossible to keep all the details in mind. They can also crowd out deep understanding and undervalue the virtues of wisdom, justice, and courage.

The operational risk capital required by Basel's Advanced Measurement Approaches provides an egregious example. It requires a huge effort in collecting and analyzing data, but the impact has been to increase capital by some 10 percent, which is barely material. Operational risks are dependent on what are called "business environment and internal control factors." The Basel committee has recently noted, however, that few banks "are currently able to substantiate how they quantify the impact of those factors on the capital calculation" (2006, 11). In other words, in spite of their huge analytical effort, they cannot tell what to do to reduce the risks. Much of the data collected (often of irrelevant incidents in different institutions) has minimal bearing on the important operational risks that they face. Accounting and risk expert, Michael Power suspects that the idea of operational risk may be viewed as a "fantasy perhaps, of hyper-rational management" (595). In its current format, regulators would show good judgment by removing it from regulation, banks by limiting their participation to the bare minimum.

Overly complex regulation should be opposed on the grounds that it is an infringement of liberty, unfair to smaller businesses, wasteful, and an obstacle to innovation. One possible approach is to work to place the onus on regulators to justify the benefits of both new and existing regulations against their costs to both small and large businesses.

Responsive Regulation

Regulators are responsive if they focus mainly on bringing out the best in people and organizations, and only use prescription where it is necessary to change behavior. *Responsive regulation* is self-regulation in the first place; organizations are responsible for their own risk management, ensuring that they do not harm themselves or others. Figure 3.1, borrowed from the Australian Taxation Office, sets out the ideal:

> *The left hand side of the pyramid represents the stances that can be adopted by taxpayers . . . (Braithwaite, 1995) . . . The right hand side presents the pyramid of regulatory strategy which is described in . . . (Ayres and Braithwaite, 1992).*

Responsive regulation is consistent with virtue ethics in that it is more concerned with aspirations to do good rather than obeying rules that prevent evil. It must surely be more efficient in that the regulators waste less time on entities that are showing that they want to conform. It is also more effective if we accept that it garners support from those aspiring to virtue, and does address negative behavior.

One of the debates in regulation is the extent to which unsocial behavior should be punished. This is partly a matter of desert; it would be unfair for bankers who steal to get lesser sentences than burglars. There are also considerations of liberty and efficiency: whether it is necessary to take the dishonest banker off the street when society can be made safe if they are kept away from financial institutions. Both desert and efficiency come into play with the difficulty in obtaining criminal convictions. The standard of proof in criminal cases is that the matter must be beyond reasonable doubt, and wealthy individuals can employ good lawyers to sow such doubt. In civil cases the standard of proof is the

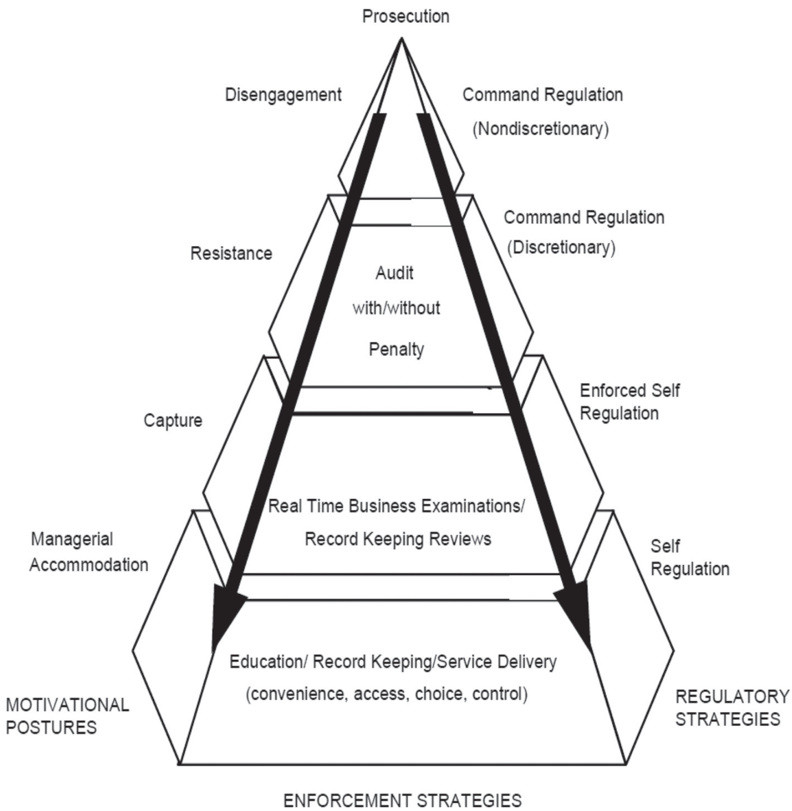

Figure 3.1 Responsive Regulation[3]

balance of probabilities. The South African experience is described by the Johannesburg Stock Exchange:

> *South Africa was the first country to initiate civil prosecution of insider trading with the added advantage of compensation for those prejudiced by insider trading. . . .*
>
> *The civil provisions of the Act have been the main tool utilised by the FSB, resulting in settlements since 1999 totalling more than R93 million. In all cases, the persons involved were named in press releases.*[4]

---

[3]Taken from Australian Taxation Office (1998), p. 23.

[4]Johannesburg Stock Exchange, *Insider Trading and Other Market Abuses (including the effective management of price sensitive information)*, Accessed August 30, 2014. https://www.jse.co.za/content/JSERulesPoliciesandRegulationItems/Insider%20 Trading%20Booklet.pdf.

They go on to report on a survey of market participants, where over three-quarters felt that the new approach had reduced insider trading. Dennis Davis reports that South African company law has followed this approach more widely in decriminalizing many offences that can be dealt with more efficiently without criminal law.

Restorative Justice and Reintegrative Shaming

Regulations ought also to be restorative in striving to get perpetrators to admit their errors, and to reintegrate them into society. It needs therefore to avoid *stigmatising shaming*, where the offender is labelled as a bad person and driven out of the community—at worst to set up a dysfunctional counter-culture. Braithwaite's alternative is *reintegrative shaming*, where the behaviour is identified as unacceptable. Reintegrative shaming makes it clear that organizations need to deal creatively with failure, mistakes, and weakness. They need to be quick to admit to being prone to making mistakes, quick to admit them when they are wrong, and quick to forgive them.

Many huge losses can be blamed on failure to ensure that there are sufficient checks and balances—because people do not admit they are prone to failure. This is more obvious in health and safety matters: protective clothing and safety mechanisms being unused. In finance, it is perhaps more often associated with over-confidence and the way that back offices are disempowered and auditors belittled. We need to recognize that we do not demean ourselves by taking precautions and admitting to mistakes.

In many organizations, those who admit to mistakes are routinely punished for them, in some way. I am afraid that my favorite story on this may be an urban myth, but is worth telling. It was true that part of the Koeberg nuclear power station near Cape Town was shut down by a "bolt in the generator" left after routine maintenance. I cannot find it reported, but it was suggested to me that a previous technician who had reported a bolt missing had been fired. The next bolt was obviously not reported missing.

Braithwaite has a number of ideas how poisonous environments can be addressed. His *Restorative Justice for Banks* includes an intriguing idea about how culture might have been changed at Arthur Anderson before it contributed to the collapse of Enron, Worldcom and HIH.

The issue arose in Australia in the 1990s where the firm apparently got a client into trouble and then told the tax office:

> *This is a rogue partner and we are going to get rid of him. We would hate you in the Tax Office to think that other partners condone what he did* (2009, 445).

Braithwaite suggested that it would have been more productive for the regulator to have refused to accept this explanation, but rather to have initiated an inquiry as to whether the problem was the culture of the firm. It would surely have been critical to speak to the rogue partner. Braithwaite suggests that this partner could have played a role in what he calls a *restorative justice circle*, which could have led to identifying the rogue nature of the Arthur Anderson culture, worldwide. If the regulators had then responsively pursued a *restorative justice* approach, they might have prevented the scandals that occurred subsequently.

The fact that his best financial example is hypothetical illustrates the difficulties in implementation, but Braithwaite's research has shown that such approaches have worked in other fields. While the process might normally be initiated by a regulator, there are opportunities for people within regulated firms to grasp the opportunity to move the culture to greater maturity.

As a Focus for Vocation

Regulators themselves need monitoring: indeed some of the problems with the industry have to be laid at their feet. There needs to be some mutual accountability, and this becomes the responsibility of academics, professional—and industry bodies and non-government organizations with a consumer or environmental mission. Regulated companies themselves can comment on inappropriate regulation. Self-interest of course muddies this mutual accountability in many ways, but it means that, whatever job you find yourself in, you will be either regulating or regulated—and the roles may switch from minute to minute.

There are therefore a number of places where individuals can make a difference in the form and application of regulations. Whether you work for one of the larger organizations or consultancies, for the national or international regulators, or in civil society NGOs or professions, there is a call to apply all your understanding to contribute to simple, effective, and human regulation and meta-regulation.

Chapter summary: We live in a system of regulatory capitalism where international companies and regulators play a role equal to government. This means power is dispersed, which is healthy, but it is increasingly dominated by large players who have contributed to the creation of excessive complexity. *Responsive regulation* is not based on complex rules but aims to bring out the best in people, and to ensure compliance—by *reintegrative shaming* if they fail.

CHAPTER 11

The Poor

Before leaving the finance sector, we can take one more look at a few areas where it could make a contribution to give justice to the poor. On the one hand, this means holding back from exploiting the weak and to "Speak up for those who have no voice, for the justice of all who are dispossessed."[1] On the other, it can mean looking for opportunities to creatively meet the needs of those finding life difficult.

Opposing Oppression

In the first place, we should ensure that we are not contributing to the poverty of others. This happens to the extent that we are extracting rents from them. This can come from gouging of various sorts, but also from the lobbying that creates benefits for the loudest at the expense of the voiceless.

In Chapter 6, we saw Adam Smith's indignation against business lobbying, and in Chapter 10 we discussed the unjustifiable benefits to large companies of much of regulatory capitalism and excess complexity. The ability of the large banks to access government support in many countries during the recent financial crisis has illustrated this well.

One of the major interests of big business is reducing tax. Tax law is clearly an arena with many opportunities for wasteful arbitrage. As a vocation, there is a role in the private sector for tax counsel that ensures that companies are honest, as well as legally minimizing their tax obligations. There is also an ongoing need for energetic and competent people within revenue departments. Once you have learnt the trade, perhaps, you could consider a time with the gamekeepers? There is surely plenty

[1]Proverbs 31:8 (Holman Christian Standard Bible).

of scope for creativity in simplifying the code, in ensuring that it is fairly and efficiently administered—both catching the cheats and falling more heavily on economic rents rather than productive activity. If you have any connections to Greece, that poor country would appear to have special needs at this time!

It is possible that a more principled approach to tax law might work better than the very technical approach now popular. One of my first jobs was to calculate the tax payable for a life insurer. I discovered that we could save some 80 times my annual salary by a slight modification of our liability calculations. I was quite astounded that the chief actuary of the time approved the changes reluctantly, and only after ascertaining that our competitors were already taking advantage of the loophole. His argument was that the tax authorities needed to collect a certain amount of tax from the industry, and would just change the rules if companies took advantage of every loophole. In retrospect, such an attitude might be more efficient if were widespread, and prevented time wasting on tax arbitrage.

My particular bugbear is the tax concessions that have been extracted for the investment income of pension funds. A legitimate argument can be made for allowing people to defer a limited proportion of taxable income from their working lives to retirement. This will tend to even out the average rate of tax paid by people with the same lifetime income—but with a different incidence of earnings. (Think of someone who earned all her lifetime income in one year and paid the top marginal rate on almost everything.) Not paying tax on investment income, however, provides a further advantage to the wealthy, and creates tax arbitrage opportunities. This is because people can borrow and deduct the interest from their taxable income outside the pension fund, and pay little or no tax on moneys invested inside the fund. Tax arbitrage diverts some of our best talent to non-productive effort. I made this point in submissions to the South African Katz Committee in the mid-90s, and one of the members told me that it helped them make a decision to impose an income tax on the interest earnings of retirement funds. The victory was short lived, however, and the tax was removed after a decade. The industry, supported by tax lawyers, persuaded the National Treasury that it was too complicated and the revenue insignificant.

It is perhaps too much to ask people not to lobby for sectional advantage. Superficially, it appears a relatively minor and largely victimless crime. The impact on society and the economy is, however, both burdensome and corrosive. Deniz Igan and Prachi Mishra show how lobbying reduced financial discipline in the years that led up to the 2008 US crisis. Responsibility for resisting special pleading falls in the first instance to civil servants responsible for policy. They need the support of their political masters, who in turn need general public opprobrium for self-interested lobbying. Politicians will tell you that they can easily pick up such self-interested lobbying, but that they need (and deserve) as much help as they can get in finding creative ways to do the right thing. Working with think tanks may fit in with your vocation. Some produce research to further sectional interests only and should probably be avoided, but others do good work for the *common good.*

Discrimination

Our prejudices and unexamined assumptions can lead to unfair discrimination against others not like us. If you have been exposed to any gender studies, you will be aware of subtle discrimination against women and especially working mothers with their *double burden*.

You will know that some of it may be unintended. In South Africa in the mid-80s, the HR team brought an affirmative action proposal to the senior management committee on which I was serving. The idea was that we would somehow recruit eight black graduates (of whom there were few) and give them a fast track into management. This led to an investigation as to why we were recruiting no black school leavers (of whom there were many). It turned out that we used recruiting firms who were not recommending any black recruits to us—because they thought we did not want them. Neither our HR team nor the recruiting firms were intentionally discriminating against the school leavers, but the system was doing so and needed to be changed.

On the other hand, it is easy to fall victim to misplaced enthusiasm of which fast tracking into management can be a problem. A number of my black South African acquaintances fell victim to affirmative action, by being promoted too quickly into jobs where they could not succeed. The educational and developmental process described in Part 4 cannot necessarily be hurried just because people have suffered historical disadvantages.

