

Crisis and Punishment? Explaining Politicians' Appetite for Retribution in Post-Crisis Europe

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ABSTRACT¹

This paper investigates the politics of holding bank executives accountable for banking crises. The aftermath of the 2008 global financial crisis was characterized by a significant variation in the extent to which European countries endorsed this type of retributive justice. In particular, while some countries established special prosecutorial bodies and took steps to facilitate prosecutions, others seemed to consider the crisis “business as usual” and relied on the existing investigative and prosecutorial mechanisms to seek out wrongdoing. We explore the experiences of two European countries, Iceland and Cyprus. We argue that the way a financial crisis unfolds plays a significant role in shaping the appetite of politicians for promoting an agenda of retributive justice. With a banking *collapse*, politicians will be most proactive, as voters’ demand for justice is high and the risks for the banking industry are minimal. With a severe yet *negotiated* crisis following a bailout/bail-in, politicians are more reluctant to endorse policies that may risk the recovery of the fragile banking sector.

Keywords: Prosecutions; Great Recession, White-Collar Crimes, Accountability

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1. Introduction

More than a decade after the 2008 global financial crisis, the conventional wisdom is that impunity prevailed. In the US no high level bank executives were prosecuted, while in most European countries affected by the crisis such as Ireland or Spain there were only a handful of prosecutions. In short, bank executives were off the hook for the bank failures that damaged the global economy and affected millions of people. The former Prime Minister of the UK, Gordon Brown, lamented the lack of prosecution, stating, “If bankers who act fraudulently are not put in jail with their bonuses returned, assets confiscated and banned from future practice, we will only give a green light to similar risk-laden behaviour in new forms”.² While various researchers have sought to shed light on the extent to which bank executives have been held accountable, most explanations have pointed a finger at the actions and omissions of prosecutors and noted the special status of banks and their executives.³

This paper takes a different perspective and focuses on the *politics* of holding bank executives accountable after a financial crisis. While politicians are not directly involved in prosecuting criminal behavior associated with the onset of the financial crisis, they have access to a number of policy tools that facilitate or hinder the prospect of prosecution, such as creating special prosecutorial authorities tasked with investigating the possibility of criminal behavior behind the bank failures or passing legislative provisions to support investigations into potential criminal offenses. However, the extent to which they deployed these policy tools in the aftermath of the 2008 Great Recession varied significantly across

² Larry Elliott (2017) “Gordon Brown: Bankers Should Have Been Jailed For Role In Financial Crisis”, The Guardian, 31 October 2017, Also Available At: <https://www.theguardian.com/politics/2017/oct/31/gordon-brown-bankers-should-have-been-jailed-for-role-in-financial-crisis> [last accessed: 15 April 2019]

³ Brandon Garrett. *Too Big To Jail*. (Cambridge: Harvard University Press, 2014); Jesse Eisinger. *The Chickenshit Club: Why The Justice Department Fails To Prosecute Executives*. (New York:Simon And Schuster, 2017).

countries. For example, in Iceland, politicians established a truth commission which was instrumental in shedding light on the patterns of misconduct in the financial industry and also created a special prosecutorial authority to bring charges for white-collar crimes committed in the run up to the crisis. Yet in other countries, politicians followed a “business as usual” model and relied on conventional mechanisms to investigate offenses and bring charges against bank executives. For instance, in Cyprus, politicians set up independent commissions of inquiry to document the causes of the crisis, but left the task of investigating financial crimes to the existing judicial authorities, despite their limited expertise in white-collar crime investigations. Not surprisingly, this curbed the effectiveness of post-crisis criminal investigations.

What explains this variation in the degree of political support for retributive⁴ justice in the aftermath of a financial crisis? In our attempt to answer, we focus not on the extent to which illegal behavior plays a role in the origins of the crisis but rather on the way a crisis unfolds. In particular, we show how the impact of a crisis on the banking sector plays a significant role in whetting politicians’ appetite for retributive justice. To be specific, when a crisis leaves the existing banking institutions fragile but operational (e.g. after a bailout), policymakers are constrained in their capacity to respond to voters’ demands for a proactive agenda of accountability, as protracted inquiries or criminal investigations may negatively impact public and market confidence in these same institutions. However, following a total collapse, policy initiatives seeking information on responsibility are less likely to have an

⁴ The term “Retributive Justice” refers to the “Repair of justice through unilateral imposition of punishment”. We use the terms “Retributive Justice” And “Accountability” interchangeably to refer to punitive measures against bank executives. Wenzel, Michael, Tyler G. Okimoto, Norman T. Feather, And Michael J. Platow. "Retributive and Restorative Justice." *Law and Human Behavior* 32 (October 2008): 375.

impact on surviving banks or new banks, creating a policy space for politicians to be more responsive to voters' demands for accountability.

The paper is structured as follows. Section 2 reviews the literature on the determinants of bank executives' prosecutions post-2008 and explores how steps taken by elected officials can facilitate (or impede) the criminal investigations of the national prosecutorial authorities. Section 3 presents our argument on the relationship between the nature of the crisis and the extent to which policymakers will pursue a policy of accountability. The research design is described in section 4, where we also justify the selection of Iceland and Cyprus as our case studies. Section 5 tests our argument by exploring the variations in policy responses to post-crisis accountability in these two countries. Section 6 discusses alternative explanations and notes their inability to offer a more convincing explanation of the puzzle. The paper concludes by discussing the implications of the analysis and suggesting avenues for further research.

2. Holding bank executives accountable after economic crises

2.1 Limits of prosecutors and the powerful status of bank executives

Unsurprisingly, debates on accountability have taken center stage of academic literature in the aftermath of the 2008 global financial crisis.⁵ In particular debates related to the responsibility of bank executives that surfaced in media reports and academic literature remained highly controversial. While some of the main causes of the crisis had no fraudulent or illegal character, scholars pointed out how some financial practices should raise concerns

⁵ For a broader theoretical discussion of post-crisis accountability see Nadia Hilliard, Iosif Kovras, And Neophytos Loizides. "The Perils of Accountability After Crisis: Ambiguity, Policy Legacies, And Value Trade-Offs." *Cambridge Review of International Affairs* (January 2020): 1-20; Dawson, Mark. "The Legal and Political Accountability Structure Of 'Post-Crisis' EU Economic Governance." *JCMS: Journal of Common Market Studies* 53 (September 2015): 976-993.

about the responsibility of individual bank executives and suggested the need for prosecution. For instance, the Financial Crisis Inquiry Commission created by the US Congress to investigate the origins of the crisis mentions variants of the word “fraud” 157 times in its report,⁶ highlighting how the selling of mortgages to borrowers who lacked the capacity to repay, the selling of obscurely structured finance products to investors, or the misvaluation of these products were not honest mistakes. In the words of Jed Rakoff, Judge of the United States District Court for the Southern District of New York, “the crisis was in material respects the product of intentional fraud.”⁷ However, for the most part, bank executives were not prosecuted post-2008, both in major economies and in more peripheral European economies. For example, US and British authorities did not bring charges against high level executives for charges related to the crisis for almost a decade. Similarly, authorities in Ireland and Spain have been unsuccessful, as they have prosecuted only a handful of bankers (allegedly) involved in crisis-related white-collar crimes, resulting only in few convictions. As the head of the IMF, Christine Lagarde, acknowledged, “Despite evidence of actual malfeasance in several cases, it has been mostly corporate balance sheets that have borne the brunt of legal sanctions for reckless behaviour -- not individuals”.⁸ What explains this outcome? Scholars tackling this question have focused on two clusters of explanations.

