INTERNATIONAL FINANCE - SPRING 2022

Compliance and Financial Regulation

Caroline Bradley[1]

Introduction

The first examples of (wilful) non-compliance we came across this semester related to non-compliance with sanctions measures (Standard Chartered and Unicredit Bank).[2] We have seen through these enforcement actions that US regulators have a reputation for being aggressive enforcers of the rules.[3] In December 2020 the CFTC

[1] Professor of Law, University of Miami School of Law, PO Box 248087, Coral Gables, FL, 33124, cbradley@law.miami.edu ; http://blenderlaw.com/ .

[2] In this section of the materials I am focusing on issues of non-compliance and misconduct by people working in finance, rather than on more general issues of economic crime and corruption, as to which see, e.g., Henry E. Hockeimer, Jr., FBI Establishes Anti-Corruption Team in Miami, National Law Review (Mar. 5, 2019); FinCen, Advisory on Human Rights Abuses Enabled by Corrupt Senior Foreign Political Figures and their Financial Facilitators (Jun. 12, 2018); House of Commons Treasury Committee, Economic Crime - Anti-money Laundering Supervision and Sanctions Implementation, HC 2010 (Mar. 8, 2019).

[3] For example, Early and Preble on fishing and whale hunting; the EU's concerns with extraterritorial enforcement of sanctions.

announced a settlement with Vitol Inc. (described as a significant participant in the oil derivatives market) with respect to claims of manipulative and deceptive conduct involving foreign corruption (bribes paid to employees of state owned entities in Brazil, Ecuador and Mexico for confidential information) including attempted manipulation of two S&P Global Platts physical oil benchmarks.[4] Credit Suisse has been involved in a number of recent scandals, including a criminal trial in Switzerland where it faces allegations of facilitation moneylaundering by Bulgarian clients,[5] its involvement with Archegos[6] and Greensill Capital,[7] two financial companies that collapsed, and the fallout from its employment of a banker who had stolen money from the bank's clients,[8] as well as its relationships with clients involved in a range of unethical and illegal activities.[9]

In 2018, Danske Bank was implicated in a moneylaundering scandal involving around €200 billion which flowed through the bank's Estonian branch between 2007-2015.[10] A significant number of the payments were suspicious. As a result of this scandal Danske Bank was excluded from Estonia,[11] and was investigated by the SEC,

---

[4] CFTC Orders Vitol Inc. to Pay $95.7 Million for Corruption-Based Fraud and Attempted Manipulation, Release No. 8326-20 (Dec. 3, 2020). The Department of Justivce announced a Deferred Prosecution Agreement at the same time. Department of Justice, Vitol Inc. Agrees to Pay Over $135 Million to Resolve Charges for Bribery Schemes in Latin America (Dec. 3, 2020).

[5] Sam Jones, Landmark Credit Suisse money laundering trial opens, Financial Times (Feb. 7, 2022).

[6] Tabby Kinder & Eric Platt, Archegos and banks in settlement talks amid block trades probe, Financial Times (Mar. 1, 2022).

[7] Eshe Nelson, Jack Ewing & Liz Alderman, The Swift Collapse of a Company Built on Debt, NY Times (Mar. 28, 2021, updated Apr. 12, 2021).

[8] Owen Walker, Credit Suisse loses case over banker who stole from billionaire clients, Financial Times (Mar. 23, 2022).

[9] David Pegg, Kalyeena Makortoff, Martin Chulov, Paul Lewis & Luke Harding, Revealed: Credit Suisse leak unmasks criminals, fraudsters and corrupt politicians, The Guardian (Feb. 20, 2022).

[10] The scandal came to light as a result of the actions of a whistleblower. Peter Briccetti, Danske Bank Whistleblower Nominated For Allard Prize for International Integrity (Sep. 18, 2020) at https://whistleblowersblog.org/2020/09/articles/whistleblower-news/danske-bank-whistleblower-nominated-for-allard-prize-for-international-integrity/.

[11] Martin Selsoe Sorensen, Estonia Orders Danske Bank Out After Money-Laundering Scandal, New York Times (Feb. 20, 2019).

US Department of Justice, and regulators in the UK, France and Denmark.[12] In December 2020, Danske Bank announced it had received a no-action letter from OFAC relating to the Estonian case.[13] Danske Bank focused on setting up a world class compliance system,[14] although the Swedish financial regulator found its initial action plan to be deficient.[15]

The European Banking Authority launched an investigation into whether the Estonian and Danish regulators breached their obligations under EU law relating to the Danske Bank AML issues,[16] but the investigation was closed shortly after it was initiated, without making any findings,[17] leading to criticisms of EU enforcement of AML rules.[18] In 2019 the EU Commission identified flaws in the EU system of AML systems relating to a lack of compliance, failures in governance, misalignment between risk appetite and risk management and negligence of group AML policies.[19] Here are some excerpts from the Commission's analysis:

In many of the cases assessed, credit institutions did not prioritise compliance with anti-money laundering/countering the financing of terrorism legislation in their policies. In some cases, although control systems were formally in place, no overall money laundering/terrorist financing risk assessment was conducted at either the level of individual entities or at group level. Furthermore, compliance departments were in some cases understaffed, or the compliance function was rarely involved in ultimate decision-making.