The Voiceless

Perhaps the main challenge is to defend the truly voiceless. Three main groups can perhaps be helped in some way by a well-functioning finance system:

1. The very old, who are no longer able to exert themselves to be heard. Debates about tax should not forget those who are subject to onerous means tests.[2] As discussed in Chapter 8, there are ways in which the financial system can provide better financial advice and products that can secure the assets they have. My view is that there need to be ways to lock away the assets of the really old, perhaps in annuities, before their husbands have spent the money!
2. Unemployed adult singles, who have no function in society. I became particularly aware of the problems facing young adult males in my year on the Taylor Social Security inquiry in South Africa. More than half had been brought up without a father in the house, a similar proportion were failed by a dysfunctional education system, and as many were without jobs throughout their 20s. A failure of all three main socializing institutions has created one of the world's highest levels of crime. More than anything, young adults need jobs. With high youth unemployment everywhere, and young males often worse off, companies could do more to create jobs for young, relatively unskilled, males. There can be opportunities within your own organizations to look for even relatively menial jobs that can be stepping stones to bigger

[2]Means tests involve intrusive inquiries into pensioners' income, assets, and any gifts they give or receive. They are also applied at very high rates (over 50 percent in many cases) and therefore more burdensome than taxes in every way. I call them administrative atrocities—harassing pensioners for immaterial amounts. A fuller argument is made in Asher (2006).

things. If you are in the business of allocating capital, companies perhaps deserve more consideration if they are employing those who otherwise might not have jobs. Without help, these men are likely to fail to support their own children, who make up another vulnerable group, although one that is mainly beyond the reach of the finance system.

3. The mentally ill seldom have a voice that we want to hear. Various types of disability insurance have a role in supporting rehabilitation and reintegration into the workplace. As with unsocialized young men, workplaces need to go out of their way to be more resilient in dealing with the difficulties posed by working with someone with a mental illness. John Noble makes further suggestions.

Opening Opportunities

Microfinance is finance for the poor. Especially in under-developed countries, the poor would benefit from better payment systems, and from banks where they can safely maintain the real value of their savings. They would also benefit from inexpensive insurance that offers protection against disasters that would otherwise wipe them out.

This is an appealing idea for those who have worked in finance and want to make a contribution. My 5 years on the board of a small micro-lender, however, alerted me to the risks that uninformed and poorly thought out interventions will do more harm than good. Hugh Sinclair has written on these and identified further problems of incompetence and corruption. He has some useful points about improving the effectiveness of the organizations by getting close to clients, and makes this interesting suggestion for whistleblowing:

> *If you are working in an MFI and perceive injustices or are obliged to perform unsavory acts to "problem clients", go on line and anonymously blog about this almost anywhere. There are enough people now aware of the problems that someone will eventually pick up the thread. Be very careful to protect your identity. Consider contacting the regulator if appropriate. If the MFI is rated, contact the rating agencies as to "areas they may wish to investigate in more detail" – they will not*

publish anything unless they can back it up, but they may consider such advice. It's worth a try.[3]

In particular, I do not like funeral insurance. You might think there is a need because the cost of culturally acceptable funerals appears prohibitive. There are community benefits to large feasts each weekend in that the poorer members of the wider family circle are fed. Offering additional insurance is, however, an intervention in existing culture as it increases the money ultimately spent on funerals. Worse, it creates perverse incentives: in 1948, the United Kingdom totally prohibited any insurance cover for children under 10 because of the moral hazards,[4] and I think it should be banned everywhere. In addition, in Africa at least, informal burial societies fulfill a social function that formal insurance cannot,[5] and it is a pity that new formal arrangements have undermined valuable social structures.

Microcredit was seen as an important way of encouraging enterprise among the poor, and it does seem to have some, small, successes in some places. It does not help, however, if it diverts energy from more productive activities. Real development comes when people enter the formal sector with its division of labour and economies of scale. Microfinance will harm the poor if it discourages them from entering the formal sector. Jobs in mainstream formal organizations with their much greater efficiencies will pay much more. For those without the appropriate background—with historical disadvantage—the transition to the formal sector is difficult. In such cases, on-the-job training is critically important. Peter Drucker has some interesting suggestions about ensuring that people from "pre-industrial" societies are given responsibility for work group activities such "the design of jobs, the arrangement of tools and machines, and the structure of work groups" (1975, 279).

There are, however, many organizations such as the Global Alliance for Banking on Values that are working at providing "sustainable development for unserved people, communities and the environment." Whether

---

[3]Taken from http://www.microfinancetransparency.com/archivos/Microfinace_Heretic_Complete_Final_Press_Kit.pdf. Accessed November 24, 2014.

[4]See the Industrial Assurance and Friendly Societies Act, 1948.

[5]Rob Thomson and Debbie Posel.

you join them directly or apply some of their successful innovations in other organizations, it is possible to make finance a force for development of the poor.

Housing

Housing is another area which is affected by the finance sector. Poorer people can be crowded out of acceptable housing by richer people's ownership of the most useful land. My earliest awakening of a social conscience was reading these lines from Isaiah[6]:

Woe to those who add house to house and join field to field,
Until there is no more room,
So that you have to live alone in the midst of the land!

If people do not have a place of their own to occupy, they must occupy someone else's property—of necessity. One of most impressive achievements of the lawyers who worked for the interests of the poor in South Africa, was that, even under an unsympathetic apartheid government, they argued successfully that squatters could not be evicted unless there was alternative space.

We cannot all be involved in such dramatic action, but it is important to look for ways to ensure that our employers do not neglect to target viable housing finance loans to poorer people. The discussion on contribution to overhead in Chapter 7 is relevant, although so do the warnings about lending too much!

Chapter summary: At very least, we should take care that we are not extracting rents from those who can least afford it. We can help by being particularly conscious of those who cannot speak for themselves, and look for opportunities to provide financial services to those who are currently unserved. The aim is to have everyone participate in a flourishing society.

[6]Isaiah 5:8 (Revised Standard Version).

PART 4

Preparing Yourself: Finding a Vocation

In this fourth part, we return to questions of personal growth. The important questions we need to answer are: what do I want to do, or what am I doing, with my life? Who do I want to be? And Augustine's question "What do I want to be remembered for?"

You cannot answer the questions overnight. Drucker illustrates this:

> *Joseph Schumpeter, one of the greatest economists of this century, claimed at twenty-five that he wanted to be remembered as the best horseman in Europe, the greatest lover in Europe, and as a great economist. By age sixty, just before he died, he was asked the question again. He no longer talked of horsemanship and he no longer talked of women. He said he wanted to be remembered as the man who had given an early warning of the dangers of inflation* (2012, 158).

Drucker's memory of the last interview is inconsistent, as he gives another reply elsewhere:

> *Schumpeter said, '. . . I want to be remembered as having been the teacher who converted half a dozen brilliant students into first-rate economists'* (1997, 110).

Both versions are consistent with an ongoing refinement of our answers. Marcia Baxter Magolda has followed some of her students through to their mid-30s and recorded their growing sense of what she calls *self-authorship.* She has identified ongoing changes as to what they believe, and how they see themselves and others. We will look in Chapter 12 at some theories on what changes can occur.

Both versions of the Schumpeter story are also perhaps a little presumptuous, and contain something of what Ignatius, founder of the Jesuit order, called vainglory—and not just the horsemanship and loving. We can recognize Schumpeter as a great economist, but his early warning of the dangers of inflation appears to have gone unheeded and forgotten, while I am uncertain whether anyone can convert their students into anything. What would it have meant if he had failed at all three objectives through no fault of his own?

Ignatius's concern with vainglory was that he found himself constantly tempted to overestimate the importance of what he was doing and to dream of great things. If you also face this timewasting fault, you may find some help in Ignatius's "remedy for that spiritual illness": acknowledge that our lives are a gift. Call it luck if you prefer, but if you find it difficult, read Daniel Kahneman and put more feedback loops into your life. When I am daydreaming about my superior insights, I find it salutary to go through my card playing with my bridge partner—over a coffee the morning after we have played. That doddery 80-year old—she had me fooled!

The question of what we want to be remembered for should also not be a burden. At school, teachers and visiting preachers frequently told us that, as rich white youths, we had enormous privileges that came with responsibilities. They told us that our generation could change the country. For some of us this became a burden that reduced our ability to enjoy life, and created an unwarranted sense of guilt. Of course, the adults who pressed these points upon us were suffering from the same burden, which they perhaps tried to alleviate by transferring the responsibilities to us. The problem was that we, like they, did not know what to do.

Part of the problem was then, and is now, the enormity and urgency of the challenges around us: reforming the financial system, removing unfair discrimination, ending poverty, stopping violence, overpopulation, and climate change. We look at a small selection of them, feel helpless, and either give up or join the first cause that allows us to develop enough enthusiasm to hide from our helplessness.

However, if we cannot start with the problems, we can start with developing the solution—our own selves—where we do have some power, however feeble. This work of developing ourselves includes clarifying our vocations. Tim Hall and Dawn Chandler (2005) report that it is widely agreed that finding your vocation requires identification of your personal skills and strengths and a strong sense of involvement or passion. What is also necessary is that the purpose needs to be to meet some real societal need. Figure 4.1 below provides an outline of what is covered in Part 4.

Clarifying our vocation means growing in ourselves. It means developing our understanding and our skills (the head and hands in the diagram) and directing our interests and passions (the heart). It also means growing externally and playing an increasingly fruitful role in the communities in which we participate.

John Zenger and Joseph Folkman use a similar diagram to help people discover what they call their "leadership sweet spot" at the intersection of three circles of competence, organizational need, and passion. As with many in their field, their focus is on helping managers develop their effectiveness, while taking organizational needs and passions as given. The intention of Figure 4.1 is to suggest that we can develop ourselves in all areas, and that applications will occur in a wider community than the workplace.

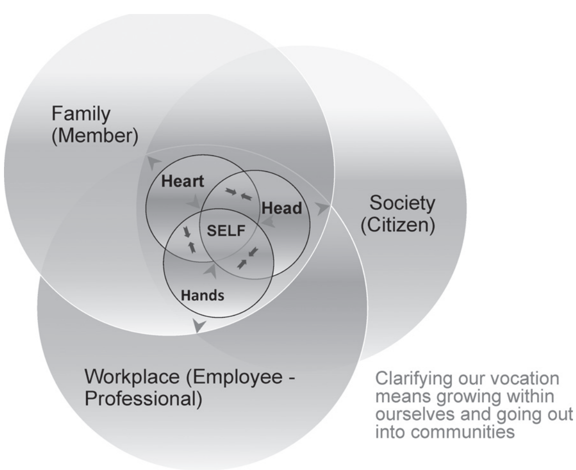

Figure 4.1 Clarifying our Vocation

Chapter 12 considers the heart, covering the relationship between our passions and the virtues, and how we can develop them. Chapter 13 discusses developing the strengths of our head and hands, and Chapter 14, how it all can be applied in the outer circles for the good of the community. We will all contribute beyond our jobs in finance, but the contributions in these other circles are beyond the scope of this book!

CHAPTER 12

Passions and Virtues

In this chapter, we explore the idea of seeing the virtues as "ethics of aspiration" rather than "ethics of obligation." Developing the virtues is not a burden: we need to reframe our perception if we see it as such. Seeking satisfaction of our own desires goes hand in hand with seeking a virtuous life, not against it.

Self-Control and Aspirations

C. S. Lewis suggests that:

> *. . . there lurks in most modern minds the notion that to desire our own good and earnestly to hope for the enjoyment of it is a bad thing, . . . We are half-hearted creatures, fooling about with drink and sex and ambition when infinite joy is offered us, like an ignorant child who wants to go on making mud pies in a slum because he cannot imagine what is meant by the offer of a holiday at the sea. We are far too easily pleased* (1965, 2).

This passage helped me to develop a creative response to the drunkenness of my fellow university students, and to aspire to find a creative response. I lived in College House, where tradition required twice-weekly binge drinking. There was a relatively small group of Christians, occasionally ribbed for not participating in pub nights. I developed a response to the ribbing that I presented to Jerry, the College drinking champion and university first-team rugby forward, one Sunday at morning tea, admittedly a time when he might not have been at his best. The key to the response was that I could not deny that getting drunk had benefits for those who participated. They had a great time and came home singing—mainly for pleasure—before passing out. There was fellowship, fun, and freedom from their worries. It was, however, temporary, costly in terms of their health as well as their pockets, and the aftermath was often disgusting. St Paul's appeal "do not be drunk with wine but be filled with the Spirit"[1] was dealing with this same fellowship, fun, and freedom—but with additional benefits to health and purse. In the New Testament, the Spirit of God is the bringer of true fellowship, joy, and freedom. Non-believers can take it as a metaphor; the point is that drunkenness is not without its short-term advantages but belongs to the category of behavior that makes "life more bearable by living less."[2] Living more meant learning ballroom dancing to get more out of parties without getting drunk, organizing touch rugby in the early evenings, and coffee and doughnuts at midnight, as well as a little volunteer work and some studying.

In corporate terms, living more means making profits by finding and developing new opportunities to serve society rather than developing schemes to charge more, or to save tax.

Some psychologists call it sublimation and see it as a defense mechanism, turning our socially unacceptable wants and desires into acceptable social behavior. Sigmund Freud is famous for having thought it was all about controlling sex. Others suggest the will to power, and more complex explanations in terms of the need for social acceptance, or the need to develop personal integrity. We can, however, see our education as refining our fundamental psychological drivers and directing them to their real fulfillment. We can recognize this in a number of different areas of our lives:

- We talk of adult tastes and of gourmets in food and drink. We also know that junk food providers pander to our childish tastes by adding sugar and salt to stimulate sales. We can decide the extent to which we cultivate simple, refined, or gross tastes.
- The metaphor of taste also applies to art, literature, and music, where we again can cultivate our ability to appreciate beauty, soul, energy etc.

---

[1]Ephesians 5: 8 (Revised Standard Version).

[2]I cannot find the source of this quote, but the idea is not mine.

- We think it better to develop a sense of self-efficacy or mastery: that we have some measure of control of our lives and can independently interact with the people and world around us. We describe those without this attitude as demotivated or even depressed.[3]
- We spend many years in formal education, and we expect those with an education to think in ways qualitatively different to those who have not had the opportunity. Not only have they developed technical skills, but we expect them to act more prudently and to exercise greater self-control when it comes to avoiding unhealthy habits.

We aspire, therefore, to the virtue of self-control to manage our appetites and lifestyles: eating, sleeping, performing, thinking, and the use of drugs and alcohol. Some of the education is explicit; other elements are tacit in that we copy our families and peers. Education and social norms are important, but we have choice in the extent to which we follow them. Recent developments in brain plasticity—popularly reported by Norman Doidge—have confirmed that our brains change when we learn to think and behave differently, confirming that we are not hard-wired and our behavioral choices do change us.