The first set of explanations emphasizes the *role of prosecutorial authorities* and the challenges they face when establishing the criminal culpability of bank executives in a court of law. The very nature of financial crimes raises intrinsic obstacles to obtaining the

⁶ Jed Rakoff "The Financial Crisis: Why Have No High-Level Executives Been Prosecuted?." *The New York Review of Books* 9 (2014):2

⁷ Ibid, 3.

⁸ Christine Lagarde, "The Role Of Personal Accountability In Reforming Culture And Behavior In The Financial Services Industry." *Speech at The New York Fed* 5 (November 5, 2015).

information required to prove culpability. An effective investigation will often involve gaining access to a vast number of documents, tracing millions of transactions, and securing testimonies, to name only a few. Not only are these pieces of evidence generally inaccessible to public scrutiny, but the technical complexity of modern finance requires prosecutorial authorities to have significant resources and specialized expertise.⁹ Moreover, beyond securing access to evidence linking individuals to actions, substantiating corporate crimes necessitates proving beyond a reasonable doubt the “intent” to commit a fraud, manipulate the market, or commit other corporate crimes.¹⁰ The complexity of prosecuting financial crimes, coupled with previous experience (or lack thereof) in investigating these crimes, shapes the likelihood of prosecutors bringing charges against executives, opting for a settlement, or targeting the corporation.¹¹

The second cluster of explanations centers on *the powerful status of the offenders*.¹² The criminology literature suggests that, unlike street criminals, corporate criminals have economic and political clout, thus inhibiting white-collar prosecutions and/or leading to more lenient sentencing.¹³ Powerful corporations – particularly in the US - cultivate a tight network of contacts with state prosecutorial authorities, as evident by the common movement of state prosecutors to work as corporate lawyers; this implicit “revolving door” minimizes state authorities’ determination to bring criminal charges against corporations or

⁹ Samuel Buell, *Capital Offenses: Business Crime and Punishment In America's Corporate Age*. (New York: WW Norton & Company, 2016).

¹⁰ Peter J. Henning "Testing The Limits Of Investigating And Prosecuting White Collar Crime: How Far Will The Courts Allow Prosecutors To Go." *U. Pitt. L. Rev.* 54 (December, 1992):450; Buell, 208.

¹¹ Brandon Garrett, *Too Big To Jail*. (Cambridge: Harvard University Press, 2014); Eisinger, 2017.

¹² Gregg Barak. *Theft of A Nation: Wall Street Looting and Federal Regulatory Colluding* (Lahman: Rowman & Littlefield Publishers, 2012); Henry Pontell, William K. Black, And Gilbert Geis. "Too Big to Fail, Too Powerful to Jail? On the Absence Of Criminal Prosecutions After The 2008 Financial Meltdown." *Crime, Law and Social Change* 61 (August, 2014): 1-13; Henning, 1992

¹³ Michael Benson and Esteban Walker. "Sentencing The White-Collar Offender." *American Sociological Review* 53 (April, 1988): 294-302

banks.¹⁴ Moreover, prosecutors may be reluctant to bring charges against banks and bank executives, fearing a possible adverse impact on economic recovery. These people are simply “too big to jail”.¹⁵ Otherwise stated, the powerful status of banks creates an obstacle to the capacity of authorities to investigate bankers.

While the constraints reviewed above certainly have a cooling effect on the desire to prosecute bank executives, these *alone* provide only a partial picture of the determinants of retributive justice in the aftermath of banking crises. The constraints on the capacity of prosecutorial initiative identified by the literature are not fixed; instead, they are partly shaped by the institutional framework within which prosecutorial authorities operate. The financial resources available to prosecutors, the existing laws determining what counts as illegal behavior and how evidence can be gathered, and the mandate and priorities of prosecutorial authorities are all subject to change. To explain these factors, we need to go beyond a focus on prosecutorial authorities and their interaction with banking executives to consider a third set of actors: politicians.

2.2 How politicians influence the prospects of prosecutions after a crisis

While politicians in western democracies cannot interfere with the operation of the national judiciary to initiate prosecutions after a financial crisis, they can shape the prospect of prosecutions. In using the term ‘politicians’ we mostly refer to the incumbent/party in power that possess the capacity and power to shape policies, while at the same time their decision making is shaped by electoral pressures. While other officials may yield significant power to shape policies in times of crisis, such as central bank governors or regulators, they

¹⁴ Barak, 2012

¹⁵ Garrett 2014; Rakoff 2014

are not subject to electoral pressures. Similarly, other representatives of the political elite, such as the opposition officials they may engage in cheap talk without having the institutional power to shape decision-making. From this vantage point, politicians have a number of tools at their disposal to facilitate (or thwart) the capacity of prosecutorial authorities to carry out effective investigations and bring charges or to indirectly influence their priorities.

First, incumbents can influence the likelihood of prosecutions by *exercising their power over the purse strings*. As discussed above, the complexity of financial activities makes evidence gathering a highly resource-intensive process. By granting (or denying) prosecutorial authorities the additional financial support required to acquire technical expertise and dedicated forensic technologies to access incriminatory evidence, the incumbent shapes prosecutors' capacity to investigate crime. When politicians provide little support, it becomes extremely difficult for judicial authorities to launch an effective criminal probe. This is particularly relevant in times of crisis when the judiciary itself may not be immune from policies of austerity and budget cuts. Operating with scarce resources makes it impossible for prosecutors to investigate all cases; they will inevitably have to be selective. The literature identifies the "likelihood of success" as the most important factor in decisions to prosecute particular sets of cases over other ones,¹⁶ with the existing caseload and the availability of resources and expertise playing a crucial role.¹⁷

Second, politicians can facilitate prosecutions by *amending the existing legal framework*. The burden of proof in white-collar crimes is usually challenging, as prosecutors have to

¹⁶ Martha Myers and John Hagan. "Private and Public Trouble: Prosecutors and The Allocation Of Court Resources." *Social Problems* 26 (April, 1979):439

¹⁷ Joan Gurney. "Factors Influencing the Decision to Prosecute Economic Crime." *Criminology* 23 (November, 1985):613; Michael Benson, L., William J. Maakestad, Francis T. Cullen, And Gilbert Geis. "District Attorneys and Corporate Crime: Surveying the Prosecutorial Gatekeepers." *Criminology* 26, (August, 1988):512.

show defendants “intended” to commit fraud or manipulate the market. This is a major obstacle; prosecutors may refrain from taking on cases of white-collar crimes with limited prospects of conviction. Although retroactive change in the legal framework to make certain actions illegal is not feasible, politicians can facilitate criminal investigations in other ways. For example, a political decision to assist prosecutorial authorities by simplifying the procedure of confiscating data from banks and individual executives could be a significant boost.