---

[12] Erik Sherman, Danske Bank Now Faces SEC Money Laundering Investigation, Fortune (Feb. 21, 2019).

[13] Danske Bank, No Action Letter received by Danske Bank A/S from the U.S. Department of the Treasury's Office of Foreign Assets Control related to the Estonia case, Company Announcement No. 12/2020 (Dec. 19, 2020).

[14] Dylan Tokar, Danske Bank Rebuilds Compliance Program After Money- Laundering Scandal, Wall Street Journal (Jan. 3, 2022).

[15] Finansispektionen Press Release, Danske Bank receives injunction to take remedial action (Oct. 20, 2021).

[16] European Banking Authority Press Release, EBA Opens Formal Investigation into Possible Breach of Union Law by the Estonian and Danish Competent Authorities Regarding Money-laundering Activities Linked to Danske Bank (Feb. 19, 2019).

[17] EBA, EBA closes investigation into possible breach of Union law by the Danish and Estonian supervisory authorities (Apr. 17, 2019).

[18] Jim Brundsen, EBA faces calls to reform after dropping Danske Bank probe, Financial Times (Apr. 28, 2019).

[19] EU Commission, Report on the Assessment of Recent Alleged Money Laundering Cases Involving EU Credit Institutions, COM (2019) 373 final (Jul. 24, 2019) at 3.

As a consequence of their failure to perform adequate customer due diligence, some credit institutions had insufficient understanding of their customers' actual operations and were ultimately unable to draw meaningful conclusions as to whether or not a customer's activity was suspicious. Many credit institutions had difficulties to determine the identity of the beneficial owners behind their customers due to the fact that identification is burdensome and beneficial ownership registers were not yet in place. In several cases, whereas the institutions were conducting business with a significant number of politically exposed persons, they were neither identified as such, nor treated as high-risk customers, in violation of national laws transposing the Anti-Money Laundering Directive. In other cases, shortcomings related to remote booking models rendered elements of transaction monitoring more difficult (for example, knowing the origins of orders and payments or identifying linked trades across different jurisdictions..). Finally, certain shortcomings could be identified as regards reporting to Financial Intelligence Units. For instance, in a specific case the number of alerts generated by automated monitoring systems was capped to a number that was considered appropriate in relation to the number of staff managing such alerts, whilst in other instances credit institutions did not have in place appropriate risk assessment tools to be able to analyse transactions. In most cases, the number of suspicious transaction reports filed was low – and the number of actionable suspicious transaction reports was even lower.

In a small number of cases examined, employees may have been directly involved in committing money laundering, or in assisting customers in committing the offence...In other cases, negligence related to anti-money laundering/countering the financing of terrorism controls made money laundering by customers possible or highly probable....

In most of the cases analysed, there was evidence of weaknesses with regard to one or more lines of defence, as well as weaknesses in the way those responsible in the different lines of defence interacted with each other. In the most serious cases, the first line of defence (business units) was practically non-existent, as the employees in the business origination did not fulfil basic obligations under anti-money laundering/countering the financing of terrorism framework, such as recognising or reporting suspicious types of customer and transactions. Often the second line of defence (risk management and compliance) also turned out to be inadequate, as it either did not correctly assess and mitigate weaknesses identified by the 'front line' employees or did not acknowledge compliance failures by 'front line' employees. In several cases, the third line (internal audit) seemed not to have adequately prioritised anti-money laundering/countering the financing of terrorism work, was not independent from the 'front line', or did not receive sufficient attention from senior management. Moreover, the resource allocation or responsiveness of the three lines of defence was often not commensurate to the levels of money laundering/terrorist financing risks to which the institution was exposed, or remained static (and therefore increasingly inadequate) despite the credit institution engaging in higher risk activities....

In several cases, the senior management of credit institutions was not sufficiently informed about failures related to compliance with anti-money laundering/countering the financing of terrorism requirements and money laundering risks, and hence unable to recognise and address failures in an adequate and timely manner. In some cases, the corporate culture promoted by senior management focused predominantly on profitability over compliance. Where internal investigations were conducted upon request of the senior management, they

were sometimes very limited in scope, although the level of risk should have triggered a much more comprehensive response. Failures in the role of senior management in large and complex credit institutions also resulted from a limited attention span of senior management for problems in smaller business units, despite the disproportionate amount of damage that would result for the credit institution as a consequence of anti-money laundering/countering the financing of terrorism issues arising in such business units....

