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The Secretary,  
Financial System Inquiry  
Treasury Building  
Parkes Place  
Parkes ACT 2600

September 6th, 1996

Dear Sir

**Anticipatory Self-Regulation:  
for consumer protection and competitiveness**

To further the mission of the Inquiry the government needs to establish an institutional framework which will anticipate the rapid de-regulation of the financial system being created from the introduction of new technology. A new regulatory regime is urgently required to ensure that entities operating in the financial system have inbuilt self-regulatory and fail-safe features to protect consumers, themselves and the system.

Technology of the "information age" is introducing substantial changes in both the nature of financial products and institutions as described in my articles included in the Appendix. Direct regulation of either financial products and/or institutions will become more ineffectual as technology introduces greater complexity in both. Attempts to increase direct regulation to counter technological de-regulation is likely to inhibit progress, competitiveness and introduce unintended consequences which could be counter productive to the mission of the Inquiry.

Complexity cannot be adequately monitored or controlled by one or more centralised "Super Regulator(s)". It can only be monitored and controlled with matching complexity from self-regulation. The phasing in of self-regulation would reduce the role and cost of existing regulators while improving consumer protection, competitiveness and the other objectives of the Inquiry's mission. However, some form of central specialised government authority will still be required to set in place the principles of self-regulation with the power to withhold the right for any business entity to operate if it does not implement prescribed self-governing principles to protect the public interest. The Reserve Bank of Australia has already initiated this approach in mandating standards of corporate governance for licensed banks. However, the specific details of their initiative is not likely to be effective for the reasons indicated below and developed more comprehensively in my paper 'What is World Best Practice in Corporate Governance?', as listed below.

The principles of self-regulation need to be embedded into the constitutions of the entities operating in the financial system in the same way DNA imprints into all living things the manner in which they develop and become self-governing. In this way, Australia could put into practice the strategy of the US Vice President, Albert Gore, who saw the role of government as "imprinting the DNA" of social structures<sup>1</sup>. This strategy would introduce "anticipatory self-regulation" by

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<sup>1</sup> Gore, Albert, 1996, 'The Technology Challenge: What is the Role of Science in American Society?' prepared remarks for the American Association for the Advancement of Science, Baltimore, MD, February 12, and also 'The Technology Challenge: Building a Government for the Information Age', remarks at The Armed Forces communications and Electronics Association Conference, Tyson's Corner, VA, February 13.

"imprinting" self-governing attributes into the constitutions of banks, building societies, cooperatives, mutual associations, unit trusts, corporations and any other institutions required to mediate self-regulation of the financial system.

At present, all incorporated and unincorporated institutions are allowed to exist in a form which denies self-regulation. This allows financial collapses and ensures failure in any attempts to introduce elements of self-regulation. As a result, politicians, bureaucrats, the general public, political and other social scientists can rightly claim that self-regulation does not and cannot work (with existing institutional structures). To introduce self-regulation, existing institutional structures need to be reformed to adopt the self-governing principles found in nature.

An understanding of self-governing principles has only been recognised by pure and applied scientists during the last fifty years. Self-regulating machinery and devices are now common place in the household, factory and they make space travel possible. Automatic pilots can now replace humans. Even trains and semi-trailers are not allowed to operate unless they have fail-safe features such as airbrakes. However, we allow financial institutions to exist without any self-regulating features and allow the government and/or the public to bear the cost of institutions not having fail-safe features. In addition, de-regulation is introduced without requiring non-market mechanisms of self-regulation.

Some principles of self-regulation are not difficult to comprehend. For example, it is only common sense that those affected by an institution or product should obtain some power to influence the institution and/or its products other than the negative power of withholding their custom in the market place. Power sharing needs to be built into the constitutions of entities operating in the financial system. The feedback provided by customers and/or their delegates or proxies, can also provide competitive advantages for the entities involved.

However, self-regulation cannot reliably work when feedback, which reflects adversely on management, is subject to the power of management. Division of power is essential for self-regulation because power corrupts and absolute power corrupts absolutely. Self-regulation cannot work with organisations who have constitutions based on centralised power as is currently the general case. The almost universal lack of division of power in current financial institutions explains why attempts to introduce elements of self-regulation are highly likely to fail. It also explains why the currently accepted guide-lines on good corporate governance as used by the Reserve Bank cannot provide reliable safeguards for the public interest.

The self-regulating principles which need to be prescribed for financial institutions are well understood by scientists and engineers who design and build self-governing machinery and devices. This knowledge cannot be ignored by the committee in reporting on either "deregulation" as required in point 1 of the Terms of Reference or "regulatory arrangements" and "regulation" as mentioned in points 3 and 4 of the Terms of Reference. Nor should the theory and practice of designing and operating "systems" be ignored in any views formed by the Inquiry on recommending any changes in the design and operation of the financial system.

I am currently researching for a dissertation on corporate governance, the application of system engineering principles to social institutions to improve their operations. I would be pleased to share further details of my research in this specialised field as may be desired. I have written a number of articles on this topic and on the future of money and banking relevant to the inquiry as listed below.