Third, the government may *set up special ad hoc prosecutorial bodies* mandated to carry out a criminal probe on actions in the run up to a crisis, thereby framing the crisis as an extraordinary event in need of special investigation. For instance, after the failure of many savings and loan institutions in the US in the late 1980s, various task forces were created by US authorities, resulting in 1,100 cases being referred to prosecutors.¹⁸ Along the same lines, during the recent Global Recession, the US government created the Financial Fraud Enforcement Task Force; this one was not as successful as its predecessor and was criticized as a “sideshow” for not prosecuting executives who bore responsibility for the 2008 financial crisis.¹⁹ The creation of special prosecutorial mechanisms is more often the exception than the rule, however, as political elites may prefer to cite “business as usual” and let existing structures of the judiciary lead investigations.

Finally, politicians can influence the likelihood of future prosecutions by *establishing a fact-finding commission/commission of inquiry* to shed light on the causes of (and those responsible for) the meltdown. A prominent example is the Pecora Commission, set up to document the

¹⁸ Kitty Calavita, and Henry Pontell. "Saving the Savings and Loans: US Government Response To Financial Crime." in Frank Pearce and Lauren Snider Eds, *Corporate Crime: Contemporary Debates* (Toronto: University of Toronto Press 1995): 199-214

¹⁹ Eisinger, 2010

causes of the 1929 Wall Street Crash. Inaugurating a fact-finding body sends a clear signal to prosecutorial authorities that accountability is a central issue to the government. Although the mandate of most fact-finding commissions precludes attribution of criminal responsibility, the final report of these bodies could direct prosecutorial authorities to potential cases of misconduct, creating momentum for criminal investigation. For example, the shocking revelations of the Pecora hearings framed criminally negligent bankers as *banksters* -- drawing parallels with famous gangsters of the time and legitimizing the political appetite to go after a handful of previously untouchable bankers.²⁰ The final report of such commissions not only gives the big picture of the causes of economic failure but can also pinpoint cases requiring investigation, thereby facilitating the work of prosecutors.

In sum, while not directly responsible for initiating prosecutions, politicians have access to important policy tools and are able to remove some of the roadblocks hindering prosecutions of bank executives. At the same time, there were significant variations in the extent to which European countries emerging from the recent global crisis deployed these tools (if at all). In some countries, politicians put criminal accountability center stage, while in other countries, they did not. For instance, while Iceland set up a special body to investigate the causes of the crisis, Cyprus followed a “business as usual” model, with the established prosecutorial and police authorities tasked to investigate and bring charges. What explains this variation? The next section outlines our theoretical answer.

3. Theory: What explains political appetite for retribution?

²⁰ Michael Perino, *The Hellbound of Wall Street: How Ferdinand Pecora's Investigation of The Great Crash Forever Changed American Finance*. (New York: Penguin, 2010)

In this section we consider the incentives of policymakers in the aftermath of a financial crisis to design policies to promote accountability in the financial sector. The extent to which politicians are proactive in this domain cannot simply be attributed to the extent to which misconduct and criminal activities trigger a crisis. The concealed nature of financial crimes makes it difficult for policymakers to assess whether widespread misconduct or illegal activities were committed in the lead-up to the crisis. Yet politicians are under pressure to devise a policy response even before the dust has settled.

To explain the variation in the extent to which different countries prioritized different policies post-2008, we propose going beyond the roots of the financial crisis and focusing on its aftermath. Our framework recognizes that the way a crisis unfolds significantly influences politicians' desire for retributive justice. We highlight two salient factors: voters' demands for a proactive approach and the impact pro-accountability policies may have on the economy.

First, in normal (non-crisis) times, the issue of holding banking executives accountable and investigating financial crimes is unlikely to receive much attention in the media and among voters. As a result, policy proposals aimed at strengthening the resources available to prosecutorial authorities to investigate corporate crimes are less likely to be a pressing issue from an electoral standpoint. Financial crises can be expected to change the equation, especially when the failure of a financial institution inflicts costs on a significant part of the population. Most commonly, the costs imposed by a bank failure are indirect, in the form of major fiscal expenditures when the government is forced to intervene and mitigate the economic spillovers of a banking collapse by bailing out the affected institutions. But as the severity of the banking crisis increases, this could result in more direct

costs imposed on voters, such as depositors not being protected or small bondholders being bailed-in.²¹

In these cases, once the people on the street are directly affected, the incumbent government faces stronger demands for proactivity.²² From an electoral standpoint, developing a policy that would apportion all blame to “reckless” bankers could prove beneficial, or at least minimize the political costs. Failure to do so might be perceived as an attempt at a “cover up”, thus incurring significant electoral costs.

Voters’ demands for accountability explain why policymakers are more likely to reform the policy and institutional framework guiding the investigations and prosecutions of financial crimes after a crisis rather than before, but this is not the only factor shaping political incentives to pursue retributive justice. As the “too big to jail” literature reviewed above highlights, the investigation of banks and bank officials could be destabilizing if it uncovers weaknesses in the management of these institutions.²³ Consider, for example, US Attorney General Eric Holder’s comment on concerns about prosecuting powerful corporate actors: “If you do bring a criminal charge, it will have a negative impact on the national economy, perhaps even the world economy”.²⁴ In this case, incumbents are likely to consider the potential impact upon the banking sector and, ultimately, the long-term political costs. In particular, they may be deterred from pursuing a proactive agenda of accountability if they think protracted inquiries or criminal investigations may negatively impact public and market confidence in the national banking industry, deterring future investments and prolonging the crisis.

²¹ Jeffrey Chwioroth, and Andrew Walter. *The Wealth Effect*. (New York:Cambridge University Press, 2019).

²² Ibid

²³ Garrett 2014; Rakoff 2014

²⁴ Cited in Robert Quigley. "The Impulse Towards Individual Criminal Punishment After the Financial Crisis." *Va. J. Soc. Pol'y & L.* 22 (May 2015): 107.

Not all types of crises generate the same concerns. It is important to distinguish between crises that result in the collapse of a banking institution or the broader banking sector and crises that lead to intervention, for example, when policymakers intervene by designing a bail-out or bail-in. In the former case, banks are no longer operational (at least in their pre-crisis form) and, as argued above, information on the responsibility for the collapse will have less impact, leaving politicians free to adopt policies that in other settings may be seen as hostile to the financial world.

In the latter case, when policymakers prevent a banking collapse through a bail-out or bail-in, their capacity to pursue an accountability agenda interacts with the fragility of the banks. More specifically, the capacity of policymakers to mitigate the impact of the crisis and restore growth is often tied to the recovery of the existing banking institutions. Criminal investigations and other policies of accountability may clash with this objective insofar as they may raise inconvenient truths that could prolong the crisis. At the most fundamental level, it could bring chronic mismanagement and corrupt practices into the spotlight. In turn, this – or fines imposed – may incur financial or reputational costs to new shareholders and harm the government’s efforts to restore confidence in the still fragile banking system and impede the possibility of privatizing the bank. Besides, in the aftermath of “managed crises,” even though their reputation may be damaged, bankers continue to yield significant power in the reconstruction of the fragile banking sector. Thus, the party in power may think twice before supporting policies of retribution, preferring to invest in a forward-looking narrative of successful economic recovery to maximize its opportunity of re-election.²⁵ Initiatives to bring banks into the spotlight are likely focus on the present health of banks and their

²⁵ Powell Jr, G. Bingham, and Guy D. Whitten. "A Cross-National Analysis of Economic Voting: Taking Account of The Political Context." *American Journal of Political Science*, 37 (May 1993): 391-414

capacity to withstand future economic shocks rather than on a backward-looking dissection of individuals' actions before the crisis. For instance, in an effort to restore public trust in the financial system, public authorities often use "stress tests" and other types of external audits to determine the present health of banks and their capacity to withstand future economic shocks; this type of transparency, in turn, attracts investors.²⁶

In sum, while a financial crisis may generate demands from voters to hold bank executives accountable, policymakers' incentives to act are mediated by the management of the crisis and the state of the banking industry. Table 1 illustrates the argument.

