

- To reveal main distinction between IFRS and UA-GAAP that should be corrected in the nearest future;
- To compare two main kinds of conceptual frameworks;
- To form a set of strategies and recommendations for Ukrainian government, which might be practically applicable in order to correct UA-GAAP.

First of all, it is vital to mention that IFRS are settled by International Accounting Standard Board or IASB. This system of standardization is related to Common law, which is cardinally different from legal system adapted in Ukraine, Codified Roman law. [1]

The roots of the problem of differences between IFRS and Ukrainian Accounting standards come from different legal systems. We can see this in two types of conceptual frameworks that become a stumbling block for auditors and investors in their decision-making processes. Those are *fair presentation* and *compliance* frameworks. Most of countries adapted IFRS (not fully, but in greater extent than Ukraine did) like the US and Australia have fair presentation framework as a basis of their accounting standards. At the same time, Ukrainian accounting bases on compliance framework.

Fair presentation requires an auditor not just examine financial indicators of a company, but also check the whole entity to make sure that financial statements depict the real situation of company's business activity. Compliance framework requires an auditor just to persuade that a company prepared financial statements in accordance to the rules of the framework. The real state of affairs may not be checked under this kind of framework.

As we can see these principles cause the core discrepancies between UA-GAAP and IFRS, which are the source of further incompatibility that can affect investment attractiveness of Ukraine, as fair representation of financial indicators play an important role in investors' decision making.

Definitely, it can be assumed that Ukrainian government should specify Ukrainian accounting standards in order to reveal real affairs of domestic companies. This can be reached with the help of convergence with IFRS, which takes time to adapt into legislation and bring to life.

Finally, to understand the differences between UA-GAAP and IFRS, it is necessary to understand the fundamental difference between frameworks. Therefore, it is necessary to begin work on studying the Conceptual Framework of IFRS. This will make it possible to simplify the process of adaptation of IFRS in legislation and their practical application through convergence.

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NUDGING THE NUDGERS: FISCAL AND MONETARY INSTITUTIONS AS THE SUBJECT TO COGNITIVE BIASES THEY FIGHT WITH

Behavioral economics insights are widely embraced by policymakers all around the world quite frequently to advocate for broader and deeper government intervention. Even the concept of 'soft paternalism' aiming to modify but not restrict the set of available choices to reach a desirable outcome is governed by how the policymakers see and define this 'desirable outcome'. According to C. Sunstein, 'for every bias identified for individuals, there is an accompanying bias in the public sphere' [19]. The essence of the argument is that the design of the democratic system in which mostly all the decisions are made through a majority voting system creates conditions when the state policies will reflect the cognitive biases of the individuals [20, 21].

Interestingly, this point of view is usually ignored by the most of the behavioral economics papers that recommend paternalistic policy intervention. In his analysis of publications in behavioral economics

field, N. Berggren analyzes 300 articles and concludes that out of 67 publications that have policy prescriptions, 95.5% of articles do not pay attention to cognitive limitations and biases policymakers might be subject to. Only two publications apply behavioral insights to the government the same way they do it with all the other economic players [2, 4].

With this essay I would like to contribute to this type of analysis in the cognitive science and policymaking and try to describe potential decision-making failures and illustrate them by examples where possible. The cognitive biases that are going to be analyzed are over optimism (overconfidence), status quo bias, inertia, loss aversion, availability and representativeness biases. Moreover, I discuss the possible ways of how to minimize such cognitive biases in public sphere. In this analysis I narrow down to a very specific type of policymakers – monetary and fiscal authorities (mainly dominated by economists) - as these are the experts who work the most with incentives of ordinary people but seem not to analyze incentives that shape their field enough to avoid institutionalization of behavioral anomalies they have [9].

Illusionary superiority the monetary and fiscal institutions might have over managing macroeconomy results in the overconfidence and overoptimism bias [3]. This causes plenty of inaccuracies in both qualitative and quantitative impact of the policies they implement: for example, timing, magnitude and even the direction of changes. One of the most popular examples is, probably, liberal reforms in transition economies after the collapse of the Soviet Union when, especially in the Russian case, the government made the decision to liberalize markets and privatize state property quite rapidly (1995) to transform country into a market democracy. This reform turned out to be an economic catastrophe which dropped the real GDP by 40% and instead of market economy transferred the capital from the state to the hands of oligarch clans. The headlines of writings by the main economist Anders Aslund who led this reform ('The triumph of capitalism' (1993a), 'Russia's success story' (1994), and 'Russian shock therapy succeeded' (1996)) definitely predicted the opposite outcome [1]. In addition to that, one can observe that fiscal institutions quite often are overoptimistic about the public finance in the future periods, the forecasts about the budget deficit or public borrowings are always underestimated [15].

The other behavioral biases described by D. Kahneman and A. Tversky as greater regret for bad outcomes that result from new actions being taken than those result from inaction – status quo bias – which is very consistent with the 'fear of liftoff' – inertia – are the cases that are quite familiar not only to the ordinary people but to policymakers as well [14, 17]. The status quo regulations in addition to the inertia caused by the bureaucratic nature of legislative process do not allow the governments to be efficient and quick in facing new economic challenges. For example, in the case of global financial crisis in 2008 which was caused partially by absence of proper reaction of the Fed to the emerging new financial instruments (collateralized debt securities) in the investment banking sphere.