Articles listed in the Appendix as AFR 1, 2 & 3 and WCN 1, 2 & 7, outline how advances in technology are likely to force substantial de-regulation of the

financial system. These articles also describe the potential benefits of such de-regulation. They include: reducing the cost of finance through competing currencies and the introduction of negative interest rate money; controlling inflation; improving the allocation of national resources between regions; reducing foreign and government borrowing; eliminating the ability of the government to hide how it appropriates private sector foreign exchange earnings and generally make government finances transparent. The article on 'Re-inventing Central Banking' (WCN 7) supports the proposals of Nobel Prize winning economist Professor F. A. Hayek to privatise money and so introduce market self-regulation through competing currencies<sup>2</sup>.

However, as noted in WCN 7 and 'Elements of Autonomous Banking' in *Building Sustainable Communities*, non-market safeguards will also be required. It is not too late to start getting these established and tested in anticipation of technology introducing radical de-regulation of the financial system. The current approach based on direct intervention by government agencies is unlikely to be effective and could be counter productive. As pointed out by the US Vice President, the idea of the government having "policy levers" and "pump priming" to regulate the economy reflects the language, metaphors and thinking of the industrial rather than the information age.

We now need to adopt the language, metaphors and thinking of the information age to "imprint the DNA" of social institutions to ensure that they are self-regulating. Examples already exist as described in the paper I am presenting to the 25th Conference of Economists later this month. A lay-persons guide to this paper and my other academic papers on self-governance will be found in WCN 3,4,5 & 6 accessible from the web site at:- <http://www.worldcitizen.org> or from myself. I would be pleased to provide further information as may be required on developing "anticipatory self-regulation" of the financial system.

Yours faithfully

Shann Turnbull  
Principal

Attachments:

- . APPENDIX containing six published articles on the future of money and banking (In the attached diskette these articles are in their un-edited form as submitted for publication)
  - . 3.5 inch Macintosh formatted diskette using Microsoft Word version 4.0.
- References: (WCN articles accessible through web page <http://www.worldcitizen.org>)

**Articles on the future of money and banking reproduced in the Appendix:**

WCN 1, 'The Coming Monetary Meltdown- Take Shelter by Starting Local Currencies', *World Citizens News*, Washington,D.C., 9:3, pp. 10 &14, Jun/July, 1995.

AFR 1, 'Banks May be Our Next Dinosaurs', *The Australian Financial Review*, comment with front page notice, p.36, July 3, Sydney, 1995.

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<sup>2</sup> Hayek, F. A. 1976, 'Choice in Currency: A Way to Stop Inflation', *Occasional Paper 48*, and 'Denationalization of Money: An Analysis of the Theory and Practice of Concurrent Currencies', *Hobart Paper Special 70*, The Institute of Economic Affairs, London.

WCN 2, 'Banking's (And Money's) Digital Future', *World Citizens News*, Washington,D.C., 9:45 pp. 11 &16, Oct./Nov., 1995.

AFR 2, 'Digital cash isn't funny money', *The Australian Financial Review*, op. ed. Opinion, p.13, April 1st., Sydney, 1996.

AFR 3, 'Let's widen the inquiry', *Australian Financial Review*, op. ed. Opinion, July 8, p. 17, Sydney, 1996.

WCN 7, 'Re-inventing Central Banking', *World Citizens News*, Washington, D.C., 10:4, pp. 15-16, August/September, 1996.

### **Articles on the theory and practice of self-governance (not included in the Appendix):**

'Beyond Markets & Hierarchies: Extending the theory of the firm', 23rd. Conference of Economists, Gold Coast International Hotel, September 28, 1994.

'What is World Best Practice in corporate governance?', Corporate Governance Conference, IBC Conferences P/L, The Boulevard Hotel, Sydney, March 6th, 1995.

'Stakeholder Democracy: Redesigning the Governance of Firms and Bureaucracies', *Journal of Socio-Economics*, JAI Press, 23:3, Fall, pp. 321-360, Connecticut, 1994.

'Powerful arguments against unitary boards', *The Australian*, Business Analysis, pp. 72, Tuesday, August 29, Sydney, 1995.

'Corporate Governance: What is World Best Practice', *Australian Company Secretary*, Chartered Institute of Company Secretaries in Australia Limited, pp 495-491, December, Sydney, 1995.

WCN 3, 'Governance Options: Beyond Markets and Hierarchies', *World Citizens News*, Washington,D.C., 9:6 pp. 10, 11 &16, Dec./Jan., 1996.

WCN 4, 'Markets and Hierarchies: A Curse of Modernity', *World Citizens News*, Washington,D.C., 10:1, pp. 7 &12, Feb./Mar., 1996.

WCN 5, 'Centralization and Self-Governance: How to Get from Here to There', *World Citizens News*, Washington,D.C., 10:2, pp. 15 & 20, April/May, 1996.

WCN 6, 'Self-Governance and World Governance: Necessary Partners', *World Citizens News*, Washington,D.C., 10:3, pp. 14-16, June/July, 1996.

'Corporate Self-regulation', *Board Report*, Corporate Directors' Association, 1:6, p.5, July, Sydney, 1996.

'Stakeholder Governance: A cybernetic and property rights analysis', 25th Conference of Economists, Australian National University, September 24, 1996.

*Building Sustainable Communities*, (revised 1996) Benello, Swann & Turnbull, ed: Ward Morehouse, The Bootstrap Press, 777 United Nations Plaza, #3C, NY, 10017, e-mail: cipny@igc.apc.org