[Please add Table 1 about here]

4. Research Design

To address the variation in policies of accountability after financial crises, we comparatively analyze two cases that are "similar" in their background conditions, yet puzzlingly different in their outcomes.²⁷ Specifically, although conditions were similar in Iceland and Cyprus, politicians in Iceland pursued a proactive agenda of retribution, but those in Cyprus did not. Exploring two 'small' peripheral European states can help us test a prevalent literature of the policy response of 'small states' to the recent crisis.²⁸ In particular, we select Cyprus because

²⁶ Giovanni Petrella, and Andrea Resti, "Supervisors As Information Producers: Do Stress Tests Reduce Bank Opacity?" *Journal of Banking & Finance* 37, (December 2013): 5406-5420

²⁷ Arend Lijphart, "Comparative Politics and The Comparative Method". *American Political Science Review*, 65 (September 1971), 682-693

²⁸ Baldur Thorhallsson, And Peadar Kirby, "Financial Crises In Iceland And Ireland: Does European Union And Euro Membership Matter?" *JCMS: Journal of Common Market Studies* 50, (August 2012): 801-818.

its pre-crisis experience is a close approximation of the Icelandic experience, making it the “most likely” case to adopt a similar policy response (i.e. proactive agenda of retribution). If we do not observe this outcome in Cyprus, we will be far less likely to see it in other “milder” crises.

[Please add Figure 1 about here]

As Figure 1 illustrates, the two countries share a number of economic characteristics. First, while other countries faced public debt or housing crises, in both Iceland and Cyprus, the roots of the crisis lie in the reckless expansion of the banking sector (vertical axis in Figure 1). The countries shared a common developmental model that relied extensively on an oversized financial sector. Second, the severity of the shock faced by the banking sector in the two countries was similar, as measured by the number of non-performing loans at the peak of the crisis (horizontal axis in Figure 1). Third, in both countries, the attempt to mitigate the crisis resulted in large societal costs, such as the extraordinary costs of recapitalizing the banking sector (see Figure 1). Moreover, in both countries, the crisis was followed by the introduction of capital controls, bank runs, a haircut on deposits, and the collapse of at least one of the largest banks. As a result, taxpayers and depositors were significantly affected, making accountability a politically salient theme from day one. Fourth, both countries had an established legal framework to deal with corporate crimes – including insider trading, market manipulation or breaches of fiduciary duty - yet limited expertise in prosecuting these crimes.

The two countries also differ in important ways, some of which we explore below. One important element of difference is the fact that Cyprus is an EU member and part of

the European Monetary Union, while Iceland remain outside both. Existing scholarship has emphasized how the EMU membership played a significant role in constraining the policy response of its members and in particular encouraging bailouts of ailing banks over letting them collapse out of fear of contagion.²⁹ At the same time, it is worth noting how the EU and EMU membership do not constrain the capacity of countries to pursue pro-accountability policies, as clear from the variation of conduct across European countries. For example, a number of EU countries including Ireland and Spain have experienced (limited) prosecutions of bank executives. Most importantly, if EMU membership were the primary deterrent factor then we would expect that other non-member states affected by the crisis would be more proactive in their accountability agenda; yet, the experience of countries like the UK or Denmark does not support this argument.

In short, given the common background conditions, the comparative analysis will illuminate the ways their policy responses towards the crisis were shaped by an independent variable - the management of the crisis and its impact on the banking industry. Notably, in Iceland, the banks collapsed: the three main banks that accounted for 97% of the banking sector were put into receivership and liquidation, and new institutions were created in their place. In Cyprus, the banking system survived. To determine how these different banking conditions influenced the policy response, we use process tracing to identify the causal mechanisms driving particular policies of retribution. To identify the respective causal chains, we deploy standard process tracing tests to eliminate alternative hypotheses (“hoop tests”) or “smoking gun” tests to increase confidence in the selected hypothesis.³⁰ Our

²⁹ Martin Sandbu, *Europe's Orphan: The Future of The Euro and The Politics of Debt*. (Princeton: Princeton University Press, 2015).

³⁰ James Mahoney, "After KKV: The New Methodology of Qualitative Research." *World Politics* 62, (January, 2010): 120-147; David Collier, "Understanding Process Tracing." *PS: Political Science & Politics* 44, (October, 2011): 823-830.

analysis draws on more than 55 in-depth elite interviews and a period of fieldwork in the two countries, bolstering our confidence in our ability to trace the processes.³¹

5. Analysis

5.1 Iceland

Iceland was the first European country to experience the aftershock of the Great Recession. The colossal and direct impact of the Crash led to an unprecedented mobilization of the citizenry - called the “Pots & Pans Revolution” – in a country with no previous culture of protest.³² A key theme in the waves of protest was retribution, expressed in demands to identify those responsible and sack them. Voters’ pressure on politicians for accountability was so great that it would have been electorally costly for any party to ignore it, especially the incumbent, the Independence Party (ibid). Having been in power for almost 15 years preceding the crisis and as the pioneer of Viking Capitalism, the Independence Party was seen as largely responsible for the (mismanagement) of the crisis and was forced to put itself under the microscope. The country’s political culture further reinforced responsiveness. According to one of the opposition leaders, the PM understood that “the events were of such magnitude that there would never be any agreement or reconciliation unless they were thoroughly investigated”.³³ Still, this “principled” response was greatly facilitated by the impact of the crisis on the banking industry.

³¹ Oisín Tansey, "Process Tracing and Elite Interviewing: A Case for Non-Probability Sampling." *PS: Political Science & Politics* 40, (October, 2007): 765-772.

³² Jón Gunnar Bernburg, *Economic Crisis and Mass Protest: The Pots and Pans Revolution in Iceland*. (London: Routledge, 2016).

³³ Cited in Ragnar Hjalmarrson, (Forthcoming) *Transitional Justice After Economic Collapse: The Case Of Iceland*, *Phd Dissertation*, Hartie School Of Governance (2020)

Unlike other countries, the government's bailout of the banking sector failed to restore faith in the main banking institutions. As a result, the three main banks (Glitnir, Kaupthing, & Landsbanki) accounting for 97% of the banking sector were put into receivership and liquidation, creating one of the world's largest corporate bankruptcies on record. New banks were created to take over domestic banking operations. As all the three major banks collapsed, preserving the confidence in these institutions was not a priority during crisis management, and reverting to the pre-crisis finance-led growth model was not an option³⁴. This meant politicians in Iceland were not constrained by the possible consequences of confrontational policies of accountability on the banking industry, and policies of accountability took root.