The analysis of cases suggests that certain credit institutions may have actively pursued business models that are risky from an anti-money laundering/countering the financing of terrorism perspective. More specifically, it appears that some institutions engaged in high-risk business carried out directly in certain (especially third country) jurisdictions or originating from such jurisdictions, and based their business model almost exclusively on non-resident deposits without establishing commensurate anti-money laundering/countering the financing of terrorism policies and controls. In addition, in several of the cases significant exposures to anti-money laundering/countering the financing of terrorism risks appeared in the context of correspondent banking services, whilst institutions did not have dedicated or sufficiently clear anti-money laundering/countering the financing of terrorism policies for such business. While pursuing business opportunities, several credit institutions were willing to accept risky customers without appropriately managing them, including politically exposed persons and commercial entities where the beneficial owner could not be identified. In some cases, credit institutions engaged in anonymous transactions or non-face-to-face business relationships without undertakinging adequate due diligence. In other instances, some credit institutions appear to have been promoting an aggressive business model of on-boarding clients and processing transactions on the basis of deliberately limited customer due diligence...

In some instances, it appears that the parent company had difficulties in forming an accurate and complete overview of the existing risks in the group. On several occasions, this seems to have prevented local anti-money laundering/countering the financing of terrorism-related problems from being taken into account in the context of wider group actions. In a few cases, the policies and control processes of acquired credit institutions (often on a cross-border basis) were not aligned in a timely manner to the group-wide risk management framework, with IT and reporting systems remaining separate and with no integration or inter-connection with the group's system. Furthermore, in certain cases, problems in branches seem to have been discarded at group level on the basis of proportionality considerations related to the size of local peripheral group entities, while seemingly neglecting the reputational impact that even peripheral entities and activities might have on the whole group.

The Commission also looked at the regulators responsible for enforcing AML rules and noted some instances of understaffing, or a lack of experience or knowledge on the part of the relevant staff. There was sometimes what was described as a "climate of trust" between the supervisor and supervised entities, and there were cases where, even though violations were discovered, no sanctions or supervisory action followed other than informal communications. Supervision of cross border groups was not comprehensive, rather each part of the group was supervised where it was located.

Following this report, in 2020 the EU Commission published an Action Plan for a

Comprehensive Union Policy on Preventing Money Laundering and Terrorism Financing, proposing a stronger AML/CFT system for the EU:

Subject to an impact assessment, including of impacts on fundamental rights, an integrated EU AML/CFT system should be put in place. Building on the example of the reforms introduced in the field of prudential banking regulation and supervision, the system should rest on a harmonised rulebook and an EU-level supervisor that works in close cooperation with national competent authorities, with a view to ensuring high-quality and consistent supervision across the Single Market. This should be coupled with the establishment of an EU support and coordination mechanism for FIUs, which enhances their effectiveness, and with the interconnection of the national centralised bank account registries, which will speed up cross-border access by law enforcement authorities and FIUs to bank account information.[20]

In July 2021 the EU Commission published a package of proposed legislative measures on money-laundering and countering the financing of terrorism.[21] A major feature of the package is a proposal for a new EU Anti-Moneylaundering Authority (AMLA):

...the Authority will become a centrepiece of an integrated AML/CFT supervisory system, consisting of the Authority itself and the national authorities with an AML/CFT supervisory mandate (hereinafter 'the supervisor authorities'). By directly supervising and taking decisions towards some of the riskiest cross-border financial sector obliged entities, the Authority will contribute directly to preventing money laundering and terrorism financing in the Union. During the last years, several incidents of a lack of proper implementation by firms and/or of adequate countermeasures taken by supervisors have been for discussion in the public domain. The establishment of direct European supervision of those entities that bear a high ML/FT risk will close these loopholes in particular for cross-border supervision. At the same time, it will coordinate national supervisory authorities and assist them to increase their effectiveness in enforcing the single rulebook and ensuring homogenous and high quality supervisory standards, approaches and risk assessment methodologies

All recent major money laundering cases reported in the EU had a cross-border dimension. The detection of these financial movements is however left to the national FIUs[22] and to cooperation among them. While this reflects the operational independence and autonomy of FIUs, the absence of a common structure to underpin this cooperation leads to situations where joint analyses are not performed for lack of common tools or resources. These divergences hamper cross-border cooperation, and thereby reduce the capacity to detect money laundering and

---

[20] EU Commission Communication, Action Plan for a Comprehensive Union Policy on Preventing Money Laundering and Terrorism Financing, C (2020) 2800 final (May 7, 2020).