Another strong finding in behavioral science is loss aversion of individuals which means that the perceived costs of potential losses are much larger than potential symmetric benefits. In application to policymakers, this concept might be found when recent market or policy failures generate bias against actions that might lead to the 'undesirable' (according to the view of policymakers) outcome even if those actions are needed to be taken at that moment. To make it clearer, let's imagine a central bank which has a numerical target, for example, inflation target of 5%. The existence of such a target (not necessarily in numeric expression) in addition to loss aversion bias will restrict policymakers and oblige them to follow the rule even if the deviation is optimal in that situation.

The set of behavioral biases which are extremely relevant for policymakers as well are availability bias (when individuals often go with the cases they know well and, accordingly, overestimate the probability of such an event or outcome) and representativeness bias (which means that policy decisions might be vulnerable to generalizations) [3]. To understand it better in economic terms, one should take into account the fact that monetary and fiscal institutions do not have the capacity to evaluate on the spot the state of the whole economic system, they have some set of indicators they use to make their decisions to react properly to the possibly emerging challenges. For instance, monitoring the increase in the overall price level by only looking at the consumer price index might be misleading as it includes very limited number of goods in the consumer basket.

At the same time, the cognitive biases inherent to policymakers are not the exhaustive explanation for behaviors described above. In order to complete the full picture of cognitive processes behind such policy decisions outcome, one should consider some alternative and/or complementary reasons. Overoptimism and overconfidence in managing the macroeconomic situation might be a conscious

decision as a part of communication strategy of monetary and fiscal institutions. This concept was developed further by a popular Swedish monetary economist D. Holmes who formulated the theory of ‘economy of words’ describing how monetary authorities have been engaging in communicative experiments to anchor people’s expectations and, respectively, shape their economic behavior [10, 11]. The canonical example of such communication strategy is ‘Whatever it takes’ speech by the President of the European Central Bank Mario Draghi who in the midst of the sovereign debt crisis in 2012 announced that even in the worst case scenario euro would be preserved [18].

With regard to status quo bias and inertia, policymakers might be also concerned about their reputation and how the public reacts to their actions. Here come also concerns about reelection which is determined by how public evaluates the capabilities of a politician and consequences of his/her decisions. All these considerations might lead policymakers to avoid risk-taking for socially beneficial reforms [8]. The same happens with a loss aversion bias which might just reflect public’s fear after a “hard fought” battle against inflation, for example, and does not represent the high weight to potential losses by politicians.

Furthermore, policy mistakes resulted from availability and representativeness biases might be alternatively explained by lack of knowledge or similar experiences in the past (for example, due to relatively short terms allowed for central bank and fiscal authority governors). Kahneman’s study confirms that expert skills are built up over time [13], but the average period of experience of fiscal and monetary economists is relatively short as compare to how frequently the financial crises or market bubbles and collapses occur: few governors might experience more than one crises to become more successful in managing macroeconomic instability.

Nonetheless, one might use the existing data on decision-making process to uncover behavioral patterns of policymakers. There is no universal formula for that, data-driven approach will be very case-specific, but the example that might outline this idea is as follows. In the study conducted by E. Meade and D. Sheets, researchers present evidence consistent with representativeness bias: voting behavior of governors of Federal Reserve System are affected by the regions they come from [7]. The researchers confirmed that representativeness bias in the American monetary sphere exists and even quantified it: a Fed governor coming from a district with higher (than national average) unemployment rate is more likely to oppose a tighter policy (which might have adverse effects on employment) by 2.4% than governors from districts with average unemployment rate. Such conclusions were made on a basis of statistical data analysis of 214 face-to-face meetings and Fed conferences.

Such data-driven approach might be incorporated not only in proving the existence of behavioral failures of policymakers, but also might help to minimize or even avoid them. Here come think tanks and academics that might conduct adversarial review of monetary and fiscal policies. At first, in the case of open, reliable, and transparent government data, economic forecasts and policy recommendations developed by independent think tanks and academic institutions might play a role of benchmark for policymaking choices. Going further, these think tanks and academics might become another core political institution. Such a transformation might be well illustrated by the Canadian case: there are major competing think tanks (C.D. Howe Institute, the Conference Board of Canada, the Fraser Institute, the Canada West Foundation, and the Centre for Policy Alternatives) that develop economic forecasts as well as provide ‘shadow budget’ plans and policy recommendations to the government that is transparent and accountable for the decisions they make [12].

Furthermore, cognitive biases of policymakers might be partially eliminated by rules-based policy framework subject to periodic modifications (but with full elimination of discretion). In the context of uncertainty, asymmetric information and all the behavioral biases discussed throughout the essay, it seems as an impossible task to distinguish whether a discretionary policy decision is optimal, efficient, socially beneficial, and is a result of sound judgement or it is a misleading policy practice caused by behavioral pathologies and asymmetry of perceived risks.

In conclusion, to summarize the points discussed above I would like to highlight once again that policymaking institutions, even the most sophisticated ones governed by mainly economists – central banks and fiscal authorities – are subject to the cognitive biases as all the other ordinary economic agents. The cognitive biases such as status quo bias, inertia, loss aversion, availability and representativeness biases are one of the most relevant cases of behavioral failures of policymaking institutions. On the contrary, poor policy outcomes caused by behavioral biases might need complementary explanations such

as conscious communication strategy, concern about reputation, lack of relevant experience etc. The possible option is case-specific data-driven approach. In order to reduce adverse impact of cognitive biases inherent to monetary and fiscal institutions, there should be open and reliable government data, very strong role of think tanks and academics providing adversarial review of policies as well as particular consideration to rule-based policy framework.

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