Another word for self-control is moderation, which suggests that we should not want too much or too little. Neither word, however, actually gets to the idea that our desires can actually change. The gourmet does not turn her nose up at a Big Mac because she is holding back her desire for a sweet burger; her education and virtue is that she genuinely wants something more subtle.

So what are the implications for our vocations in finance? How do we educate our desires, and develop our passions?

Let me start with indignation, because that is where I began—although it needs to be channeled rather than inflamed. As I have said above, my involvement in the retirement industry arose from my sense of outrage at unjust withdrawal benefits, later inflamed by the injustice

[3]Some of the benefits and ways of achieving self-efficacy are summarized by Bandura (1993), which is discussed in Chapter 13.

of the means test and its consequences for lower-income people. These two structures—or more accurately the indifference of those who derive a healthy living from them but had the power to change things—still have the power to get my adrenaline flowing. Even though I can now see that some of my initial resentment was partly seeded by my own interests, indignation at injustice provides a useful motivation if it can be constructively channeled. Strong emotions of these sorts are good indicators but poor companions. In their proper place, they provide a real motivation to seek justice.

In managing strong emotions, we can turn to the psychologists such as Walter Mischel's work on what he calls self-regulation. In *The Marshmallow Test*, he tells of following up children (of about 4) who wait 15 minutes for two marshmallows and those who would rather eat the one in front of them immediately. Those more able to control their desires perform better at university, are healthier, earn more, and are less likely to be divorced 30 years later. The differences in approach to decisions can be seen in their brain patterns, and appear to arise not only from genes and upbringing (supportive mothers and reliable fathers), but from training. What is noteworthy about the training is that its success is situation specific. One can be self-controlled in some circumstances and not in others, but can also teach ourselves to be more consistent by reminding ourselves of our aspirations, and preparing ourselves not to fall straight into temptation. In this he uses the distinction between fast and slow thinking that Daniel Kahneman has also been popularizing. Fast thinking can mean falling for temptations, while slow thinking is more considered and takes a longer-term perspective.

Cool self-control is, however, not enough. We can turn to the positive psychologists such as Robert McGrath, who finds that self-control is clustered with positivity, a future orientation, and even spirituality—in his analysis of how people see their own strengths. Self-control allows us to direct our passions and energies into activities with a socially useful purpose, characteristic of a fulfilled vocation.

Integrity

Integrity means we possess wholeness; the different parts of our lives are brought together; we are true to ourselves. We are not two-faced. Without integrity, we set ourselves the wasteful task of rationalizing and justifying inconsistent elements of our lives to ourselves and others.

Integrity obviously has social value, because, without the ability to trust others, we cannot usefully interact with them. Without sufficient tax honesty, governments falter. On a personal level, we usually abhor hypocrites, and constantly rationalize and justify our own actions when we seem to fall short. Although we can have an admiration for the clever, but deceitful, trickster, this can be explained in that the trickster is usually bringing down the greater hypocrite with power. We all lose respect for those who would trick the poor and helpless.

That our desires can be trained unfortunately works both ways. We may start idealistically, but can then be corrupted by our environment. If we really want integrity, we have to commit to it.

Ron Howard and Clint Korver have written a useful book for students that looks at how to make this commitment. They look at three ethical issues: lying, stealing, and doing harm. Lying and stealing are failures of integrity, and all three can be a failure of justice. They point out that these prohibitions are found in the major religions and in almost anyone who writes on ethics. They suggest three phases: awareness, thoughtfulness, and then a determination to do the best thing. An important part of implementing this determination is to develop a personal code of ethics, which they suggest be written out. We can think of people, who have set themselves high standards of integrity. It is said, for instance, of "Honest Abe" Lincoln that he was a "lawyer who was never known to lie." We all know those who are trustworthy and those who are not.

In their chapters on awareness, they refer to the confronting fact that we humans are often deceitful. It is not just that we tell white lies to protect others' feelings, but we exaggerate our achievements and importance and are quick to deflect blame by lying. Dan Ariely is a psychologist who has explored this in some detail, showing how much we rationalize—even by changing our values in order to justify our previous behavior.[4] Howard and Korver highlight that the ethical prohibition on lying cannot be absolute—illustrating again that detailed rules fail. They retell the story of Kausika, from the Hindu Mahabharat, who "ignorant of the subtleties of

[4] See his book (2013), and the paper written with Michael Norton (2008).

morality, fell into a grievous hell" by vowing to tell the truth. He thereby betrays the whereabouts of refugees fleeing from robbers who then kill them. My colleague Jim Franklin reports that English Jesuits had a similar problem when they were being persecuted. The Jesuits concluded that while an outright lie was wrong, lying could be justified after considering "the harm that will follow from truly answering such questions as whether there is a priest hidden in one's home" (2002, 85). While most of us will never face such questions, we daily face mundane temptations to tell small lies to save face or time—and white lies to keep the peace. Practically speaking, there may well be times to succumb—or least to be creative in our response.

Aspiration needs, however, to lead to preparation. This is where Mary Gentile's program is of particular help as she identifies ways to "action—that is, developing the 'scripts' and implementation plans for responding to the commonly heard 'reasons and rationalizations' for questionable practices, and actually practicing the delivery of those scripts" (2010, xiii).

Even if we are able to voice our concerns, we may need to live with the tensions and bide our time before we can see results. The issue of earnings management was discussed in Chapter 7. I faced such a problem when asked for second opinion on the value of an exotic derivative, and I am still not sure whether I made the right decision. It appeared that the company's board and shareholders were not being informed about the risks involved in the product. I did raise it with a few of the people with more direct responsibility, but saw no progress, nor opportunity to take further action. I was not directly responsible, I had insufficient proof of wrongdoing, and could have betrayed confidentiality if I had made a stand. The problem seemed to have arisen because the CEO had given key performance indicators (KPIs) to the CFO that required her to reduce borrowing costs without consideration of the risks involved. This, in turn, could have reflected a misunderstanding about financial risks and how to measure them. In retrospect, I could have been more active in looking for an opportunity to suggest that the KPIs be addressed, and the costs of borrowing measured using the actuarial analysis of surplus described in Chapter 7. This would have identified the impact of changes to interest rate assumptions that could be clearly understood by the CEO and board.

We do not have to make a stand on every issue though. There is no point getting into a huge fight unless the wrong is critically important. If you have no responsibility and limited knowledge of a matter it may be better to let it rest rather than become a busybody. In any event, we cannot save the world—and there is normally enough hard work to do that can be useful, without taking up hopeless cases. The idea of vocation is important here. It is clear that we cannot get involved in every good cause. We are surrounded by other people, who experience the same world and strive to maintain their own integrity. Although often remotely, we are with them in their efforts as they are with ours. We are called to play our part—with all our might. For others with different parts, we can be encouraging—without trying to play their roles too.

Because the different parts of our lives are continually changing, we need to continue to work on bringing them together to maintain our integrity. I have not found it to get much easier over time, perhaps, because I have changed jobs too frequently. I have, however, become more aware of my own tendency to rationalize and hide inconsistencies—and perhaps to identify it in others. My favorite story is the cab driver trying to persuade me to use him regularly because of this trustworthiness. His brother phoned to ask whether he could pick up one of the brother's fares. Without shame, he advised his brother to tell the other fare that the brother had a puncture!

Donald Longevoorts writes about the conflicts between the need to sell products and the duty to serve clients' interests, and the problems of over-servicing. He also warns of the slippery slope, which—contrary to what you might expect—normally starts not with the decision to deceive for gain, but with an error that we do not admit. Vigilance in protecting our integrity requires that we are quick to admit mistakes.

Before leaving the subject of integrity, one can make the point that we may need courage to maintain it. Chesterton makes a useful point, when he says:

> *The strong cannot be brave. Only the weak can be brave; and yet again, in practice, only those who can be brave can be trusted, in time of doubt, to be strong* (1905, 87).

We only really have to call on our courage when we are threatened in some way, and it is important, as Mary Gentile emphasizes, to be prepared. The only time I was ever in a position where our organization was asked for a bribe, I was able to steer off any conflict by calling the request by its name early in the discussions. While doing that required some courage, it was much easier and more effective than it would have been if some of my colleagues had inadvertently committed themselves to the proposed agreement.

Preparation, and the thought that needs to go into it, are perhaps the keys to maintaining integrity, which brings us on to wise thinking.

Wisdom

"Wisdom is the principal thing; therefore get wisdom"[5] was inscribed on my school crest, perhaps because our school founders saw it as the ultimate aim of education. It is the virtue to make sound judgments in the face of uncertainty and conflicting criteria, as is required particularly by experts and those in positions of responsibility.

One of the keys to obtaining wisdom can be found in the same section of Proverbs: "the fear of the Lord is the beginning of wisdom."[6] I appreciate that many people, religious and otherwise, can be repelled by this idea of fear. I use it nevertheless, because, as a metaphor, it suggests a deep respect for truth, or of the reality beyond us. It emphasizes the need to pursue ideas beyond our zones of comfort. In particular, it requires us to become conscious of "cognitive dissonance," which occurs when our existing theories and hidden assumptions fail to fit the facts. Sometimes this dissonance is marked and pleasing: coming from an all boy family and school, I remember the delight of my first intellectual conversation with a girl and realizing girls are people! Sometimes it is depressing: the results of the 1987 South African election showed, for the first time that the majority of English speaking voters supported apartheid. At the time I read the election result, I had an office with a good view of Table Mountain, and I sat for an hour or more looking at the beauty and feeling devastated—as

[5]Proverbs 4: 7 (King James Version).

[6]Proverbs 9: 10 (Revised Standard Version).

a stranger in my own land. Some of you may find this book's criticism of the finance sector similarly difficult. You may want to dismiss it as impractical and disconnected from the real world. You may be right in large measure, but please work at the cognitive dissonance!

For those in the finance sector perhaps the most difficult question is to decide to prefer wisdom to money if we have to choose. Solomon, who is said to have written Proverbs, is famous for having chosen wisdom over wealth, when he was asked by God in a dream what he most desired. Perhaps every person entering the finance industry is faced with the same question: will we be motivated by extrinsic rewards, or search for the rewards intrinsic to doing the job well?

Wisdom is one of the intrinsic rewards. We gain wisdom by delving deep into a subject for the intrinsic rewards. This deep learning is what universities are meant to encourage. One of the main teaching challenges is to get students to be more interested in the subject than in the results of the examinations. Only then will they be on the path to wisdom!

If you look around, you will find many people have made choices to pursue intrinsic rather than extrinsic rewards. I have worked with them especially in school, universities, in government and non-government organizations, and in actuarial professional committees that have always relied on volunteers. John Biggs's *Study Process Questionnaire* has an item: "I feel that virtually any topic can be highly interesting once I get into it" (1987, 49). Deep learners strongly agree; probably everyone does when they really try it.

Writers on wisdom emphasize that it moves us from a black-and-white view of the world, but keeps us from falling into the trap of thinking that everything is grey and equally worthless. One way of falling into the opposite error is to become cynical—as the agency theorist enthusiasts of Chapter 6. I suggest to you that out-and-out cynicism comes from the depths of hell (metaphorically if you like). This is because it refuses to recognize that anything can be good, that people can be well intentioned, and that the world may even reward good behavior. As a schoolboy, I was pleased at the comment *Cynic!* written on an essay. As a first-year student, however, I came across this quotation from the sociologist Peter Berger, who put me right:

> *It is possible to view social reality with compassion or with cynicism, both attitudes being compatible with clear sightedness* (1973, 47).

Being clever, particularly putting others down, is not wise. Cynicism is attractive because it makes us feel superior: but if we face the facts this is unlikely, if not absurd!

In the chapter from which I took the quote, Berger is arguing that the sociologist has to be detached from the glib answers that are given by respectable society. We all find it uncomfortable to free ourselves from prejudice. Berger is not, however, wanting to reject the considered answers of our best intellectual traditions. There is a proper adolescent desire to throw off the restrictions of our parents, and decide on our own views and identities. Graeme McLean makes the case that many adults—artists and academics among them—take this desire for autonomy too far. Wisdom is unlikely to be found in novel values.

It is admittedly not easy to find a foundation for knowledge, let alone wisdom. Philosophers have long struggled with the question of how we can know anything. They ultimately come to a similar answer to the theologians. As philosopher Michael Polanyi puts it, "we must now recognise belief once more as the source of all knowledge" (1958, 266). He is not writing about a particular set of beliefs, but does go on to write that such beliefs need to take place in a "like-minded community." Observation and reason do not provide us with indisputable truth. To recognize this teaches us humility, but to take it too seriously is foolish. We can legitimately believe that we walk on solid earth, and we can learn facts about the real world around us. Failing to believe in this way runs counter to almost all we do.

Not only do we have to live with facts we cannot prove, we also know that we cannot always know enough to make completely rational decisions. I like Herbert Simon's idea of *bounded rationality* that led to the behavioral economics that is popular today. He has observed that people use relatively simple rules of thumb to deal with complex decisions. He also suggested that, because we are not able to calculate and maximize the results of our action, that we are *satisficed* (a word he coined for this purpose) once our aspirations have been met. As he says at the end of his Nobel Memorial Lecture:

> *With all these qualifications and reservations, we do understand today many of the mechanisms of human rational choice. We do know how*

> *the information processing system called Man, faced with complexity beyond his ken, uses his information processing capacities to seek out alternatives, to calculate consequences, to resolve uncertainties, and thereby—sometimes, not always—to find ways of action that are sufficient unto the day, that satisfice* (1979, 513).

This is a rather poor version of wisdom, but it is where we stop if we do not develop a desire for a more thorough understanding of the world. In this respect, we can commend academic work that defines and quantifies different economic relationships. There is, however, much to criticize where it is more interested in models and theory rather than reality. My colleague Rob Thomson (2003) argues that we should be using utility theory for normative purposes—as a basis for making more rational, and prudent, decisions. But as he wrote (when commenting on this section of this book): "Though rationality and prudence are arguably necessary conditions for (good) decisions . . . I'm not sure that they are sufficient." Wisdom will go further and consider the decisions in context and their role in achieving social good.

Finding wisdom requires hard work; we have to want it and to place ourselves in a position where we can learn. This often requires experimentation, or finding people who see things differently, so that we can explore the cognitive dissonances!