[21] EU Commission, Anti-money laundering and countering the financing of terrorism legislative package (Jul 20, 2021) at https://ec.europa.eu/info/publications/210720-anti-money-laundering-countering-financing-terrorism_en

[22] Financial Intelligence Units.

terrorism financing early and effectively. This results in a fragmented approach that is exposed to misuse for money laundering and terrorist financing and that cannot timely identify trends and typologies at Union level...

The new Authority should also play a vital role in improving the exchange of information and cooperation between FIUs. The Authority will serve as a support and coordination hub assisting their work on, inter alia, joint analyses of Suspicious Transaction Reports and Suspicious Activity Reports with significant cross-border footprint, and providing stable hosting of the FIU.net platform. Moreover, the Authority will enable a development of common reporting templates and standards to be used by EU FIUs...

With the objective of ensuring a more effective and less fragmented protection of the Union's financial framework, a limited number of the riskiest obliged entities should be directly supervised by the Authority. As ML/TF risks are not proportional to the size of the supervised entities, other criteria should be applied to identify the most risky entities. In particular, two categories should be considered: high-risk cross-border credit and financial institutions with activity in a significant number of Member States, selected periodically; and, in exceptional cases, any entity whose material breaches of applicable requirements are not sufficiently or in a timely manner addressed by its national supervisor. Those entities would fall under the category of 'selected obliged entities'...

The first category of credit and financial institutions, or groups of such institutions should be assessed every three years, based on a combination of objective criteria related to their cross-border presence and activity, and criteria related to their inherent ML/FT risk profile. Only large complex financial groups present in a number of Member States that could be more efficiently supervised at Union level should be included in the selection process. With respect to credit institutions, minimal cross-border presence for inclusion in the selection process should be based on the number of subsidiaries and branches in different Member States, because risky banking activities of significant volume require a local presence in a form of an establishment. Other financial sector entities may, in contrast, carry out activities that can be sufficiently risky from an ML/TF perspective by means of direct provision of services, for example via a network of agents, but may not have established subsidiaries or branches in a large number of Member States. Therefore, applying the same cross-border criteria, that is to say the one related to freedom of establishment, would result in scoping out large financial sector entities that can have a significant risk profile in a number of Member States, without being established there. Since the volume of activities via direct provision of services is generally smaller than the volume of activities carried out in a branch or a subsidiary, it is appropriate to consider only groups that are established in at least two Member States, but provide services directly or via a network of agents in at least eight more Member States...

In order to ensure that only the riskiest obliged entities among those with significant cross-border operations are supervised directly at the level of the Union, the assessment of their inherent risk should be harmonised. Currently, there are various national approaches and supervisory authorities use distinct benchmarks for assessment and classification of inherent ML/TF risk of obliged entities. Using these national methodologies for selection of entities for direct supervision at Union level could lead to a different playing field among them. Therefore, the Authority should be empowered to develop regulatory technical standards laying out a harmonised methodology and benchmarks for categorising the inherent ML/TF risk as low,

medium, substantial, or high. The methodology should be tailored to particular types of risks and therefore should follow different categories of obliged entities which are financial institutions in accordance with the Regulation of the European Parliament and of the Council on the prevention of the use of the financial system for the purposes of money laundering or terrorist financing... That methodology should be sufficiently detailed and should establish specific quantitative and qualitative benchmarks considering at least the risk factors related to types of customers served, products and services offered, and geographical areas, including third country jurisdictions that obliged entities operate in or are related to. Specifically, each assessed obliged entity would have its inherent risk profile classified in each Member State where it operates in a manner consistent with the classification of any other obliged entity in the Union. The quantitative and qualitative benchmarks would allow such classification to be objective and not dependent on the discretion of a given supervisory authority in a Member State, or the discretion of the Authority.[23]

The EU Commission has also focused on encouraging compliance with sanctions measures. For example, the Commission publishes a Sanctions Map to facilitate compliance,[24] and in a Communication in 2021 the Commission wrote:

EU sanctions are most effective when information about their impact is promptly available. In 2021, the Commission will develop a database, the Sanctions Information Exchange Repository. This will enable prompt reporting and exchange of information between Member States and the Commission on the implementation and enforcement of sanctions. The Commission will consider obtaining specialised information, including data collected by EU agencies and bodies. The Commission will work in coordination with the High Representative as appropriate. Moreover, the Commission will assess the need to review existing reporting obligations for Member States.

In parallel to the adoption of this Communication, the Commission is setting up an expert group of representatives of Member States on sanctions and extra-territoriality. Representatives of the European External Action Service shall be invited to assist to the meetings of the Group. The group's mandate will cover issues related to the technical implementation of EU sanctions and of Regulation (EC) No 2271/96 (Blocking Statute)..