The Emergency Law (No.125/2008), enacted with wide cross-party consensus in December 2008, clearly established the centrality of accountability in the broader crisis management policy. This legislation outlined the crisis management response and included a number of provisions directed at promoting the accountability of the bank executives responsible for the crisis. A cornerstone of the accountability architecture included in the Emergency Law was "truth recovery". In the early period after the crisis, the "Viking bankers" signaled their willingness to participate in a truth commission similar to the South African model, with amnesty offered in exchange for revealing the truth.³⁵ However, with the collapse of the banks, the idea was flatly rejected. Instead, the legislation included the creation of a truth commission (Special Investigation Commission, SIC) to investigate and

³⁴ Sigridur Benediktsdottir, Jon Danielsson, and Gylfi Zoega. "Lessons From A Collapse of a Financial System." *Economic Policy* 26, (April, 2011): 183-235; Gudrun Johnsen, *Bringing Down the Banking System: Lessons From Iceland*. (New York: Palgrave, 2014).

³⁵ Cited In Hjalmarsson, Forthcoming

document patterns of policy, institutional, and other failures.³⁶ The truth commission's mandate was very harsh, with provisions to punish those obstructing access to evidence with up to two years' jail time. Drawing on a very thorough "forensic" investigation, the final report identified the key causes of the meltdown, including the rapid expansion of the banking sector, the excessive access of the owners of the largest banks to their banks' credit, and the instrumental use of banks to pursue the interests of large shareholders rather than the banks' interests.³⁷

Another cornerstone of the accountability architecture was "prosecutions." More specifically, politicians had to decide whether the task of investigating cases of alleged white-collar crimes flagged by the SIC and bringing charges against those responsible for the Crash would be led by existing law enforcement and judicial authorities or new/ad hoc prosecutorial authorities. Our interviews with members of the judiciary indicated that the established structures were anemic. The designated state authorities tasked to investigate white-collar crimes had limited experience. For example, the "Economic Crimes Unit" – part of the national Commissioner of the Icelandic Police – was an understaffed unit with inadequate capacity to investigate corporate crimes. As a state prosecutor remarked, "There was really not much understanding of this area, these so-called white-collar crimes. So our experience was not that great, though of course economic crimes were taking place".³⁸

Instead of relying on the national judicial authorities, a decision was made to establish a new ad hoc body to investigate the crisis-related cases, the Office of the Special

³⁶ Iosif Kovras, Shaun McDaid, & Ragnar Hjalmarrsson, "Truth Commissions After Economic Crises: Political Learning or Blame Game?." *Political Studies*, (January, 2018) 66: 173-191

³⁷ Ragnar Hjalmarrsson 'Accountability After Crisis'. Country Report: Iceland. London (March, 2018):14 Also available at: <https://Accountabilityaftereconomiccrisis.Com/Assets/Uploads/Policy-Report-Iceland-Eng-.Pdf> [Last Accessed 16 April 2019]

³⁸ Interview with Icelandic State Prosecutor, Reykjavik, 8 December 2016.

Prosecutor (OSP).³⁹ The government also took action to ensure the success of this body. One important step was a legal provision vesting the OSP with the power to procure data related to its investigation.⁴⁰ Accessing data, documents, and other potentially incriminatory evidence was crucial if the investigations were to succeed. A novel clause in the Act establishing the OSP authorized the authorities to confiscate data related to their scope of investigation (Act No. 25/2009, art 5). In effect, while in the past, a court order was needed, this clause forced banks under investigation to share all the data requested by the OSP. The Chief Prosecutor explained to us how the legislation facilitated the work of the OSP: “[I]f you are constantly requesting material from the banks, you always have to have a court ruling on each and every application, you hit some problems. It takes too much time”.⁴¹

The second step taken by the government to facilitate the pursuit of accountability was the allocation of ample resources for the OSP to carry out its investigations.⁴² When the parliament set up the OSP in early 2009, it was envisioned as a small office of approximately 5-10 staff on a tight budget; it would investigate only a handful of cases associated with the Crash and close down by the end of 2010. But subsequent decisions strengthened its operations. By 2012-13, the OSP had received ample resources, allowing it to employ over 100 staff members and acquire expertise in areas that immensely facilitated the pace of investigations. Consequently, between 2010 and 2016, the OSP prosecuted 67 individuals, a large number for a small country with a population of approximately 350,000.

³⁹ Ibid

⁴⁰ Act No. 25/2009 (Art 5). there was also a provision for whistle-blowers to come forward and share information to support criminal investigations

⁴¹ Interview with the Head of The Office Of The Special Prosecutor, Reykjavik, 18 April 2017

⁴² The estimated total cost of its operations is 5,9 bn ISK (Approximately €36,7 Million, cited in Hjalmarrson 2018:17

It is important to note how the government's proactive stance at the beginning of the crisis and the gradual success of the OSP generated an "accountability cycle". After the incumbent government collapsed as a result of the "Pots & Pans Revolution," the Social Democrats and Left-Green Movement formed a coalition government in early 2009; they promised to continue to pursue a policy that would identify and punish the culprits.⁴³ This commitment was reflected in the gradual expansion of the mandate of the OSP to include all white-collar crimes in Iceland beyond the crisis-related cases. But the support for this institution did not wane even after the return to government of the Independence Party five years after the Crash. Although the new leadership wanted to draw a line with the past and move forward, the budget tabled for 2014 spared the OSP from the budget cuts imposed on other parts of the state.

In effect, the total collapse of the banking industry was instrumental in boosting support for retributive justice. As the banks were effectively wiped out, political elites did not need to worry about the potential impact of investigations on the stability or reputation of the banking institutions. A local prosecutor explicitly cited the collapse of the banks as the most crucial factor driving the investigations by highlighting a counterfactual: "If the banks had weathered this (crisis) then nobody would have wanted to rock the boat [...] If they would have just barely survived, one does not know what would have happened...it would have been a completely different situation, so that of course changed the situation".⁴⁴ A senior member of the judiciary confirmed this: "I think that just somehow that this would have looked completely different if the Crash had not happened. Then somehow the whole

⁴³ Hjalmarsson 2018:10

⁴⁴ Interview with 2nd anonymous Icelandic Prosecutor, Reykjavik, 8 December 2016

scene would have been different in regards to access to data, I think that is absolutely safe to say”.⁴⁵

5.2 Cyprus⁴⁶

The Cypriot banks followed a similar trajectory to the Icelandic ones, with rapid expansion in the pre-crisis years, reaching almost eight times the GDP in 2009.⁴⁷ The financial crisis took longer to reach the periphery of the Eurozone, and Cyprus was the last casualty. In 2013, the Cypriot government agreed to an international bailout package with the European Commission, the European Central Bank (ECB), and the International Monetary Fund (IMF) (the “Troika”) that included a “bail-in” of deposits above €100,000 in the country’s second-largest bank (Laiki Bank) and an equivalent levy on half of the uninsured deposits in the country’s largest bank (Bank of Cyprus). The bail-in paved the way for a run on the banks and the imposition of capital controls.