Virtues in Psychology

If the virtues are inherent in us, but require development, one might expect to find theories about their development. I was introduced to the some of these through James Fowler's book on stages of the structure of faith, by which he means ways of thinking about the meaning of life, and sources of power to influence it. Table 4.1 is based on this book, augmented by further insights from the other writers to whom he refers.

The table gives a rough indication of how our thinking, moral reasoning, perspectives, and psychology develop over time. As might be expected, developmental stages are relatively easy to see in children—IQ is measured against chronological intellectual age, for instance, and the other childhood stages mentioned have other, empirical,

Table 4.1 Stages of Development

	Cognitive (Piaget)	Moral reasoning: (Kohlberg)	Meaning/ Perspective (Fowler, Selman)	Psychological virtues (Erikson)
Childhood	Thinking remains concrete	Rules are given, self-interested primarily	Limited to family, school	Trust, autonomy, initiative, and efficacy
Teen years	Operational (abstract) thinking	Rules of local society	My in-groups, nation	Identity/integrity—failure is fanaticism or gang culture
Early adulthood	Analytical becoming holistic	Social contracts, with greater appreciation for differences	My chosen communities, with perhaps faith and a global view	Intimacy/love—failure is isolation or promiscuity
Middle age				Generativity/care—failure is stagnation or self-absorption
Old age	Slower			Peace—failure is despair or loneliness

justification. I was astounded at how strongly my youngest son, at age 7, argued that I was telling a lie when I said I could eat a horse. At that age, everything is taken literally!

For purposes of this book, Erik Erikson's approach is most relevant as it identifies eight stages of development each culminating in a virtue. This is not the place to discuss the first four stages. The last four are, however, relevant to adult development. In each of the stages, he suggests that we face a psychological task or crisis that is created by the interaction of our physical and mental development and our environment—particularly with our most significant relationships. If we work through the crisis, we develop the appropriate virtue or basic strength. If we fail, which will often be because relationships are toxic, but may be the result of our own mistakes, then we can display one of the failures listed.

The stages (and particularly the ages) cannot be taken as too definitive, as few, if any, people fit perfectly. It is helpful to be told that we may regress in times of stress: our focus narrows and I for one become impulsive and selfish.

The evidence for stages of adult development is not as strong as that for child development, in that many adults fail to proceed to the adult stages as identified by the researchers. It is possible that the theories are wrong, or alternatively to think that some people do fail to reach their full potential and develop the virtues they are meant to have. At least some of the faults that we see around us are due to immaturity—some of which is probably our own.

Identity as Part of Integrity

Our progress through the stages depends a great deal on the challenges life gives us, and how we rise to them. The rising number of years people spend in education, for instance, appears to have extended adolescence. There appear to be more in their early 20s who have not worked through the issues of identity. One of these issues is that of accepting the different elements of our identities. Our group—family, gender, race, nation, and school, provide us with elements of a childish identity. As we grow older, we may define and redefine ourselves in terms of occupation, employer, religion, or political party. This is right; we need to know who we are. It does not, however, justify chauvinism, which is to give our loyalty to those like us, rather than to diverse communities to who we do owe some allegiance. We turn to the question of loyalty in Chapter 14.

Fowler suggested that it is necessary to leave home—at least figuratively—in order to resolve the challenge of identity. Leaving home provides a wider awareness of perspectives other than those of parents and school. As adults, we can no longer rely on other authority, but must make our own choices. In doing so, we become more analytical, which may create impatience with some of the associations of groups with which we previously identified. My experience was of finding a sense of personal continuity and integrity. I remember, soon after my 21st birthday, thinking that I was a person, not merely a series of events tied together by the same skin! I also realized that I no longer had to be embarrassed when introducing myself and saying my name.

James Marcia has suggested that this transition to identity achievement can be seen along two dimensions: exploration and commitment. The general view of those who have followed this line of research has been that exploration should come first, and commitment later. This does seem to be the more common route for today's students, but—if it leads to what they call a moratorium on commitment to values—it has its risks. If integrity is of absolute value, exploring the concept theoretically can obviously be of value, but to do so practically is not merely risky, but destructive. It would be like saying: why not try cheating at examinations and see if you like the consequences. The idea of virginity provides the physical illustration: once lost never recovered. We can of course recover in large measure from the errors we make—whether as adolescents or adults—but it would be much better to avoid costly mistakes in terms of drug and alcohol abuse, promiscuity, loss of integrity, and a failure to develop the knowledge and skills required for the later phases of life.

The researchers also talk about foreclosure, when young adults make premature commitments, possibly under pressure. Such people are inflexible in their thinking, rigid in their relationships, and develop an authoritarian style later in life. It can be associated with fundamentalist religious beliefs, and with those whose thinking is dominated by their parents, co-religionists, or other in-groups. Commitment to personal integrity and virtue has to be open eyed and unforced if it is to lead to personal growth.

The traditional view of education saw the need to hold strong personal values together with an openness to alternative theories of the world. William Perry described how his Harvard students started from a rigid concept of right and wrong with a reliance on authority. They then moved, through various degrees of uncertainty and doubt, to a personal commitment to truth and meaning. He wrote of the "paradoxical necessity to be both whole hearted and tentative—attitudes that one cannot 'compromise' but must hold together with all their tensions" (1981, 96). He describes the anxiety faced by students when the meanings and truths they had previously accepted as certain are shown not only to be uncertain, but often mistaken. This anxiety can be expressed as anger and frustration with the lecturers, which is perhaps one reason why universities are so often places of conflict.

I have used John Bigg's study process questionnaire to help my students develop a deeper learning style. One of the questions asks whether their studies have changed their view of life. It is noticeable that some of those who are more committed to their religion answer that it has not. This appears to come from a defensive approach to university learning by Christian and Muslim groups. It is a pity because, the theistic view would say that God surely wants us to understand his world as well as possible and wants us to be open to truth wherever it is to be found. It is important to guard one's integrity and other values against cynicism in all its forms, but this requires searching for deeper understanding, not resistance to any change.

The identity we achieve cannot ultimately be based on what we achieve, because we are otherwise at the mercy of circumstance. In one of my earlier jobs in the 80s, I invested 4 years on redesigning the products our company was selling. Just as we finished making the changes that I felt were necessary, the company was taken over and my innovations were effectively undone. What was the point of my efforts? Not much unless I saw the value in the striving and the making of who I am as a person—rather than what I did. T. S. Eliot has it much more dramatically:

The good man is the builder if he build what is good
. . .
And if blood of Martyrs is to flow on the steps
We must first build the steps;
And if the Temple is to be cast down
We must first build the Temple (1934, 9, 42).

Our identity is ultimately within us: the continuity of our commitments to family, relationships, work, and virtue. Working these out is *self-authorship*.

Intimacy and Love

These theories of life stages suggest that we need to develop the virtue of each stage before moving on to the next. Once we are confident in our own identity, we are ready for mature and intimate relationships, especially in marriage. Marriage does not concern us here, but the intimacy includes deeper and more mature relationships with all of those with whom we come into contact—including through our work.

Like many, I developed good friendships with my contemporaries after starting work. We played sport, socialized, and went camping together.

This is normal and healthy, but it is capable of manipulation. I have been told of consulting firms that not only demand long hours but also actively encourage younger staff to socialize actively—to develop team coherence and to prevent them from spending too much time with their spouses! Recent graduates, when I see them at professional functions, not only start looking smarter, but also paler as they get much less sun and much longer working hours.

Part of the problem lies with bosses who manipulate their young recruits' enthusiasm and need for intimacy. It is a good thing to work for a dynamic, excellent organization. It is a better thing to have time for family, leisure, friends, and exercise. This means that calls to make sacrifices for the overall good of the company often need to be resisted; bosses and colleagues will appeal to all one's guilt and fears. Early morning, late night, and weekend meetings can become routine. Anyone who leaves in daylight can be labeled as uncommitted or disloyal, and somehow socially misshapen. I remember being told that long hours in a stimulating environment would make me, together with the extra money earned, that much more attractive to my wife. The thought has stayed with me, but it stands in stark contrast to everything else I have learnt about marriage.

Excessive executive pay aggravates this manipulation. Those with large profit incentives can take an unbalanced view of their own lives, let alone those of their staff. Current fashion does not even require lip service to the obligations that companies have to be loyal to employees. Managers have no right, therefore, to ask for loyalty beyond that for which they pay. Even if they do pay, it may represent seduction to spend too much of your time on work. You should rebuff bosses that imply that you have moral obligations to put in work beyond your formal contract. Some Australians are proud that Australian building workers first won the right to an 8-hour working day in 1855. After 150 years of productivity improvements, it is a mystery why longer working days are still necessary.

Generativity

Erikson says that the challenge of middle age is to choose generativity over stagnation. His original research seems to have started middle age at age 25; later going as high as 40. The upper end started at 65 but has also increased;

people are living and working longer. It may be that Shakespeare's poem *The seven ages of man* is right in dividing this stage into two:

Then a soldier,
Full of strange oaths and bearded like the pard,
Jealous in honour, sudden and quick in quarrel,
Seeking the bubble reputation
Even in the cannon's mouth. And then the justice,
In fair round belly with good capon lined,
With eyes severe and beard of formal cut,
Full of wise saws and modern instances;
And so he plays his part.

The earlier part is likely to be more energetic but less focused. As I understand Erikson's challenge, it is to ensure that, at the end of our working lives, we have more than forty times one year of experience! He believes that a fruitful life will be concerned with caring for children, and for leaving a legacy. For those of us with children and grandchildren, this is relatively easy to envisage. For those without, we can define legacy as what we leave to future generations. This is the measure of a fruitful vocation, which in turn provides the foundation for what Erikson calls wisdom—but may be more like peace—in the last stage of life.

Making Money

However, I hear some people object, I also want to make money. Is this perverted? Do not take offence if I suggest it may be—if you are in the position that you already have enough. Let us be a little more precise and define enough as having achieved at least the average lifestyle of your nation. Before you close the book, let me give examples that are a little more subtle than the *Wolf of Wall Street*—a movie too long and distasteful to recommend, but which illustrates perversion well enough! Why would you want more money?

- To be able to compare yourself more favorably with your contemporaries? The research on happiness finds this to be important—but embarrassing to admit to it!

- To afford the good things in life? As the proverb has it, "Better a dry crust eaten in peace than a house filled with feasting—and conflict."[7] Are you fully savoring what you have, and what is available on your existing income? If yes, then more money may well increase your pleasure.
- To be able to do more good? This is possibly a little arrogant. Would you have the capacity to administer the good works you intend? Read Michael Maren, one writer who has looked at the failures of third-world aid, as one example of how difficult it is really to do good for others. Be generous with your plenty, but do not use it as an excuse for greed.
- For financial security? This is a good answer, and worth considering long and hard, because it gives us insight into how we in the financial sector can create security for everyone. People on high incomes, however, often feel a sense of financial insecurity because they are overcommitted. I have done the same myself—at a rather modest level! The solution here is merely to scale back.

I am not suggesting that it is wrong to negotiate a fair salary package, nor your fair share of entrepreneurial profit if you are in that type of job. It is also right to want to maximize entrepreneurial profit. But if you are attempting to create economic rents, or acting opportunistically in overcharging vulnerable customers destroying the environment, or garnering more than your fair share of the salary pie, then please stop. As I suggested in the first chapter, the aim that satisfies is fruitfulness, which is much wider than success, which in turn is wider than money!

Chapter summary: How do we decide what we want out of life? The cardinal virtues are required for this: self-control, integrity, and wisdom. Erikson's theory of psychological stages of development confirms the importance of these virtues, and suggests that the twenties is the time in our lives to develop the love that enables us to commit to productive personal relationships and to contribute to general human flourishing. While making money is not wrong, the ultimate objective has to be much wider.

[7]Proverbs 17.1 (New Living Translation).

CHAPTER 13

Developing Our Strengths

The head and hand circles of Figure 4.1 make up our personal competences. We need to be developing our strengths—even if not encouraged by our employers! This chapter is intended to encourage some reflection on how we can do this.

Satisfaction and Success

Thus far, I have tried to avoid making arguments that aspiring to virtue is likely to make us more successful, or even to feel better. The main reason is that we aspire to obtain the virtues for their intrinsic value, not for incidental reasons like success and happiness. One of the other reasons is that we cannot guarantee success. Another reason is that feeling successful and happy requires different methods. In this section, therefore, we now turn to finding satisfaction and happiness.

In their research, Hall and Chandler ask whether the arguments made for a vocation or calling are really just *ex post* rationalizing—by older people when they see what they have achieved. While rationalization does occur, they confirm that there are those who do live out a life in which they have set out and reached difficult long-term goals. They confirm that there is much psychological satisfaction in setting goals, in working toward them—particularly in a community—and obviously in achieving them.

Achievement

We should not underestimate our need for a sense of achievement. John Perry has written an amusing little book on procrastination, where he tells how he writes a list of trivial tasks the night before: get up, get dressed, have coffee etc. He finds satisfaction in crossing them off when he gets down to work. I find the same—our emotions are peculiar.

The obverse of this is that setting ambitious long-term goals can lead to personal unhappiness if they take too much time to complete. We need to turn long-term vocational aspirations into achievable shorter-term goals. Without them, we get depressed. Bandura's work on self-efficacy says:

> *The most effective way of creating a strong sense of efficacy is through mastery experiences. Successes build a robust belief in one's personal efficacy. Failures undermine it, especially if failures occur before a sense of efficacy is firmly established.*
>
> *If people experience only easy successes they come to expect quick results and are easily discouraged by failure. A resilient sense of efficacy requires experience in overcoming obstacles through perseverant effort. . . . After people become convinced they have what it takes to succeed, they persevere in the face of adversity and quickly rebound from setbacks* (1998, 624).

This applies at home, school, and workplace. For home and school, it ties in with Erikson's virtues of purpose and competence. For workplace, you need to work where your bosses or colleagues appreciate you and your contribution.

Bullying and Stress

The worst of bosses to work for are those who are cruelly critical. They undermine your self-esteem and performance, not least because you spend so much emotional energy defending yourself. Bandura writes about managing the emotional energy:

> *. . . 'You cannot prevent the birds of worry and care from flying over your head. But you can stop them from building a nest in your head.' Perceived self-efficacy to control thought processes is a key factor in regulating thought produced stress and depression. It is not the sheer frequency of disturbing thoughts but the perceived inability to turn them off that is the major source of distress* (1993, 133).