Further coordination on certain cross-border sanctions-related matters is needed. Currently, Member States' authorities that deal with requests for authorisation from EU businesses or humanitarian operators that are active in multiple Member States are often not informed of parallel requests to, or decisions issued by, other national authorities. This could result in the uncoordinated enforcement of EU sanctions and forum shopping. The Commission will work with Member States to set up a system to centralise notifications and the dissemination of information across Member States, and to help coordinate Member States' replies, in full compliance with the division of competences in the treaties.

---

[23] EU Commission, Proposal for a Regulation establishing the Authority for Anti-Money Laundering and Countering the Financing of Terrorism, COM (2021) 421 final (Jul. 20, 2021).

[24] https://sanctionsmap.eu/#/main.

The Commission will also discuss the implementation of EU sanctions with Member States to ensure a harmonised approach in this regard. Applicable standards and respective best practices could also be discussed in the expert group mentioned above...
In its role of guardian of the treaties, the Commission monitors and collects information on possible breaches of EU law by Member States. To address the confidential nature of information on violations of EU sanctions and potential implications for those who report illicit activities, the Commission will create a dedicated tool to facilitate anonymous reporting.
In the first half of 2022, the Commission will draw up a roadmap (including criteria and a timetable) for moving from detection of systematic non-compliance with EU sanctions to action before the Court of Justice of the European Union.
Finally, the Commission will work with Member States, including within the framework of the expert group on sanctions and extra-territoriality, to ensure that national penalties for breaching EU sanctions are effective, proportionate and dissuasive.[25]

In 2021 the Financial Conduct Authority, a UK financial regulator, began criminal proceedings against Natwest plc, a large UK bank, for violation of AML rules with respect to cash deposits amounting to £264 million.[26] This was the first time the FCA used its criminal moneylaundering powers. Although the FCA could have sought to remove the bank's license to operate as a bank it chose not to do so.[27] Fitch Ratings stated that the action did not immediately affect Natwest's rating, but that it "highlights the tougher stance that various stakeholders, including authorities in the UK and elsewhere, are taking against banks with governance failings."[28] In December 2021, Natwest was fined £264.8 million after pleading guilty to the charges of failing to comply with money laundering regulations.[29] In her sentencing remarks, Mrs Justice Cockerill noted that although the bank had policies and procedures in place, and the overall design of the bank's monitoring systems were in line with industry guidance, there were gaps. For example, the "policies and procedures did not address the need for staff to guard against overreliance being placed on relationship managers when considering suspicious activity on a customer account," and there were weaknesses in the

[25] EU Commission Communication, the European Economic and Financial System: Fostering Openness, Strength and Resilience, COM(2021) 32 final (Jan. 19, 2021).

[26] FCA, FCA starts criminal proceedings against NatWest Plc (Mar. 16, 2021).

[27] Nicholas Megaw & Caroline Binham, FCA brings money laundering charges against NatWest, Financial Times (Mar. 16, 2021).

[28] Fitch Ratings, NatWest Case Shows Bank Governance Is Increasingly in Spotlight (Mar. 17, 2021).

[29] Financial Conduct Authority, NatWest fined £264.8 million for anti-money laundering failures (Dec. 13, 2021).

automated transaction monitoring system such that cash deposits were interpreted by the system as cheque deposits, and that for periods of time there were no cash - specific rules or rules for high risk customers.[30] The relevant customer had wrongly been identified as low risk in part because its business was incorrectly described as 'wholesale of metals and metal ores' rather than 'precious metals.'[31] After previous compliance failures the bank had attempted to improve its systems, but the office responsible for investigations was a new office lacking experience and emphasising dealing with alerts quickly rather than thoroughly. Although large amounts of cash were at times being deposited these were not always notified: “The non-notifiers included branches/centres which received sums between £12 and 43 million and situations which included the deposit of such large sums of cash that they were brought in in black bin bags, which tore because of their weight, and sums so large that the bank’s safes were inadequate to store them.”[32] In addition to the fine, Natwest was also subjected to a consfication order with respect to the fees and charges gained from the relevant account relationship, and required to pay the FCA’s costs.[33]

In addition to sanctions-busting and money laundering there have been a number of transnational misconduct/non-compliance case involving benchmarks, such as Libor and the S&P Global Platts physical oil benchmarks referred to above. For example, in June 2012 the US Department of Justice,[34] the CFTC,[35] and the UK’s

---

[30] R v National Westminster Bank, Southwark Crown Court, Sentencing Remarks of Mrs Justice Cockerill (Dec. 13, 2021).

[31] For some reason the original description of the business as precious metals was changed.

[32] Sentencing remarks, note 30.