All these ingredients ensured the crisis had a direct and severe impact on people’s daily lives. As a result, the bail-in was followed by the first massive wave of protests since the Turkish invasion in 1974. The protest was even more impressive when we consider that the Greek Cypriot political culture is strongly averse to anti-government protest.⁴⁸ The outcry increased the salience of holding individuals responsible for the crisis accountable and forced the government to respond. Days after signing the bail-in package and agreeing to the confiscation of uninsured deposits, the government added a policy of accountability for the

⁴⁵ Interview with District Court Judge in Iceland, Reykjavik, 6 December 2016

⁴⁶ We use the term Cyprus to refer to developments in the Republic of Cyprus.

⁴⁷ Alexander Michaelides, “Cyprus: From Boom To Bail-In”, In Alexander Michaelides,, & Athanasios Orphanides Eds. *The Cyprus Bail-In: Policy Lessons from The Cyprus Economic Crisis*. (London:World Scientific, 2016):122; Stavros Zenios. "Fairness and Reflexivity In The Cyprus Bail-In." *Empirica* 43, (September, 2016): 579-606.

⁴⁸ Giorgos Charalambous, andnd Gregoris Ioannou."Party Systems, Party-Society Linkages, And Contentious Acts: Cyprus In A Comparative, Southern European Perspective." *Mobilization* 22, (March, 2017): 97-119.

crisis to its agenda. In the ceremony welcoming the new Chief of Police and the new Attorney general, the President clearly framed the priorities of the government, explaining “we have no right to disappoint society,” thus explicitly acknowledging the public demand to punish those responsible.⁴⁹

In all these respects, the Cypriot experience mirrors the aftermath of the Crash in Iceland. At the same time, the development of this agenda did not match the scope and ambition of Iceland. First, a few weeks after the meltdown, the government set up an independent commission of inquiry to shed light on the causes.⁵⁰ While the mandate of the commission initially included the provision that evidence collected during hearings could be used for criminal cases, within a few weeks, the mandate was changed, turning the commission into a purely fact-finding enterprise.⁵¹

Second, politicians in Cyprus and Iceland faced similar dilemmas over the extent to which they could rely on the established investigative authorities to lead the investigation and prosecution of potential white-collar crimes associated with the crisis. The police included a special branch on economic crimes, the Economic Crimes Investigation Office, but this unit dealt with very few cases in the pre-crisis years, and it was not well equipped to deal with more complex corporate crimes. The former Attorney General (AG) admitted that the “inability to effectively investigate such cases” was probably the most important reason for the non-effective prosecution of bankers in Cyprus: “[H]onestly we didn’t even understand the crime, neither me nor the police”.⁵² Still, instead of creating a new special/ad hoc body as

⁴⁹ Adonis Pegasiou (2018) *Accountability After Crisis. Country Report: Cyprus*. (March 2016) London: Also Available At: <https://Accountabilityaftereconomiccrisis.Com/Assets/Uploads/Policy-Report-Cyprus-Eng.Pdf> [Last Accessed 16 April 2019]

⁵⁰ Zenios 2013

⁵¹ Pantelis Pantelides " AG Orders Criminal Probe Into Economic Crisis', Cyprus Mail, July 2nd 2013, (2013) Also available at: <https://Cyprus-Mail.Com/Old/2013/07/02/Ag-Orders-Criminal-Probe-Into-Economic-Crisis>

⁵² Interview with the former Attorney General of the Republic of Cyprus, Nicosia, 27 July 2017

in Iceland, the Cypriot government decided to reshuffle existing personnel from different departments of the police and the economic crimes investigation office into a new Special Task Force within the existing structures to lead the inquiries. Moreover, the Task Force reported to the Ministry of Justice, setting the tone of the investigations; decisions on the budget, expertise, and staff deemed essential for success were screened by the Ministry.

Third, unlike in Iceland, the incumbent government did not introduce changes to the legislative framework to set the stage for an effective investigation. According to a prominent Cypriot MP, the framework remained out-dated and inhibited police investigations, making it extremely difficult to access and confiscate data (Interview N.7).

Finally, the government provided only limited additional resources to the existing prosecutorial authorities to support criminal investigations.⁵³ In particular, most resources directed towards the office the Law Office were used to cover expenses related to the legal representation of the state in international courts and arbitration processes stemming from the bail-in provisions of 2013 (Fileleftheros 2018), with no parallel investment of new resources in criminal investigations. Although precise data are not publicly available,⁵⁴ most informed participants estimated the total number of investigative staff working on cases related to the crisis were in the region of 25 to 30.⁵⁵ This adversely affected the pace of investigations. When asked about the reasons for the delay in processing cases, a senior member of the Supreme Court pinpointed the lack of resources and staff.⁵⁶

In sum, unlike in Iceland, the policy of accountability endorsed by the Cypriot government after the crisis did not remove the structural, financial, and legal constraints to

⁵³ Pegasiou, 2018

⁵⁴ Despite repeated official requests to get access to the budget and the manpower of the bodies involved in criminal investigation, we received no response from the Cypriot authorities.

⁵⁵ Interview with MP of the center-right Party DISY and economics professor, Nicosia, 26 July 2017

⁵⁶ Interview with high ranking staff at the Supreme Court of the Republic of Cyprus, Nicosia, 15 July 2017

the investigation and prosecution of individuals responsible for the crisis. Instead, according to informed observers, the incumbent government's plan was to selectively focus on a few cases to appease the public demand for justice, without launching a thorough investigation (Interview Nos 18, 19). What could explain this outcome?

To answer, we need to consider how the political appetite for a proactive policy of accountability interacted with the fragile state of the banking system. While in Iceland, new banks were founded to take over the domestic operations of three major banks (Kaupthing, Landsbanki, and Glitnir), in Cyprus, a decision was made to turn the weaker of the two main Cypriot banks (Popular/Laiki Bank) into a "bad bank" to absorb all toxic assets from the banking sector in Cyprus. At the same time, all guaranteed deposits were moved to the Bank of Cyprus (BoC), the ("good") bank the state decided to save.

The interaction between the prospect of a proactive policy of accountability and the policy objective of preserving the fragile financial sector was particularly evident in the handling of the Cyprus Cooperative Bank (CCB), a network of local credit institutions. As part of the IMF-sponsored program, the government nationalized 77% of the CCB, incurring a total cost of approximately €1.8bn for taxpayers.⁵⁷ The public anger about lingering corruption/mismanagement, along with the powerless status of the local board members involved in the practices, made this a "most likely" case to see official investigation in 2013,⁵⁸ but no specific action was taken in the aftermath of the crisis by the government to investigate the widespread corrupt practices that characterized this institution in the years

⁵⁷ Gikas Hardouvelis. "Overcoming the Crisis In Cyprus". In Alexander Michaelides,, & Athanasios Orphanides Eds. *The Cyprus Bail-In: Policy Lessons from The Cyprus Economic Crisis*. (London:World Scientific, 2016): 251