He suggests therapy and exercises in achieving mastery to deal with this type of stress. I find shouting, singing, and praying all work! Getting professional help can be a good idea. Getting out of the situation is another. It is wise to prepare yourself by not becoming too dependent on the income from the job.

Criticism from your boss is a real source of stress. It can help to recognize it as bullying. If there are no protections within your workplace that you feel you can use, it may be possible to respond firmly in a way that discourages the bullying. In a fight with a school bully, I gave him a bloody nose: no skill, pure accident. He did not return for another fight. Twice I have found the metaphorical equivalent. Pick a fight you can win and fight it hard. On both occasions, it occurred when a boss criticized me and copied his e-mails to one of my subordinates. I made it clear to them in private that they were entitled to criticize me, but that it was unacceptable to undermine me at the same time. In both cases, they kept their distance thereafter. This approach may not always be possible. If not, resign or get a transfer. Do not be ashamed to get psychological help.

Bandura offers a surprising word of comfort to those more prone to stress:

> *People who experience much distress have been compared in their skills and beliefs in their capabilities with those who do not suffer from such problems. The findings show that it is often the normal people who are distorters of reality. But they display self-enhancing biases and distort in the positive direction. People who are socially anxious or prone to depression are often just as socially skilled as those who do not suffer from such problems. But the normal ones believe they are much more adept than they really are. The non-depressed people also have a stronger belief that they exercise some control over situations.*[1]

Overconfidence

He then goes on to suggest that social reformers and business innovators must be optimistic of their chances of success. Without "a tenacious

[1]Accessed August 30, 2014. http://web.stanford.edu/~kcarmel/CC_BehavChange_Course/readings/Bandura_Selfefficacy_1994.htm.

self-efficacy," they will not have the perseverance to overcome obstacles. He then provides examples of people with an enormous confidence, who have succeeded against long odds. This is a version of the common view that "you can do anything you want." This is probably not true. It is not enough to know the successes of those who are overoptimistic; we also need to know the failures or we fall prey to *survival bias*. I am afraid that it reminds me of the joke that the definition of a social scientist is someone who thinks that data is the plural of anecdote.

While there is much to learn from anecdotes and more expansive stories of success (and failure), we need a deeper analysis. The research[2] suggests that optimism in business is more likely to end in failure than success. Donald Duchesneau and William Gartner find that, when compared with less successful start-ups, successful entrepreneurs were more aware of the risks beyond their control and so worked harder and more carefully. When the optimism leads to hubris (pride), then the likelihood and consequences of failure are likely to rise. Enron, the Equitable, HIH in Australia are all recent examples.

On a mundane level, the research also brings out the way in which individuals who are more certain of themselves can have greater influence—and thereby dominate those who have a more realistic grasp of the situation, and who understand the uncertainty. My most vivid experience of this was how we elected our platoon captain during my basic military service. We had to select a leader on the first evening, before we had come to know anyone else in the platoon. Predictably, we elected the loudest and the most confident individual. He was, however, useless as a leader, and had to be replaced before a week had elapsed.

Of course, like this anecdote, studies are stories from a particular time and place, and not necessarily useful for predicting what might happen in another environment. If we are to value our integrity, we want a sober measure of our abilities. If we are thinking of attempting a project, we need to weigh up the potential benefits as well as our chances of success, and then put in the hard yards. Clarity as to our real strengths and abilities is more likely to increase our chances of success than mere confidence.

How do we go about identifying our specific strengths? For those in or emerging from your education, your results will provide a first guide.

[2]See for instance Hmieleski and Baron; Lovallo and Sibony; and Ucbasaran et al.

Careers counselors will provide further guidance. They will use various tests, such as those found at *strengthsquest.com*, which look at how you think; relate to others; and the environments that stimulate you. Like personality tests, some of these will be context specific, but some insights will resonate.

Once your career has begun, the scientific approach is to reflect on activities that you have especially enjoyed or found particularly successful. On this topic, Peter Drucker tells what he learnt from his study of history:

> *I found that two European institutions had become dominant forces in Europe: the Jesuit Order in the Catholic South and the Calvinist Church in the Protestant North. Both were founded independently in 1536. Both adopted the same learning discipline. . . . Whenever a Jesuit priest or a Calvinist pastor does anything of significance—making a key decision, for instance—he is expected to write down what results he anticipates. Nine months later he traces back from the actual results to those anticipations. . . . I have followed that method for myself now for 50 years. It brings out what one's strengths are—and that is the most important thing an individual can know about himself or herself. It brings out areas where improvement is needed and suggests what kind of improvement is needed. Finally, it brings out things an individual cannot do and therefore should not even try to do.*[3]

It takes time. It may be painful because we may not have even the basic talents necessary to succeed in things on which we have set our hearts. Albert Einstein apparently wanted to be a great violinist!

For me, it was relatively clear by my late 20s that ideas were my stock-in-trade, but explaining them was not. It took a little longer to find ways of taking smaller steps in my explanations, and to stop exploring new thoughts aloud when lecturing. I am afraid that my students still find me confusing—initially at least! I also prefer working on my own or in smaller groups, but again it took time to appreciate that people have been surprisingly willing to help when you ask. It remains a big and pleasant surprise to find collegiality—even if everyone has his or her own agenda!

---

[3]From My Life as a Knowledge Worker, http://www.inc.com/magazine/19970201/1169.html.

Developing the picture requires reflection more frequently than nine month intervals. The Jesuits' *daily examen* looks not so much at fruitfulness, which is long term, but at our feelings of what they call consolation and desolation. The examen[4] involves reflecting on each activity of the day, and our emotional responses both now and at the time: anger, disappointment, frustration etc. It then requires us to make an appropriate response to the emotion—after reading a passage about Jesus. Such responses include repentance at inappropriate actions, letting go our obsessions, and finding a sense of forgiveness for those who have wronged us. I cannot say how others will find the approach. Similar processes may well appeal to Muslims and Jews. Others will need to develop a suitable metaphor for the presence of God, and perhaps make other adaptations. The practice of honest reflection on our feelings, and responding to them appropriately must, however, be emotionally healthy and contribute to developing peace with ourselves, others, and the world. Chris Lowney (2010), having experienced both the Jesuit training and 17 years working for J. P. Morgan, writes convincingly of the *Heroic Leadership* he sees as having been developed by the former.

Developing Expertise

There are no short cuts to expertise, and while wisdom is more than knowledge and expertise, one cannot be ignorant and make consistently wise decisions.

Psychologists Daniel Kahneman (the Economic Nobel winner) and Gary Klein have written a delightful paper on their different approaches to claims of expertise. They agree one can only become expert in a field that displays "a regular environment and an adequate opportunity to learn it as preconditions for the development of skills." They also agree that experts need humility. They observe that:

> . . . *professionals exhibited genuine expertise in some of their activities but not in others. We refer to such mixed grades for professionals*

[4]The Irish Jesuit website http://www.sacredspace.ie/ provides an outline of the steps with some helpful hints.

> *as 'fractionated expertise,' and we believe that the fractionation of expertise is the rule, not an exception* (2009, 522).

Like Nassim Taleb, author of the *Black Swan*, they identify finance—investment management particularly—as a field where it is difficult to develop and identify expertise. Expertise in finance can have two sides to it. The first is knowledge based, Bent Flyvbjerg writes:

> *Common to all experts, however, is that they operate on the basis of intimate knowledge of several thousand concrete cases in their areas of expertise. Context-dependent knowledge and experience are at the very heart of expert activity* (2006, 219).

The second is skill—mathematical for some, legal for others, programming for yet others. Expert skills require practice. Experts in the development of expertise, such as Anders Ericsson and Neil Charness, suggest that one needs 10 years of:

> *individualized training on tasks selected by a qualified teacher as deliberate practice . . . Unlike play, deliberate practice is not inherently motivating; and unlike work, it does not lead to immediate social and monetary rewards* (1994, 738).

This example given by Albert Carr encapsulates what I am attempting to say:

> *An executive persuaded his company's management to make a major advance in its antipollution policy. His presentation on the alternatives, on which he had spent weeks of careful preparation, showed, in essence that, under his plan, costs prove to be substantially less than the potential costs of less vigorous action.*
>
> *When he finished his statement, no man among his listeners, not even his most active rivals, chose to resist him. He had done more than serve his company and satisfy his own ethical urge; he had shown that the gap between the corporate decision and the private conscience is*

> *not unbridgeable if a person is strong enough, able enough, and brave enough to do what has to be done* (1970, 64).

If Chesterton is right that strength comes from courage developed by the weak, and passion comes from directed self-control, expertise comes from hard work and practice rather than innate skills.

Blind Alleys and Defeats

There is no pleasure without the potential for pain

No truth without the risk of hypocrisy
No faith without doubt
No courage without fear
No reward without risk
No life without death.

The more ambitious your vocational goals, the greater will be the risk. I finish this chapter, however, with some words meant for encouragement in times of defeat. Even if the risks were carefully calculated and failure not your responsibility, such times are difficult. They are even worse when we know we are partly responsible, or at least cannot stop blaming ourselves. We therefore come back again to the need for forgiveness to give us the strength to move on. Recovery is possible, for the story of our vocation is not complete until we are being remembered!

Chapter summary: To develop our strengths we need to reflect—deeply—on what we are good at, and set goals that we are capable of achieving. Expertise does not come without practice. Everyone has to pick themselves up and carry on at times.

CHAPTER 14

Serving Society's Needs

The larger circles in Figure 4.1 are the communities in which we participate. The first section below looks at the nature of the communities that we might serve. I then outline an approach to management that applies to both government and private organizations that creates value in a manner based on service and integrity. The final section suggests that it is best to start with the nearest tasks and not be distracted by big ideas.

Communities

While short-term successes are important to our psychological health, relationships in our communities are critical. This is clear in Erikson's model. These communities also provide the context for our development of vocation.

We can distinguish three types of community to which we owe some loyalty. The first type is small groups of people with strong personal relationships between them, communities of which we are members. I have called them families in Figure 4.1, but they include communities of faith, our friends, neighbors, and perhaps the group of people with whom we work. Justice, which underlies trustworthiness, reciprocity and the fair sharing of benefits and obligations, is a prerequisite for building these communities. Failure to participate dismembers the community; but demanding too much distorts it. The definition of justice as what we owe to others helps us to recognize it when people demand too much from us. Even family members are not entitled to make appeals to loyalty that require breaches of the law (or of just laws anyway). If they were loyal to us they will not put us in that position. Giving everyone their due has limits, sometimes more than we want to give, and sometimes less than they want to take.

The second type of community is the political communities to which we belong by rights of residence or citizenship: city and state. We may never meet or even have much in common with our fellow citizens, but we owe them something by virtue of our common membership of the body politic. Feelings of loyalty to these communities are often much weaker—many people will not even vote, let alone get involved in the political process. They therefore present a collective action problem: *common goods* benefit everyone, but the costs of each contributing individually exceed the marginal benefit gained by doing so. If some people voluntarily contribute to creating the goods, there is a temptation for others to *free ride*.

Finding an element of service to the *common good* in our vocations is one of the characteristics of the just person, who would want to give back to the community at least what he or she had received. It would be a mistake to frame this in terms of psychic benefit, or utility, because it mistakes both the direction of causation and the nature of the benefit. We serve because it has become a part of our character, and the satisfaction from successful service is a bonus that we have not looked for.

The organization for which we work creates a third type of community, where our interactions are necessarily commercial and contractual—in part at least. We owe service to our employers or customers, and there is a compulsion to provide it, that does not exist in other communities. Work places can become unpleasant places to the extent that those with the power of compulsion exercise it unjustly, and without a sense of service to the greater good. In the workplace, I suggest that our vocation will lead to us to becoming professional, in the sense of ensuring that we develop competence and integrity to meet our clients' needs. It is a bonus if we can also develop a sense of camaraderie that can exist in the personal first type of community discussed above, but I do not believe that virtue will necessarily seek intimate friendships with work colleagues.

There is also a fourth type of community with which we have no real connection or responsibility, except that we share similar characteristics, interests, values, or culture. These are ethnic, religious, and cultural communities, which Benedict Anderson calls *imagined communities*. He suggests that they originate from reading a common literature. While we may share a sense of community, it is right to be suspicious of calls for loyalty—especially when they are defined ethnically, but even where they are identified with nations, or sports teams! Unscrupulous politicians everywhere abuse a sense of national, religious, or racial identity for their own unjust purposes. The result is often conflict.

You might like to take an evolutionary perspective here. Loyalty and justice form important functional purposes in the first two types of community: the better they are developed, the more successful the communities will be. The application of loyalty to the third and fourth types of community is, in these terms, a manipulation of the evolutionary instinct.

The first three types of communities have institutions of governance: formal and informal; beneficial, neutral, and perverse. If they will not evolve spontaneously, we have to engage with the development or reform of these institutions—the need to do so often being a call for vocation.

Doing the Work: Leading and Controlling

Even if, like mine, your managerial roles are modest, you will need to think about how organizations (private and public) create value, and how you can contribute. The practice of management—particularly if it seen as a profession—can be part of a valid calling that creates communities of service. In this, I think that Alistair MacIntyre is too pessimistic in his assessment of the modern "corporate manager, who is now mouthing formulas that she or he learned in a course in business ethics, while still trying to justify her or his pretensions to expertise" (2007, xv). There is obviously a lot of puffery written and spoken, but the difference between good and bad managers cannot be denied!

Making People's Strengths Productive

I have had the opportunity of working for some good leaders and observing others while serving as non-executive director. My experience agrees with Drucker's view (with apologies for the masculine gender) that:

> *The effective executive makes strength productive. He knows that one cannot build on weakness. To achieve results, one has to use all the available strengths—the strengths of associates, the strengths of the superior, and*

> *one's own strengths. These strengths are the true opportunities. To make strength productive is the unique purpose of organization. It cannot, of course, overcome the weaknesses with which each of us is abundantly endowed. But it can make them irrelevant. Its task is to use the strength of each man as a building block for joint performance* (1967, 71).

A focus on strengths makes a huge difference to morale. I have written about the need to avoid bosses who criticize. Those that contrive to "catch people doing things right" are a joy to work for. Robert Carr was chair of the Prudential in the United Kingdom when I was actuary of their South African subsidiary. He took pains to talk to managers a long way down the chain of command. My wife told me that I came out of my meetings with him "with my tail visibly wagging." All he did was to take time to read my board reports carefully, and to encourage me to continue in what was good about them.