[33] *Id.*

[34] Department of Justice, Barclays Bank PLC Admits Misconduct Related to Submissions for the London Interbank Offered Rate and the Euro Interbank Offered Rate and Agrees to Pay $160 Million Penalty (Jun. 27, 2012) at http://www.justice.gov/opa/pr/2012/June/12-crm-815.html .

[35] CFTC Orders Barclays to pay $200 Million Penalty for Attempted Manipulation of and False Reporting concerning LIBOR and Euribor Benchmark Interest Rates (Jun. 27, 2012). Order at http://www.cftc.gov/ucm/groups/public/@lrenforcementactions/documents/legalpleading/enfbarclaysorder062712.pdf (“Over a period of several years, commencing in at least 2005, Barclays PLC, Barclays Banle and Barclays Capital, by and through their agents, officers and employees located in at least New York, London and Tokyo, repeatedly attempted to manipulate and made false, misleading or knowingly inaccurate submissions concerning two global benchmark interest rates, the British Banleers' Association's ("BBA") London Interbank Offered Rate ("LIBOR") and the European Banking Federation's ("EBF") Euro Interbank Offered Rate ("Euribor"). “)

Financial Services Authority[36] announced settlements of enforcement actions against Barclays Bank with respect to manipulations of Libor and Euribor rates. Barclays submitted quotes to the US dollar Libor and Euribor setting processes based on requests of its interest rate derivatives dealers, tried to influence the submissions of other banks to the Euribor (and to some extent to the Libor) setting process, and made submissions to the Libor setting process which were designed to reduce negative media perception. The Financial Services Authority said that Barclays did not have any specific systems or controls relating to the Libor and Euribor setting processes until December 2009. Before these announcements with respect to enforcement much speculation in the press about abuses of the Libor setting process had focused on the financial crisis, and the idea that during the crisis banks were reluctant to quote accurate rates for Libor because this would suggest that other market participants lacked confidence in their financial health. However, Barclays derivatives traders made requests to those responsible for making rate submissions going back as far as the beginning of 2005. The FSA's final notice cited emails and instant messages by the traders, and tracked the extent to which submissions seem to have followed the email requests. Strikingly some of the cases of manipulation involved requests by traders at firms other than Barclays.

Other enforcement actions also related to benchmark regulation to benefitr firms other than the manipulators' employers. For example, in discussing enforcement action with respect to Rabobank, [37] then CFTC Chair, Gary Gensler, said:

> With today's settlement, the CFTC has shown – now for the fifth time – how banks have pervasively rigged key interest rate benchmarks, such as LIBOR and Euribor.
> Unfortunately, we once again see how the public trust can be violated through bad actors readily manipulating benchmark interest rates.
> Through hundreds of manipulative acts spanning six years, in six offices, and on three continents, more than two dozen Rabobank employees, including a senior manager, manipulated, attempted to manipulate and falsely reported crucial reference rates in global financial markets. Rabobank employees also aided and abetted other banks to manipulate benchmark interest rates.
> I wish I could say that this won't happen again, but I can't. LIBOR and Euribor are not sufficiently anchored in observable transactions. Thus, they are basically more akin to fiction than fact. That's the fundamental challenge so sharply revealed by Rabobank and our prior

[36] Financial Services Authority, Barclays fined £59.5 million for significant failings in relation to LIBOR and EURIBOR (Jun. 27, 2012). The FSA was replaced by the Financial Conduct Authority and the Prodential Regulation Authority.

[37] *See* CFTC Order with respect to Rabobank (Oct. 29, 2013) at http://www.cftc.gov/ucm/groups/public/@lrenforcementactions/documents/legalpleading/enfrabobank102913.pdf ; FCA Final Notice with respect to Rabobank (Oct. 29, 2013) at http://fca.org.uk/static/documents/final-notices/rabobank.pdf .

cases.
This fifth instance of benchmark manipulative conduct highlights the critical need to find replacements for LIBOR and Euribor – replacements truly anchored in observable transactions. Though addressing governance and conflicts of interest regarding benchmarks is critical, that will not solve the lack of transactions in the market underlying these benchmarks.
That is why the work of the Financial Stability Board to find alternatives and consider potential transitions to these alternatives is so important. The CFTC looks forward to continuing to work with the international community on much needed reforms.[38]

In June 2013 RBS entered into a deferred prosecution agreement with the US Department of Justice with respect to charges of wire fraud and price fixing.[39] This was "the first time a financial services firm was ever held criminally liable under antitrust laws for a trader-based market manipulation scheme." [40]