⁵⁸ George Ioannides, "Who is to blame for the co-op bank disaster?" *Cyprus Mail*, July 1st 2018, Also available at: <https://Cyprus-Mail.Com/2018/07/01/Who-Is-To-Blame-For-The-Co-Op-Bank-Disaster/> [Last Accessed 16 April 2019]

before the crisis. This course of action was influenced by concerns about the implications of an investigation. A key priority during this period was stabilizing the cooperative sector so that “in the future it [CCB] can cover potential capital needs by raising money from private investors”.⁵⁹ The Troika’s timeline for the privatization of the bank shaped the political priorities of the government, most notably its reluctance to inflict financial or reputational costs on new shareholders that the government had to entice to join in the first place. An anonymous member of the Cooperative Bank was clear about possible consequences: “Pushing hard for criminal investigations could act as a disincentive for potential investors given the legal and other repercussions this could have for the bank” (Interview No.20). An investigation could also have unearthed inconvenient truths about the politicians themselves; for example, the chronic lack of political control of the boards of cooperative banks was partly responsible for the dire straits of the cooperative sector during the crisis.⁶⁰ All these considerations curbed the politicians’ enthusiasm for criminal investigations in the cooperative sector (and, more broadly, in the banking industry after the 2013 meltdown).

It was only after the party in power decided in 2018 to sell the CCB to a competitor (Hellenic Bank) that politicians seriously considered launching an inquiry into its management. The decision to allow Hellenic Bank to acquire the “good part” of the CCB while the government guaranteed that any “bad/non-performing loans” would be absorbed by the government was seen as extremely unfavorable for the interests of Cypriot taxpayers and created a public uproar.⁶¹ As a result of the public discontent, a second committee of

⁵⁹ European Commission ‘Press Release: Commission Approves Additional Aid For Cypriot Cooperative Banks On The Basis Of An Amended Restructuring Plan,’ December 18th, 2015, Available At: [Http://Europa.Eu/Rapid/Press-Release_IP-15-6365_En.Htm](http://europa.eu/rapid/press-release_IP-15-6365_en.htm)

⁶⁰ Yorgos Arestis, Yorgos Charalambous, Yorgos Georgiou. ‘Final Report Of The Commission Of Inquiry On The Causes Of The Collapse Of The Cooperative Sector’, Nicosia, March 1st 2019, Available At: [Https://Cyprus-Mail.Com/Wp-Content/Uploads/2018/06/REPORT.Pdf](https://Cyprus-Mail.Com/Wp-Content/Uploads/2018/06/REPORT.Pdf) (In Greek)

⁶¹ Leslie Manison, ‘The Hellenic Bank-Cyprus Cooperative Bank Deal’, Stockwatch, 4th July 2018, available at: [Https://Www.Stockwatch.Com.Cy/El/Blog/685933-Hellenic-Bank-Cyprus-Cooperative-Bank-Deal](https://www.stockwatch.com.cy/El/Blog/685933-Hellenic-Bank-Cyprus-Cooperative-Bank-Deal)

inquiry was set up to investigate both the chronic problems of the CCB and the conditions of its privatization in 2018. Other than this specific case, however, the accountability agenda was far less prominent in Cyprus than in Iceland. In the 2018 electoral manifesto, the President did not make a single reference to any of the policies of accountability deployed during his time in office.

In sum, in Cyprus, the bail-in to save banks from a total collapse and the resulting capital controls generated popular demands for accountability. Yet the political appetite for retribution was curbed by the fragility of the banking sector and the need to restore confidence in its institutions. As such, Cyprus is a “crucial” case: despite the debilitated state of the banking sector and growing public demands for accountability, stability and economic recovery were more important than accountability, even when it was expedient for the government to seek accountability.

6. Alternative Explanations

Although we have illustrated how the different levels of political desire for a proactive policy of accountability in Cyprus and Iceland interacted with the conditions of their respective banking industries, there are limitations in the extent to which we can find conclusive evidence through process tracing in cases like Cyprus where “the dog did not bark.” So to increase confidence in our argument, we should consider other plausible hypotheses that could account for variations in politicians’ responses. These include the electoral cycle, the electoral/political system, and party ideology.

The level of incumbent culpability may shape politicians' responsiveness to popular demands for accountability, and a common concern in times of crisis is to deflect blame.⁶² Those in power in the period leading up to crisis might be concerned about the inconvenient facts that a criminal investigation could unearth, such as regulatory failures or omissions. In contrast, a new party in government, with limited previous exposure to power and no part in the crisis, might be more interested in investigating the causes (as their predecessors might be found culpable) and holding bank executives accountable.

In Iceland, the decision to set up a special commission of inquiry on the roots of the crisis was taken by the center-right Independence Party seen as the architect of "Viking Capitalism" and as responsible for (the mismanagement of) the crisis. If blame avoidance were the chief concern, the Independence Party would have been the least enthusiastic supporter of retributive justice, not the party setting it in motion. In Cyprus, the newly elected conservative government that came to power in 2013 after a decade in opposition with limited responsibility for the creation of the crisis should have endorsed policies of accountability, seeking to heap blame on their predecessors. Yet mindful of the adverse consequences of prosecutions on the stability of the banking sector and the broader economic recovery, it decided to downplay the justice discourse. Overall, then, this hypothesis fails to explain why even though both countries examined here experienced a change in government and saw the emergence of new parties with limited pre-crisis exposure to power, only one was interested in retribution.

We could also point to the degree of influence business (in this case, banking) has on the policymaking processes. The literature shows how the proximity of bankers to

⁶² Arjen, Boin, Eric Stern, And Bengt Sundelius. *The Politics of Crisis Management: Public Leadership Under Pressure*. (New York: Cambridge University Press, 2016); Christopher Hood, *The Blame Game: Spin, Bureaucracy, And Self-Preservation in Government*. (Princeton: Princeton University Press, 2010).

policymakers and the structural power they can leverage determine the nature of bail-in/out in times of crisis.⁶³ An important literature on the “financialization of the economy”⁶⁴ has theorized how the structural power of the financial industry has further been enhanced by the increase in the size of financial industry and its centrality within the business community since the 1970s.⁶⁵ From this perspective, it could be argued that banks’ level of political influence and structural power may also affect how keenly politicians seek retribution.

Although obviously relevant, the structural power of bankers and the banks’ institutional relations with the state are not fixed and linear, and the balance of power may be significantly affected by the impact of the crisis. For instance, the structural importance of the financial industry in the economy has in many cases been a poor predictor of the stringency of the regulatory requirements imposed by different governments after the global financial crisis.⁶⁶ As a result, the level of political influence of bankers before the crisis does not necessarily predict politicians’ appetite for retribution. As we have pointed out, Cyprus and Iceland followed a similar pre-crisis developmental model that relied on a disproportionate expansion of the financial sector. Financial actors accrued significant political influence in both countries in the years before the crisis. Yet the impact of the crisis

⁶³ Pepper Culpepper and Raphael Reinke. "Structural Power And Bank Bailouts In The United Kingdom And The United States." *Politics & Society* 42, (September, 2014): 427-454.

⁶⁴ Gerald Epstein (Ed.). *Financialization And the World Economy*, (Cheltenham: Edward Elgar, 2005)

⁶⁵ For a review, see Stefano Pagliari, and Kevin Young. “How Is Financialization Reproduced Politically”. In Mader Mertens, and Van Der Zwan, *The Routledge International Handbook Of Financialization*, (London: Routledge, 2020).