We are talking about those strengths that get the job done. Drucker emphasizes the importance of giving people responsibility. The need to give responsibility for the job arises partly from the nature of the work and partly from the way in which people are motivated. The argument from the nature of work requires us to understand that workers are not automatons performing to manager's detailed instructions. Machines are in any event increasingly replacing this type of work. The argument from motivation arises from Herzberg's research mentioned above—that motivation is intrinsic to the work.

Controlling Without Interference

Personal integrity and organizational effectiveness and efficiency also require that people and organizations squarely face up to the material facts about their performance. Measuring performance is also required for continuous learning, but is an outworking of the virtue of self-control more than criticism, even if it is well-balanced. It is the worst of managers who see their role as the control of their staff.

I spent a few weeks with Scottish Life in the 90s, when it had a reputation for administrative efficiency. Each of the functions in their pensions administration division had been allocated a standard time (how long it should take on average to perform), and a service standard (the maximum elapsed time before the client has a response). Each day, tasks were allocated to staff based on the time they had available, the standard times of the tasks and their priority. The objective of the system was to ensure the company met its service standards. Efficiency, however, benefited considerably, as Brian Duffin, the CEO, wrote to me:

> *Our experience is that we cannot really distinguish between service standards and performance efficiency—if you are well-organised both will improve together. The key is the preparation of useful management information and to make this available as far down the organization as possible. In this way, individuals and teams can take ownership for their activities and work for minor as well as major improvements—and see the extent to which they are successful. It even allows them to experiment and of course to compare best practice on similar activities in different parts of the company.*

Those interested in the effect of remuneration on performance may be interested to know that this quantitative performance system did not determine pay. I was not given the reasons, but the assumption may have been that the people were already motivated!

The same idea is captured by the principle of subsidiarity that is intended to underlie the design of European Union governance arrangements. The Oxford English Dictionary defines subsidiarity:

> *as the idea that a central authority should have a subsidiary function, performing only those tasks which cannot be performed effectively at a more immediate or local level.*

As with Vincent Ostrom's discussion of democracy and the *common good*, quoted in Chapter 3, we flourish better in shared organizations where power is distributed widely.

Codes of Ethics and Practice

I have found that the ethical codes of the actuarial profession do make it easier to challenge unethical behavior in other actuaries. I have therefore invested many hours in committees refining and developing them. The codes have, however, recently tended to grow into depressingly detailed lists of what not to do. While this makes it easier to convict an offender, it may make it more difficult to reform poor—and reinforce better—behavior. I find it much easier to phone a fellow professional and suggest that he or she is close to a rather vague line, than to point out that they have infringed a clear boundary that must be enforced. At time of writing, I am enforcing a rule against "self-plagiarism", which as one offender accurately observed, is an oxymoron!

On the other hand, I have not been enthusiastic about company codes of ethics, because they seem to feed hypocrisy. I seem to have been wrong. The research does indicate that affirming the virtues, even in such ways as repeating or signing a code of ethics, does help make people more honest.[1] The risk of hypocrisy will be there, as a manifestation of vice, but it gives no reason not to aspire to virtue. François de la Rochefoucauld puts it nicely: "Hypocrisy is the homage which vice pays to virtue."

The best ethical codes are concise if not exactly simple. Ten Commandments are more than enough. Focusing on meeting the needs of clients is a good start. Peter Drucker regards the most important ethical principle for businesses as being the same as found in the doctors' Hippocratic Oath: "primum non nocere"—above all not, knowingly, to do harm. This involves avoiding adverse consequences including the unintended, and is often a difficult standard to meet.

Dysfunctional Organizations

Communities can be dysfunctional, and not just in over-populated under-developed areas where the land is overgrazed and fisheries exhausted. Robert Jackall describes the relationships in some American corporations:

[1]Lisa Shu and her colleagues have done recent work on this.

> *. . . success and failure seem to have little to do with one's accomplishments. . . . Rather managers see success depending principally on meeting social criteria . . .* (1988, 604).

However, the social criteria he speaks of mean obsequious kowtowing to bosses and laughing at their jokes. "It means saying one thing and meaning another . . . and maintaining bland, smiling, and agreeable public faces." I have not seen anything quite as crude, but believe that it can be true. Blake Ashforth and Vikas Anand describe the *normalization of corruption* in both private and public sectors:

> *We argue that three mutually reinforcing processes underlie normalization: (1) institutionalization, where an initial corrupt decision or act becomes embedded in structures and processes and thereby routinized; (2) rationalization, where self-serving ideologies develop to justify and perhaps even valorize corruption; and (3) socialization, where naïve newcomers are induced to view corruption as permissible if not desirable. The model helps explain how otherwise morally upright individuals can routinely engage in corruption without experiencing conflict, how corruption can persist despite the turnover of its initial practitioners, how seemingly rational organizations can engage in suicidal corruption and how an emphasis on the individual as evildoer misses the point that systems and individuals are mutually reinforcing* (2003, 1).

The obvious strategic response is to get out if possible. If you cannot, or feel challenged to try to make a difference, Geoff Moore has outlined some general ideas. The first is to attempt to refocus the culture of the organization on its *core practice*, creating customers in Drucker's language. Second is to begin to reinstate a culture of virtue. It makes a difference if it is acceptable to talk about integrity, courage, and justice or fairness. You may well find, as I did, that it was difficult to introduce the concept of fairness. One approach I have found helpful is to harness the insights of a lawyer who has studied jurisprudence—or better still some philosophy—and who will explain the law of equity and the risks of acting unethically.

An ethical community has to set standards, but also to be able to forgive, which brings us back to John Braithwaite's work on *restorative justice* and *reintegrative shaming* that recognizes the perpetrators' membership of the community, and not *stigmatizing shaming* that rejects the perpetrator.

Leadership

It is possible to frame the idea of vocation as that of leadership: changing the world for the better. In many cases, a vocation will propel you into positions of leadership, or require of you a stand that others will follow. There is, however, a danger of vainglory on one hand, or developing a sense of inadequacy on the other—and there may be some discomfort that you are manipulating of others. If you do find yourself in positions of responsibility, I like another of Drucker's summaries (again with apologies for the masculine gender):

> *But the leader who himself has strength and leaves behind strength—the truly 'great man' and genuine 'leader'—looks completely different and acts completely differently from the 'great man' of popular myth. He does not lead by 'charisma'—an abomination and phony, even when it is not a press agent's invention. The truly strong man leads by hard work and dedication. He does not centralize everything in his hands but builds a team. He dominates through integrity, not through manipulation. He is not clever, but simple and honest* (1996, 155).

Robert Greenleaf coined the phrase *servant leader*, which encapsulates the idea of the founder of Taoism, Lao Tze's: "When the best leader's work is done the people say, 'We did it ourselves'." The purpose of leadership is ultimately service to those being led, and other stakeholders who benefit.

Starting with the Nearest Challenge

My wife had a house rule for my sons and me, "he, who has the vision, has the job." If you see the cupboard is bare, or the windows are dirty, do something about it! We can apply the same principle more widely. Feeling that "someone should do something" is an indication that you should perhaps think about doing it yourself. In terms of the community need, heart and hands of Figure 4.1:

- You have identified the need.
- You obviously feel something about the matter.
- You have some idea about how to do it, and so you are likely to be competent!

The place to start is with our families, local communities, and own organizations. The temptation to make an impression at a higher level is the stuff of the vainglory mentioned earlier, and in the discussion of the *common good*. You cannot meet the needs of society, only the needs of particular people, and then only those with whom you come into contact. As T. S. Eliot has it about the desert (as a place of need):

> *The desert is not remote in southern tropics,*
> *the desert is not only around the corner,*
> *the desert is squeezed in the tube-train next to you,*
> *the desert is in the heart of your brother* (1934, 9).

We can be tempted to give up on the immediate challenge. How many students start talking about going into church and charitable work as their first-year examinations approach? I confess I did! When we get older, in different environments, good works can replace doing our own jobs well. Drucker is blunt:

> . . . *Good intentions are no excuse for incompetence. And the manager who believes that social consciousness is a substitute for managing his business—or his hospital or his university—so that it produces the results for the sake of which it exists, is either a fool or a knave or both* (1975, 809).

It is great to have a wide and global vision, but action must be local.

Chapter summary: We add value to our communities by service and creating goods that would not be created but for the existence of institutions. There are reasonable mutual obligations of loyalty. Management practice is more effective if it encourages the best in people, building on their strengths and attempting to restore dysfunctional situations. Codes of practice can be helpful. We need to start with the nearest duties.

Conclusion

I have tried in this book to bring together a cluster of resonating views from a variety of perspectives and disciplines. The perspectives do not create a blueprint so much as a scaffold within which to understand the development of your vocation. I have often quoted my favorite authors, especially:

- philosophers Alisdair MacIntyre and David Carr on our aspirations to virtue
- Adam Smith's voicing of the values of traditional economics and indignation against injustice
- psychologist Erik Erikson on stages of personal development
- management writer Peter Drucker on vocation and building strengths in organizations
- political economists Vincent and Elinor Ostrom on the development of *common goods* and
- criminologist John Braithwaite on *responsive regulation* and *restorative justice*

They come from disparate disciplines but their views fit into views of the world that are wide, generous and nurturing of the virtues.

They have each provided insights into the different components of what makes for a vocation. Vocation links our psychological needs for achievement and relationships with the social and economic purposes of the organizations in which we work. It involves developing ethics and competence. Vocation is an evolving story of *self-authorship*, an aspiration as much as a plan, and so provides a context in which to find—and give—forgiveness for errors and failures. It gives us freedom from slavishly following inflexible rules, calls us to challenge injustice where we can make a difference, and construct institutions that provide *common goods* to flourishing communities.

Those with a sense of vocation may find it uncomfortable to work in organizations where overweening greed and ambition lead to over-servicing, overcharging, dishonesty, and manipulation of others. The finance sector is, however, more than this. It has an important social role in the allocation of capital to its most productive and innovative uses, and the provision of financial security. The first lifts people out of poverty and the second prevents them from entering it. The sector can, however, only fulfill its role to the extent that there are people with the courage to confront injustice, and the wisdom, skill, and imagination to direct energy to where it will be most fruitful.

My hope is that, in this book, you would have found some affirmation of your best desires to develop a vocation of service in the financial industry. If you are starting out, I wish you well as you grow into that vocation. May your work be fruitful, your friendships enriching, and may you enjoy peace and prosperity too! If you are mid-career, I hope that some of the ideas have resonated and helped you clarify what you can do for the better building of our common life together. If you are older and wiser, I challenge you to caste off any cynicism that you have accumulated, and look to make the stands of courage that we need to restore and maintain the integrity of the world that we are building.

Reflection Exercise

- Name the four cardinal virtues. To what extent have you developed them? Can you say that you actively aspire to them? Do you want to? Why?
- What about integrity and love? Do you agree with Erikson's view that they are particular challenges of young adulthood? Are there reasons why you have not completely met the challenges?
- What expertise have you developed? In which areas do you have the greatest strengths? Where have you been the most productive? Where have you enjoyed yourself the most in the past year? Where would it be more fruitful to add to your skills?
- Where in the community do you want to make your vocational contribution? What would you like to achieve in the next year? And the next 20 years? What do you want to be remembered for?
- Did you avoid some of these questions because you have failed? If so, do you need to make restitution or be reconciled to others? Can you put the failures behind you? Do you need help?

Bibliography

Abrahamson, M., T. Jenkinson, and H. Jones. "Why Don't US Issuers Demand European Fees for IPOs?" *The Journal of Finance* 66, no. 6 (2011):2055–2082.

Agarwal, V., and N. Y. Naik. "Risks and Portfolio Decisions Involving Hedge Funds." *Review of Financial Studies* 17, no. 1 (2004):63–98.

Akerlof, G. A., and R. J. Shiller. A*nimal Spirits: How Human Psychology Drives the Economy, and Why It Matters for Global Capitalism.* Princeton, NJ: Princeton University Press, 2010.

Alesina, A., R. Di Tella, and R. MacCulloch. "Inequality and Happiness: Are Europeans and Americans Different?" *Journal of Public Economics* 88, no. 9 (2004):2009–2042.

Amin, G. S., and H. M. Kat. "Hedge Fund Performance 1990–2000: Do the 'Money Machines' Really Add Value?" *Journal of Financial and Quantitative Analysis* 38, no. 2 (2003):251–274.

Anderson, B. *Imagined Communities: Reflections on the Origin and Spread of Nationalism*. London: Verso, 2006.

Ariely, D. *The Honest Truth About Dishonesty: How We Lie to Everyone—Especially Ourselves*. New York, NY: HarperCollins, 2013.

Ariely, D., and M. I. Norton. "How Actions Create—Not Just Reveal—Preferences." *Trends in Cognitive Sciences* 12, no. 1 (2008):13–16.

Asher, A. "Effective and Ethical Institutional Investment." *British Actuarial Journal* 4, no. 5 (1998a):969–1027.

Asher, A. "Investment Performance Measurement." *Transactions of the International Congress of Actuaries* 7 (1998b):239–248.

Asher, A. "Pension Benefit Design and the Integration of Insurance Benefits over the Life Cycle." *South African Actuarial Journal* 7 (2007):73–115.

Asher, A. "Salary Linked Home Finance: Reducing Interest Rate, Inflation and Idiosyncratic Salary Risks." *Australian Actuarial Journal* 17, no. 1 (2011):117–148.

Asher, A. "The Fight Against Poverty: Social Security, Job Creation and Responsibility." In *Defining a New Citizenship for South Africa and the Fundamental Values that Will Shape It*. Johannesburg: Konrad-Adenauer-Stiftung—South Africa Office, 2004, pp. 63–70. http://www.kas.de/wf/doc/kas_4869-1522-2-30.pdf?040623160934 (accessed April 7, 2015)

Asher, A. "The Lifetime Harvesting Plan: Smoothed Annuities with Sharing of Mortality, and Averaging of Investment," Presented to the Actuaries Institute Financial Services Forum (2012). http://www.actuaries.asn.au/Library/Events/FSF/2012/FSF2012PaperAnthonyAsher.pdf (accessed December 12, 2014).

Asher, A. "The Relative Investment Performance of the Community Growth Fund." *South African Actuarial Journal* 5 (2005):1–26.

Ashforth, B. E., and V. Anand. "The Normalization of Corruption in Organizations." *Research in Organizational Behavior* 25 (2003):1–52.