Within domestic regulatory regimes compliance is a perennial issue,[41] but firms carrying on business in multiple jurisdictions through subsidiaries and branches raise some additional questions about the possibility of effective cross-border supervision, as we can see from the EU AML example and the benchmarks example. And questions about the effectiveness of cross border regulation can arise in the context of a broad range of non-compliant behavior from AML and sanctions violations to corruption and other matters.[42] A 2021 report from the OECD focuses on "lawyers, accountants, financial institutions and other professionals who help engineer the legal and financial structures seen in complex tax evasion and financial crimes," that the report describes as "professional enablers."[43] The report distinguishes between these professional

---

[38] Statement of Chairman Gary Gensler on Settlement Order against Rabobank (Oct. 29, 2013) at http://www.cftc.gov/PressRoom/SpeechesTestimony/genslerstatement102913 ;

[39] *See* US v RBS Deferred Prosecution Agreement at http://www.justice.gov/atr/cases/f292500/292555.pdf

[40] John Terzaken, A New Era of Antitrust Enforcement, New York Times Dealbook (Feb. 18, 2014).

[41] See, e.g., Mark Egan, Gregor Matvos & Amit Seru, *The Market for Financial Advisor Misconduct*, 127 JOURNAL OF POLITICAL ECONOMY 233 (2019) (noting that 7% of financial advisors have misconduct records).

[42] *Cf.* High Level Panel on International Financial Accountability, Transparency and Integrity for Achieving the 2030 Agenda, Report on Financial Integrity for Sustainable Development (Feb. 2021) at https://www.moneylaunderingnews.com/wp-content/uploads/sites/12/2021/03/FACTI_Panel_Report.pdf (arguing for a global pact for financial integrity for sustainable development).

[43] OECD, Ending the Shell Game: Cracking down on the Professionals Who Enable Tax and White Collar Crimes (2021). Although the report is primarily focused on tax crimes, "it is also intended to be helpful to other law enforcement authorities, given the links between tax offences and other financial

enablers (the subject of the report) and professionals who are experts in finding legal loopholes. Here the report says: "[t]he possibility of using "grey areas of the law", while not technically illegal, should be limited by jurisdictions through the enhancement of their tax legislation and by fostering international co-operation."[44]

Examples of transnational non-compliance raise some additional questions about fixing the culture of finance. A concern about the culture of finance has been expressed in the US,[45] as well as in the OECD, and in other markets.[46] Regulatory responses to the issue of misconduct range from rules designed to limit the possibility of misconduct, such as reforms to benchmarks,[47] to regimes for regulating senior employees in financial institutions.[48]

In 2012, the UK established a Parliamentary Commission on Banking Standards to examine the culture of banking.[49] The Commission carried out a wide-ranging review of banking in the UK, was critical of banks, regulators, governments and investors, and made a number of suggestions for reforms. One of the suggestions involved increasing

---

crimes such as money laundering or corruption and the commonalities in the ways these crimes are committed, and particularly insofar as it outlines the importance of multi-agency and multilateral action." *Id*. at 8.

[44] *Id.* at 11.

[45] See, e.g., Kevin J. Stiroh, Executive Vice President, Federal Reserve Bank of New York, The Complexity of Culture Reform in Finance, Remarks at the 4th Annual Culture and Conduct Forum for the Financial Services Industry, London (Oct. 4, 2018).

[46] See, e.g., High-level summary: BCBS SIG industry workshop on governance, culture and conduct at https://www.bis.org/bcbs/events/20181107_sig_summary.htm ; Financial Stability Board, Strengthening Governance Frameworks to Mitigate Misconduct Risk: A Toolkit for Firms and Supervisors (Apr. 2018).

[47] Regulation 2016/1011 on Indices Used as Benchmarks in Financial Instruments and Financial Contracts or to Measure the Performance of Investment Funds, O.J. No L 171/1 (Jun. 29, 2016). Recital 1 of the Regulation states: "The pricing of many financial instruments and financial contracts depends on the accuracy and integrity of benchmarks. Serious cases of manipulation of interest rate benchmarks such as LIBOR and EURIBOR, as well as allegations that energy, oil and foreign exchange benchmarks have been manipulated, demonstrate that benchmarks can be subject to conflicts of interest. The use of discretion, and weak governance regimes, increase the vulnerability of benchmarks to manipulation. Failures in, or doubts about, the accuracy and integrity of indices used as benchmarks can undermine market confidence, cause losses to consumers and investors and distort the real economy. It is therefore necessary to ensure the accuracy, robustness and integrity of benchmarks and of the benchmark determination process."

[48] For example, the UK's Senior Managers and Certification Regime. See https://www.fca.org.uk/firms/senior-managers-certification-regime .

[49] See Changing Banking for Good, Report of the Parliamentary Commission on Banking Standards Vol 1, HL Paper 27-1, HC 175-1 Jun. 2013).

competition in banking, in part to reduce reliance on a small number of institutions (which could be seen as too big to fail). At the same time, the Commission argued that seeing banking as a profession could improve the situation. What do you think of this idea? Does the Commission have too much faith in the idea of professional self-regulation? Traditionally the idea of a (learned) profession has involved two main components: knowledge which was not generally available, combined with an expressed commitment to high standards of behavior.