⁶⁶ Kevin Young and Sung Ho Park, “Regulatory Opportunism: Cross-National Patterns In National Banking Regulatory Responses Following The Global Financial Crisis”, *Public Administration*, 91 (February, 2013): 561–581; David Howarth, And Lucia Quaglia 2013, “Banking On Stability : The Political Economy Of New Capital Requirements In The European Union”, 35 (April, 2013): 37–41.

affected the relationship/power of bankers differently in the two countries, with a sharp desire for political retribution seen only in Iceland.

A third explanation focuses on the role of party ideology. Parties ideologically aligned with the financial industry, often on the right of the political spectrum, are less likely to promote policies favoring the prosecution of bankers than parties whose ideology is antagonistic to finance. Although this could explain the meager response of the Cypriot center-right DISY party – traditionally seen as close to the banking industry - it fails to account for the decision of its counterpart in Iceland, the pro-banking Independence Party, to design a proactive agenda of accountability that included criminal investigation.⁶⁷ As the mastermind of the Viking Capitalist venture, the Independence Party was the least likely candidate to investigate bank executives. Hence, this hypothesis can explain the new government's (social-democrats) continued support for policies of accountability but not the original decision to put this issue on the political agenda. After the 2008 Crash, it seems ideology lost relevance.

Finally, political culture may be a factor in retribution. We would expect that politicians in countries with perception of widespread corruption (even in the period preceding the crisis) would be less inclined to pursue policies of retribution, as transparency may expose inconvenient truths about their own potential misconduct. This is the case of Cyprus where the very government which did not pursue pro-accountability policies is largely accused by domestic NGOs and international organizations for high-levels of alleged

⁶⁷ We acknowledge that DISY and the Independence Party are quite different species and that accountability has been more salient in the Icelandic case, yet we show that this is not sufficient reason to explain the divergent outcomes.

corruption;⁶⁸ this perception of widespread corruption may affect how politicians deal with accountability as they may be reluctant to deploy investigative mechanisms that may expose their own wrongdoing. Besides, political culture of silence there is limited public expectation that the incumbent respond to public calls for a criminal investigation. On the contrary, in countries like Iceland where pre-crisis levels of trust in institutions were high, the degree of responsiveness to popular calls for justice should be higher. As we show in the analysis, this is true to some extent, as evident by the decision of the party (most) responsible for the crisis to adopt a pro-accountability agenda, as well as the strong cross-party consensus. Yet we are not in a position to determine whether political culture could have triggered this outcome if it were not for the unique impact of the crisis on the banking sector. In fact, other Nordic countries with similar high integrity and levels of trust in institutions did not pursue a similar policy of retribution after the crisis in the 1980s (Sweden, Finland) or after 2008 (Denmark). The role of political culture in shaping political responses requires further attention but it does not seem to be the most crucial causal factor.

7. Conclusion

This paper sheds light on how politics shape the extent to which bank executives are held accountable after a financial crisis. Politicians can influence the likelihood of investigations and prosecutions of bank executives in various ways, such as establishing novel prosecutorial authorities tasked to document white-collar crimes related to the crisis and creating fact-finding commissions subjecting bank executives' actions to public scrutiny. They can facilitate the work of prosecutorial authorities by providing resources, manpower, and

⁶⁸ Elias Hazou, "Citizenship Linked To President's Family Ties", *Cyprus Property News*, February 10th 2019, also available at: <https://www.news.cyprus-property-buyers.com/2019/02/10/citizenship-linked-president-family/id=00155380> [Last Accessed 28 February 2020]

(forensic/technological) expertise. They can also amend the legislative framework to facilitate prosecutors' access to (incriminatory) evidence.

In our examination of the different reactions to the recent financial crisis in two European countries, we have identified the demand from voters and the impact of the crisis on the banking institutions as crucial explanatory factors. In particular, in crises marked by the collapse of the banking sector, the potential systemic or reputational risks associated with criminal investigations are minimal, as banks are already inoperative, making it easier for politicians to accommodate the high public demand for accountability. In negotiated crises, where the government intervenes to prevent the collapse of banking institutions (bailout-bail-in), the impact of voters' demands is mitigated by concerns about the impact investigations could have on the stability of a weakened financial system; this could unnecessarily prolong the crisis and incur further political costs for those in power.

Although we have taken the first step towards explaining differences across countries in the promotion of accountability after a crisis, we have only compared two countries: Iceland and Cyprus. The similar background conditions of the two countries and the different conditions of the banking industry after the crisis make this choice appropriate to develop our argument. At the same time, future research should probe the generalizability of our theoretical framework by exploring cases with different background conditions, including bigger economies with no external supervision. In particular, while both Cyprus and Iceland both experienced severe crises that directly affected the livelihood of citizens such as capital controls and depositors' haircuts and triggered mass protests, our case selection does not allow us to explore to what extent politicians embark on an agenda of accountability in the absence of these dynamics.

For instance, further work could explore why other larger European countries and the US did not embrace a more proactive agenda of accountability, despite the emergence of protest movements demanding justice (e.g. Occupy Movement in the US or Indignados in Southern Europe). Further work could also draw on historical cases to understand the origins of the demand for retribution after a crisis. One example is the reluctance of US authorities to promote accountability after Lehman vs. the aftermath of the saving and loans crisis in the 1980s/1990s when hundreds of individuals were prosecuted.⁶⁹ Our framework suggests the de facto collapse of hundreds of institutions in the latter example, coupled with the limited “systemic” impact on the global financial system, made it more likely to see a retributive policy than the 2008 crisis.

Further research is needed to explore the impact of the dynamics theorized in this paper on a broader range of policies beyond those aimed at facilitating the investigation and prosecution of individuals. There is a significant body of research on corporate prosecutions and other forms of corporate sanctions, as they are the most frequent and easy forms of punishment.⁷⁰ More work is also needed to understand the extent to which the conditions of the banking industry in the aftermath of crisis constrain the appetite for accountability policies targeting financial institutions or other forms of regulatory policies.

Finally, we have focused on explaining the variations in the political responsiveness to calls for retribution, not the impact of the policies of accountability per se. We need to understand the short-term consequences of these policies on the initiation and outcome of actual criminal investigations, as well as their long-term consequences. As crises are

⁶⁹ Calavita & Pontell, 1995

⁷⁰ Garrett 2014:13

opportunities for learning from past failures and, as such, represent “critical junctures,” decisions made in response to a crisis can have a lasting impact on national institutions. For example, the OSP in Iceland was converted into a permanent prosecutorial authority to deal with corporate crimes. The expertise developed in the process of investigating cases related to the recent crisis and the “institutional memory” of its members created one of the most knowledgeable and well-trained prosecutorial bodies in Europe. As a result, Iceland has the institutional capacity to investigate white-collar crimes, arguably protecting it from a similar crisis in the future. Meanwhile, the half-hearted political response in Cyprus led to smaller changes, and an opportunity was lost. Taken together, these case studies suggest political responses can lead to important institutional legacies, but more work is required to understand the long-term consequences of the decision to pursue accountability.