Australian Taxation Office. *Improving Tax Compliance in the Cash Economy.* Report to the Commissioner of Taxation, Cash Economy Task Force, Australian Taxation Office, Canberra, 1998.

Ayres, I., and J. B. John. *Responsive Regulation, Transcending the Deregulation Debate.* New York, NY: Oxford University Press, 1992.

Bai, J., T. Philippon, and A. Savov, *Have Financial Markets Become More Informative*? Working Paper no. w19728. National Bureau of Economic Research, 2013.

Bandura, A. "Health Promotion from the Perspective of Social Cognitive Theory." *Psychology and Health* 13, no. 4 (1998):623–649.

Bandura, A. "Perceived Self-Efficacy in Cognitive Development and Functioning." *Educational Psychologist* 28, no. 2 (1993):117–148.

Barro, R. J. "Democracy and Growth." *Journal of Economic Growth* 1, no. 1 (1996a): 1–27.

Barro, R. J. *Determinants of Economic Growth: A Cross-Country Empirical Study*. Working Paper no. w5698. National Bureau of Economic Research, 1996b.

Basel Committee on Banking Supervision. *Observed Range of Practice in Key Elements of Advanced Measurement Approaches.* Basel: Bank for International Settlements, 2006.

Basel Committee on Banking Supervision. *Supervisory Guidance for Managing Risks Associated with the Settlement of Foreign Exchange Transactions.* Basel: Bank for International Settlements, 2013.

Baumol, W. "Entrepreneurship: Productive, Unproductive and Destructive." *Journal of Political Economy* 98 (1990):893–921.

Baxter Magolda, M. B. *Making Their Own Way: Narratives for Transforming Higher Education to Promote Self-Development.* Sterling, VA: Stylus, 2004.

Berger, A. N., and G. F Udell. "The Economics of Small Business Finance: The Roles of Private Equity and Debt Markets in the Financial Growth Cycle." *Journal of Banking & Finance* 22, no. 6 (1998):613–673.

Berger, P. L. *Invitation to Sociology: A Humanistic Perspective*. Woodstock, NY: Overlook Press, 1973.

Berle, A. A., and G. C. Means. *The Modern Corporation and Private Property.* New York, NY: The Macmillan Company, 1933.

Biggs, J. B. *Study Process Questionnaire Manual. Student Approaches to Learning and Studying*. Hawthorn: Australian Council for Educational Research Ltd. 1987.

Boatright, J. R. *Ethics in Finance: Critical Issues in Theory and Practice*, New Jersey, NJ: John Wiley and Sons, 2010.

Bodie, Z. "An Analysis of Investment Advice to Retirement Plan Participants." In *The Pension Challenge: Risk Transfers and Retirement Income Security*, ed. O. S. Mitchell and K. Smetters, New York, NY: Oxford University Press, 2003, pp. 19–32.

Bogle, J. C. *The Battle for the Soul of Capitalism*. New Haven, CT: Yale University Press, 2005.

Braithwaite, J. "Accountability and Governance under the New Regulatory State." *Australian Journal of Public Administration* 58, no. 1 (1999):90–94.

Braithwaite, J. "Institutionalizing Distrust, Enculturating Trust." In *Trust and Governance*, ed. V. Braithwaite and M. Levi, New York, NY: Russell Sage Foundation, 1998, pp. 343–375.

Braithwaite, J. *Restorative Justice and Responsive Regulation.* Oxford: Oxford University Press, 2002.

Braithwaite, J. *Neoliberalism or Regulatory Capitalism*. Regulatory Institutions Network, Australian National University, Working Paper, 2005a.

Braithwaite, J. *Meta Regulation of Justice*. Regulatory Institutions Network, Australian National University, Working Paper 2005b.

Braithwaite, J. *Regulatory Capitalism: How It Works, Ideas for Making It Work Better.* Cheltenham: Edward Elgar Publishing, 2008.

Braithwaite, J. "Restorative Justice for Banks through Negative Licensing." *British Journal of Criminology* 49, no. 4 (2009):439–450.

Braithwaite, V. "Games of Engagement: Postures within the Regulatory Community." *Law & Policy* 17, no. 3 (1995):225–255.

Campbell, J. Y., H. E. Jackson, B. C. Madrian, and P. Tufano. "Consumer Financial Protection." *The Journal of Economic Perspectives* 25, no. 1 (2011a):91–113.

Campbell, J. Y., H. E. Jackson, B. C. Madrian, and P. Tufano. "Making Financial Markets Work for Consumers." *Harvard Business Review*, July–August Reprint 11078 (2011b).

Carr, A. Z. "Can an Executive Afford a Conscience." *Harvard Business Review* 48, no. 4 (1970):58–64.

Carr, D. *Educating the Virtues.* London: Routledge, 1991.

Cederman, L.–E., N. B. Weidmann, and K. S. Gleditsch. "Horizontal Inequalities and Ethno-Nationalist Civil War: A Global Comparison." *American Political Science Review* 105 (2011):478–495.

Chesterton, G. K. *Heretics.* New York, NY: John Lane, 1905.

Chesterton, G. K. O*rthodoxy.* New York, NY: John Lane, 1909.

Cohn, A., Fehr, E., & Maréchal, M. A. "Business culture and dishonesty in the banking industry." *Nature 516, no.* 7529 (2014):86–89.

Dahlsgaard, K., C. Peterson, and M. E. P. Seligman. "Shared Virtue: The Convergence of Valued Human Strengths Across Culture and History." *Review of General Psychology* 9, no. 3 (2005): 203–213.

Damodaran, A. "Equity Risk Premiums (ERP): Determinants, Estimation and Implications—A Post-Crisis Update." *Financial Markets, Institutions and Instruments* 18, no. 5 (2009):289–370.

Davis, D. M. "Dealing with Corporate Defaulters: Curbing the Unfettered Exercise of Criminal Law: Enforcement and Regulatory Regime: Part IV." In *Acta Juridica: Modern Company Law for a Competitive South African Economy*, ed. J. Glazewski. Cape Town: Juta's, 2010, pp. 411–432.

de Roover, R. "The Concept of a Just Price: Theory and Economic Policy." *Journal of Economic History* 18, no. 4 (1958):418–434.

Di Mascio, R., A. Lines, and N. Y. Naik. *Trade-Based Performance Measurement: New Tools for Assessing Skill and Active Risk.* Inquire UK Working Paper, 2013.

Dimson, E., P. Marsh, and M. Staunton. *Credit Suisse Global Investment Returns Yearbook.* Credit Suisse Research Institute, 2014.

Doidge, N. *The Brain that Changes Itself: Stories of Personal Triumph from the Frontiers of Brain Science*. New York, NY: Penguin, 2007.

Downey, F. R. "Insurance in Installment Credit Transactions." *Insurance Law Journal* 423 (1958):256–263.

Drucker, P. F. *The Effective Executive*. New York, NY: Harper Collin, 1967.

Drucker, P. F. *Management: Tasks, Responsibilities, Practices.* Mumbai: Allied, 1975.

Drucker, P. F. *The Changing World of the Executive*. New York, NY: Times Books, 1985.

Drucker, P. F. *The Age of Discontinuity: Guidelines to Our Changing Society*. New York, NY: Harper and Rowe, 1992.

Drucker, P. *Adventures of a Bystander*. New Brunswick, NJ: Transaction Publishers, 1996.

Drucker, P. F. *Drucker on Asia: A Dialogue between Peter Drucker and Isao Nakauchi*. London: Routledge, 1997.

Drucker, P. F. *Managing the Non-Profit Organization: Practices and Principles*. London: Routledge, 2012.

Duchesneau, D. A., and W. B. Gartner. "A Profile of New Venture Success and Failure in an Emerging Industry." *Journal of Business Venturing* 5, no. 5 (1990): 297–312.

Earl, J. K., P. Gerrans, A. Asher, and J. Woodside. "Investigating the Influence of Cognitive Decline on the Quality of Financial Decision-Making in Older Adults: The Case of Self-Managed Superannuation Funds." *Australia Journal of Management* (Forthcoming).

Eliot, T. S. *The Rock*. London: Faber, 1934.

Elkington J. *Cannibals with Forks: The Triple Bottom Line of 21st Century Business*. Oxford: Capstone, 1997.

Ericsson, K. A., and N. Charness, "Expert Performance, Its Structure and Acquisition." *American Psychologist* 49 (1994):725–747.

Erikson, E. *The Life Cycle Completed.* New York, NY: Norton, 1982.

Février, P., L. Linnemer, and M. Visser. *Life and Death and Real Estate in France: Testing for Asymmetric Information in the Viager Market*, 2004. http://epee.univ-evry.fr/EPEE/colloques/PhilippeFEVRIER.pdf, 2004.

Flyvbjerg, B. "Five Misunderstandings About Case-Study Research." *Qualitative Inquiry* 12 (2006):219–245.

Frankl, V. E. *Man's Search for Meaning*. New York, NY: Simon and Schuster, 1985.

Franklin, J. *The Science of Conjecture: Evidence and Probability Before Pascal.* London: Taylor and Francis, 2002.

Friedman, M. *Essays in Positive Economics.* Chicago: University of Chicago Press, 1953.

Friedman, M. "The Social Responsibility of Business is to Increase Its Profits." *The New York Times Magazine*, September 13, 1970. http://www.umich.edu/~thecore/doc/Friedman.pdf.

Fowler, J. W. *Stages of Faith: The Psychology of Human Development and the Quest for Meaning.* San Francisco: Harper and Rowe, 1981.

Gentile, M. C. *Giving Voice to Values: How to Speak Your Mind When You Know What's Right*. New Haven, CT: Yale University Press, 2010.

Gilbert, G. "Adam Smith on the Nature and Causes of Poverty." *Review of Social Economy* 55, no. 3 (1997):273–291.

Goodman, J. S., R. E. Wood, and M. Hendrickx. "Feedback Specificity, Exploration, and Learning." *Journal of Applied Psychology* 89, no. 2 (2004):248.

Gouldner, A. W. "Anti-Minotaur: The Myth of a Value-Free Sociology." *Social Problems* 9, no. 3 (1962):199–213.

Graham, J., R. Iyer, and P. Meindl. *The Psychology of Economic Ideology: Emotion, Motivation, and Moral Intuition*. Demos Report, New York, NY, 2013.

Grantham, J. *My Sister's Pension Assets and Agency Problems*, GMO Newsletter, 2012.

Greenleaf, R. K. *Servant Leadership*. New York, NY: Paulist Press, 1977.

Haldane, A. G., and V. Madouros. "The Dog and the Frisbee." *Revista de Economía Institucional* 14, no. 27 (2012):13–56.

Haldane, A. G., and R. M. May. "Systemic Risk in Banking Ecosystems." *Nature* 469, no. 7330 (2011):351–355.

Hall, D T., and D. E. Chandler. "Psychological Success: When the Career is a Calling." *Journal of Organizational Behavior* 26 (2005):155–176.

Hausman, D. M., and M. S. McPherson. *Economic Analysis and Moral Philosophy.* Cambridge: Cambridge University Press, 1996.

Heath, J. "Agency Theory." In *Finance Ethics: Critical Issues in Theory and Practice*, ed. J. R. Boatright. Hoboken, NJ: Wiley, 2010, pp. 125–142.

Herzberg, F. "One More Time: How Do You Motivate Employees?" *Harvard Business Review*46, no. 1 (1968): 53–62.

Hmieleski, K. M., and R. A. Baron. "Entrepreneurs' Optimism and New Venture Performance: A Social Cognitive Perspective." *Academy of Management Journal* 52 (2009):473–488.

Howard, R. A., and C. D. Korver. *Ethics for the Real World: Creating a Personal Code to Guide Decisions in Work and Life*. Boston, MA: Harvard Business Press, 2008.

Igan, D., and P. Mishra. *Three's Company: Wall Street, Capitol Hill, and K Street.* SSRN Working Paper, 2011. http://ssrn.com/abstract=1915164.

International Actuarial Association. *The Principles of Professionalism* (2012). http://www.actuaries.org/ABOUT/Documents/Principles_of_Professsionalism_EN.pdf (accessed November 8, 2014).

Jackall, R. "Moral Mazes: The World of Corporate Managers." *International Journal of Politics, Culture and Society* 1, no. 4 (1988):598–614.

Jensen, M. C., and W. Meckling. "Theory of the Firm: Managerial Behavior, Agency Costs, and Capital Structure." *Journal of Financial Economics* 3 (1976): 305–360.

Jos, P. H., M. E. Tompkins, and S. W. Hays. "In Praise of Difficult People: A Portrait of the Committed Whistleblower." *Public Administration Review* 49, no. 6 (1989):552–561.

Kahneman, D., and G. Klein. "Conditions for Intuitive Expertise: A Failure to Disagree." *American Psychologist* 64 (2009):515–526.

Kahneman, D. *Thinking, Fast and Slow*. London, Macmillan, 2011.

Kay, J. "Should We Have Narrow Banking?" In *The Future of Finance: The LSE Report*, ed. Turner, Adair, A. Haldane, P. Woolley, S. Wadhwani, C. Goodhart, A. Smithers, A. Large et al. London: London School of Economics and Political Science, 2010, pp. 217–234.

Keynes, J. M. *The General Theory of Employment, Interest and Money*. London: Macmillan, 1936.

Kidder, R. M. *How Good People Make Tough Choices*. New York, NY: Morrow, 1995.

Kohlberg, L. *Essays on Moral Development.* New York, NY: Harper Rowe, 1981.

Langevoort, D. C. "Psychological Perspectives on the Fiduciary Business." *Boston University Law Review* 91 (2011):995–1010.

Layard, R. "Happiness and Public Policy: A Challenge to the Profession." *The Economic Journal* 116, no. 510 (2006):C24–C33.

Levi-Faur, D., and J. Jordana. "The Rise of Regulatory Capitalism: The Global Diffusion of a New Order." *The Annals of the American Academy of Political and Social Science* 598, no. 1 (2005):12–32.

Levitt, T. "Marketing Myopia". *Harvard Business Review* 53, no. 5 (1975):26–48.

Lewin, C. G., S. A. Carne, N. F. C. De Rivaz, R. E. G. Hall, K. J. McKelvey, and A. D. Wilkie. "Capital Projects." *British Actuarial Journal* 1, no. 2 (1995): 155–249.

Lewis, C. S. *The Weight of Glory.* Grand Rapids, MI: Wm. B. Eerdmans, 1965.

Lewis, C. S. *The Four Loves*. London: Fount Paperbacks, 1977.

Lohmann, L. "Toward a Different Debate in Environmental Accounting: The Cases of Carbon and Cost-Benefit." *Accounting, Organizations and Society* 34, no. 3 (2009):499–534.

Lovallo, D., and O. Sibony. "The Case for Behavioral Strategy." *McKinsey Quarterly* 2 (2010):30–43.

Lowney, Chris. *Heroic Leadership: Best Practices from a 450-year-old Company that Changed the World*. Chicago: Loyola Press, 2010.Lucas, J. R. *On Justice.* Oxford: Clarendon Press, 1980.

MacIntyre, A. *Three Rival Versions of Moral Enquiry: Encyclopedia, Genealogy and Tradition*. Notre Dame: University of Notre Dame Press, 1990.

MacIntyre, A. *Dependent Rational Animals: Why Human Beings Need the Virtues*. Chicago: Open Court, 1999.

MacIntyre, A. *After Virtue.* Notre Dame: University of Notre Dame Press, 2007.

Marcia, J. E. "Development and Validation of Ego-Identity Status." *Journal of Personality and Social Psychology* 3, no. 5 (1966):551.

Maren, M. *The Road to Hell*. New York, NY: Simon and Schuster, 2009.

Manove, M., A. J. Padilla, and M. Pagano. "Collateral versus Project Screening: A Model of Lazy Banks." *Rand Journal of Economics* 32, no. 4 (2001):726–744.

McGrath, R. E. "Scale-and Item-Level Factor Analyses of the VIA Inventory of Strengths." *Assessment* 21, no. 1 (2014):4–14.

McGrath, R. E. "Character Strengths in 75 Nations: An Update." *The Journal of Positive Psychology* ahead-of-print (2014):1–11.

McLean, G. R. "The Imagination of Our Hearts." St Mark's Review 221 (2012):1–13.

McLeay, M., A. Radia, and R. Thomas. "Money Creation in the Modern Economy." *Quarterly Bulletin* 54, no. 1 (2014):14–27.

Minsky, H. P., and Henry Kaufman. *Stabilizing an Unstable Economy*. Vol. 1. New York, NY: McGraw-Hill, 2008.

Mischel, W. *The Marshmallow Test*. New York, NY: Little, Brown, 2014.

Moore, G. "Re-imagining the Morality of Management: A Modern Virtue Ethics Approach." In *The Heart of the Good Institution*, ed. Harris, Wijesinghe and McKenzie. The Netherlands: Springer, 2013, pp. 7–34.

Noble, J. H. "Policy Reform Dilemmas in Promoting Employment of Persons with Severe Mental Illnesses." *Psychiatric Services* 49 (1998):775–781.

Novaes, W. "Capital Structure Choice When Managers Are in Control: Entrenchment Versus Efficiency." *The Journal of Business* 76, no. 1 (2003):49–82.

Oakes, G. *The Soul of the Salesman: The Moral Ethos of Personal Sales*. London: Humanities Press International, 1990.

Olson, M. *The Logic of Collective Action: Public Goods and the Theory of Group*. Cambridge, MA: Harvard University Press, 1965.

O'Neill, D., R. Dietz, and N. Jones. *Enough is Enough. Ideas for a Sustainable Economy in a World of Finite Resources. The Report of the Steady State Economy Conference*. Center for the Advancement of the Steady State Economy (Arlington, Virginia, USA) and Economic Justice for All (Leeds, UK), 2010.

Ostrom, E. *Governing the Commons: The Evolution of Institutions for Collective Action.* Cambridge: Cambridge University Press, 1990.

Ostrom, V. *The Meaning of Democracy and the Vulnerability of Democracies: A Response to Tocqueville's Challenge*. Ann Arbor: University of Michigan Press, 1997.

Owen, N. *HIH Royal Commission, The Failure of HIH Insurance*. Australian Government Canberra, 2003.

Palmisano, S. "Managing Investors." *Harvard Business Review* 92, no. 6 (2014): 80–85.

Pearce, J. *Wisdom and Innocence: A Life of G.K. Chesterton*. San Francisco: Ignatius Press, 1997.

Perry, J. *The Art of Procrastination: A Guide to Effective Dawdling, Lollygagging and Postponing*. New York, NY: Workman Publishing, 2012.

Perry, W. G. "Cognitive and Ethical Growth: The Making of Meaning." *The Modern American College*, ed. A. W. Chickering. San Francisco: Jossey–Bass, 1981, pp. 76–116.

Philippon, T. *Has the US Finance Industry Become Less Efficient? On the Theory and Measurement of Financial Intermediation*. Working Paper No. w18077. National Bureau of Economic Research, 2012.

Polanyi, M. *Personal Knowledge: Towards a Post-Critical Philosophy*. London: Routledge, 1958.

Power, M. "The Invention of Operational Risk." *Review of International Political Economy* 12, no. 4 (2005):577–599.

Power, M., S. Ashby, and T. Palermo. *Risk Culture in Financial Institutions: A Research Report*. Economic and Social Research Council, United Kingdom, 2013. http://www.lse.ac.uk/researchandexpertise/units/carr/pdf/final-risk-culture-report.pdf (accessed December 12, 2014).

Prendergast, C. "The Provision of Incentives in Firms." *Journal of Economic Literature* 37, no. 1 (1999):7–63.

Rawls, J. *A Theory of Justice.* Cambridge, MA: Belkup, 1971.

Redington, F. M. "The Flock and the Sheep." *Journal of the Institute of Actuaries* 108, no.3. (1981): 361–404.

Roszak, T. *Where the Wasteland Ends: Politics and Transcendence in Post–industrial Society*. New York, NY: Doubleday, 1972.

Ruggles, S. "Reconsidering the Northwest European Family System: Living Arrangements of the Aged in Comparative Historical Perspective." *Population and Development Review* 35, (2009):249–273.

Samuelson, P. A. "Discussion." *The American Economic Review* 53, no. 2 (1963):231–236.

Samuelson, P. A. *Economics* (Eighth Edition). New York, NY: McGraw Hill, 1970.

Sandel, M. J. *Justice: What's the Right Thing to Do?* New York, NY*:* Farrar, Straus and Giroux, 2010.

Sen, A. *The Idea of Justice.* Cambridge, MA: Belknap, 2009.

Shiller, R. J. *The New Financial Order: Risk in the 21st Century*. Princeton, NJ: Princeton University Press, 2009.

Shu, L. L., F. Gino, and M. H. Bazerman. *Dishonest Deed, Clear Conscience: Self-Preservation through Moral Disengagement and Motivated Forgetting*. Working Paper, Harvard Business School, 2009.

Simon, H. A. "Rational Decision Making in Organizations." *American Economic Review* 69, no. 4 (1979):493–513.

Schich, S., and B-H Kim. "Developments in the Value of Implicit Guarantees for Bank Debt: The Role of Resolution Regimes and Practices." *OECD Journal: Financial Market Trends* 2012, no. 2 (2012):35–65.

Sinclair, H. *Confessions of a Microfinance Heretic: How Microlending Lost Its Way and Betrayed the Poor*. San Francisco: Berrett-Koehler Publishers, 2012.

Smith, A. *An Inquiry into the Nature and Causes of the Wealth of Nations.* Hazleton, PA: Pennsylvania State University, 2005.

Swann, G. M. P. *Putting Econometrics in Its Place: A New Direction in Applied Economics*. Cheltenham: Edward Elgar Publishing, 2006.

Taylor Committee. *Transforming the Present—Protecting the Future Report of the Committee of Inquiry into a Comprehensive Social Security System for South Africa*. Taylor Commission Report RP/53/2002, Department of Social Development, Pretoria, 2002.

Thomson, R. J. "The Use of Utility Functions for Investment Channel Choice in Defined Contribution Retirement Funds 1: Defence." *British Actuarial Journal* 9 (2003):653–710.

Thomson, R., and D. Posel, "The Management of Risk by Burial Societies in South Africa." *South African Actuarial Journal* 2, no. 1 (2002):83–127.

Turner, A. "Mansion House Speech." *The City Banquet, the Mansion House, London, September* 22 (2009). http://www.fsa.gov.uk/pages/Library/Communication/Speeches/2009/0922_at.shtml (accessed April 7, 2015)

Turner, J. *Rating Retirement Advice: A Critical Assessment of Retirement Planning Software*. Pension Research Council Working Paper No. 2010–03 (April 9, 2010). http://ssrn.com/abstract=1706204.(accessed December 11, 2014).

Tyler, T. R., and H. J. Smith. "Social Justice and Social Movements." In *Handbook of Social Psychology*, ed. D. Gilbert, S. T. Fiske, and G. Lindzey, Vol. 4. Boston: McGraw–Hill, 1998, pp. 595–629.

Ucbasaran, D., P. Westhead, M. Wright, and M. Flores. "The Nature of Entrepreneurial Experience, Business Failure and Comparative Optimism." *Journal of Business Venturing* 25, no. 6 (2010):541–555.

Uslaner, E. M. *The Moral Foundations of Trust.* Cambridge: Cambridge University Press, 2002.

van Hooft, S. *The Handbook of Virtue Ethics*. Durham: Acumen Publishing, 2014.

Verba, S., and G. R. Orren. "The Meaning of Equality in America." *Political Science Quarterly* 100, no. 3 (1985):369–387.

Vitali, S., J. B. Glattfelder, and S. Battiston. "The Network of Global Corporate Control." *PloS one* 6, no. 10 (2011):e25995.

Waring, M. B. *Pension Finance: Putting the Risks and Costs of Defined Benefit Plans Back Under Your Control*. New York, NY: Wiley Finance, 2012.

Wilkie, A. D. "The Risk Premium on Ordinary Shares." *British Actuarial Journal* 1, no. 2 (1995):251–293.

Wilkinson, R. *The Impact of Inequality—How to Make Sick Societies Healthier.* The New Press, 2005.

Winter, J. "Corporate Governance Going Astray: Executive Remuneration Built to Fail." In *Festschrift for Professor Klaus Hopt*, ed. W. de Gruyter, 2010 pp. 1521–1535. Available at SSRN: http://ssrn.com/abstract=1792483.

Wolterstorff, N. *Justice: Rights and Wrongs*. Princeton, NJ: Princeton University Press, 2010.

Yoder, J. H. *The Politics of Jesus: Vicit Agnus Noster*. Grand Rapids, MI: Wm. B. Eerdmans Publishing, 1990.

Yu, J. *The Ethics of Confucius and Aristotle: Mirrors of Virtue.* London: Routledge, 2013.

Zenger, J. H., and J. R. Folkman. The *Extraordinary Leader*. New Delhi: Tata McGraw-Hill Education, 2009.

Index

GIVING VOICE TO VALUES ON BUSINESS ETHICS AND CORPORATE SOCIAL RESPONSIBILITY COLLECTION

Mary Gentile, Editor

The Giving Voice To Values initiative teamed up with Business Expert Press to produce a collection of books on Business Ethics and Corporate Social Responsibility that will bring a practical, solutions-oriented, skill-building approach to the salient questions of values-driven leadership. Giving Voice To Values (GVV: www.GivingVoiceToValues.org)—the curriculum, the pedagogy and the research upon which it is based—was designed to transform the foundational assumptions upon which the teaching of business ethics is based, and importantly, to equip future business leaders to not only know what is right, but how to make it happen.

- *Ethical Leadership in Sport: What's Your ENDgame?* by Pippa Grange
- *The ART of Responsible Communication: Leading With Values Every Day* by David L. Remund
- *Engaging Millennials for Ethical Leadership: What Works for Young Professionals and Their Managers* by Jessica McManus Warnell

FORTHCOMING TITLES IN THIS COLLECTION

- *Social Media Ethics Made Easy* by Joseph W. Barnes
- *Business Ethics: A Moral Reasoning Framework* by Annabel Beerel
- *Leadership Ethics: Moral Power for Business Leaders* by Lindsay Thompson
- *Sales Ethics: How To Sell Effectively While Doing the Right Thing* by Alberto Aleo and Alice Alessandri

THE BUSINESS EXPERT PRESS DIGITAL LIBRARIES

EBOOKS FOR BUSINESS STUDENTS

Curriculum-oriented, born-digital books for advanced business students, written by academic thought leaders who translate real-world business experience into course readings and reference materials for students expecting to tackle management and leadership challenges during their professional careers.

POLICIES BUILT BY LIBRARIANS

- *Unlimited simultaneous usage*
- *Unrestricted downloading and printing*
- *Perpetual access for a one-time fee*
- *No platform or maintenance fees*
- *Free MARC records*
- *No license to execute*

The Digital Libraries are a comprehensive, cost-effective way to deliver practical treatments of important business issues to every student and faculty member.

Working Ethically in Finance
Clarifying Our Vocation

Anthony Asher

"*… a must read for those wanting to craft a vocation in finance.*"
Adrian Gore, CEO, Discovery Group

"*… no better book for a student or practitioner who wants more than is usually on offer in finance courses in our universities.*"
Paul Oslington, Professor of Economics and Dean of Business, Alphacrucis College, Sydney

To develop a vocation we ask: what do I want to be remembered for? This involves aspiring to personal integrity and a life well lived.

Those working in the financial sector fulfill vocations by finding ways to serve social purposes, to allocate resources efficiently and to provide financial security—while remembering the needy. This means contributing to institutions, where people can flourish personally and create appropriate products and services. The ethics of those working on finding their vocation do not flow from rules and obligations, but from a personal commitment to seeking what is good. This life is based on the fundamental personal virtue, integrity.

This book is written for those who aspire to the cultivation of the personal virtues of wisdom, self-control, courage, and justice.

Anthony Asher has divided his working life between practice and academia. His early work culminated in four years as chief actuary of a medium sized life insurer in South Africa. He was subsequently director of actuarial studies at the University of Witwatersrand, and is now associate professor at the University of New South Wales. He has served a variety of other financial service organizations as consultant and director, and is an active contributor to professional activities in Australia since 2003. His service to the profession was recognized by the Murray Medal, the highest award for service given by the Actuarial Society of South Africa (ASSA), in 2002.

Giving Voice To Values on Business Ethics and Corporate Social Responsibility Collection

Mary Gentile, *Editor*

BUSINESS EXPERT PRESS

ISBN 978-1-60649-874-3
90000
9 781606 498743