In the twenty-first century there are reasons to be skeptical of these two characteristics of professions: professionals are subject to increasing competition from people outside the profession (for example, legal services outsourcing), and in many ways professional activities seem hard to distinguish from business activities which may undermine the idea of high standards.

In the US, scholars of the legal profession have thought about how professional self-regulation should be adapted to fit new models of law practice.[50]

Milton Regan has described law firm ethics as "nested":[51]

... we can conceptualize the components that influence ethical behavior as nested inside one another. The first level is the individual who engages in decision-making, who may receive advice from colleagues who act informally to provide ethical guidance. The second level, which provides the larger context for the first, is a firm's ethical infrastructure, which attempts in various ways to shape and channel that behavior. The third level, which provides the larger context for the first two, is a firm's ethical culture. This can prompt an individual to embrace ethical values to which a firm is committed, which provides intrinsic motivation to comply with the procedures and policies that make up the firm's infrastructure. ...

The ethical culture in a law firm thus provides the larger context in which individual action and the firm's ethical infrastructure operate. Ideally, it communicates that a firm is committed to practicing law consistently with the values reflected in the professional responsibilities of lawyers. While this can be crucial in strengthening ethical behavior, there still may be limits to its effectiveness. First, members of an organization are more likely to be receptive to its ethical culture as they identify more with the organization. An expanded sense of identity more closely aligns individuals' self- interest with that of the organization, so that they see their own success

---

[50] *See, e.g.*, Ted Schneyer, *On Further Reflection: How "Professional Self-Regulation" Should Promote Compliance with Broad Ethical Duties of Law Firm Management*, 53 ARIZ. L. REV. 577, 589 (2011) (" Since the vast majority of lawyers in 1908 practiced alone and had few, if any, lay employees, the absence of references to firms or firm governance in the 1908 Canons was hardly surprising. By the 1980s, however, law practice was very different. Two-thirds of the bar practiced in multi-lawyer workplaces, and well over half the lawyers in private practice worked in multi-lawyer firms. Many firms had branch offices, making intra-firm coordination both more difficult and more important. The ratios of associates to partners had also risen markedly, underscoring the need for supervision. And firms were hiring more nonlawyers who required training and supervision, including lay administrators." (Footnotes omitted))

[51] Milton C. Regan,, Jr. *Nested Ethics: A Tale of Two Cultures*, 42 HOFSTRA L. REV. 143 (2013).

as tied to the success of the larger entity. Prompting this identification, however, can be a challenge for a contemporary law firm. Most firms are extraordinarily fragile, vulnerable to the departure of their most profitable partners in the lateral market. This fragility may make partners feel that it is hazardous to act as if their long-term self-interest is tied to that of the firm. In addition, competitive pressures now prompt many firms to terminate lawyers who are not performing at a level that the firm deems adequate. This heightened vulnerability also can prevent the formation of any deep sense of attachment to a firm.
A second potential limit to the effectiveness of efforts to promote an ethical culture is that when individuals in an organization think of ethics, what tends to come to mind is behavior broader than the type that is the focus of an ethics program. For members of an organization, ethics relates most prominently to how fairly the organization treats the people who work there. Research indicates that there is a strong connection between this assessment and ethical attitudes and behavior. The greater the perception of fairness, the more credible an organization's professed commitment will be to ethical values and the more successful it will be in prompting its members to identify with it. This directs attention to policies and practices that we may not even think of as relating to ethics. They include matters such as promotion, compensation, and whether people who are generous or selfish tend to get ahead in the organization. These issues relate to the broader culture of an organization, which in turn affects the ability to promote an ethical culture. We therefore can conceptualize organizational culture as an additional component to our model within which the others are nested..

Here is an excerpt from the **Report of the Parliamentary Commission on Banking Standards** :[52]

Our approach

The UK banking sector's ability both to perform its crucial role in support of the real economy and to maintain international pre-eminence has been eroded by a profound loss of trust born of profound lapses in banking standards. The Commission makes proposals to enable trust to be restored in banking. These proposals have five themes:
- making individual responsibility in banking a reality, especially at the most senior levels;
- reforming governance within banks to reinforce each bank's responsibility for its own safety and soundness and for the maintenance of standards;
- creating better functioning and more diverse banking markets in order to empower consumers and provide greater discipline on banks to raise standards;
- reinforcing the responsibilities of regulators in the exercise of judgement in deploying their current and proposed new powers; and
- specifying the responsibilities of the Government and of future Governments and Parliaments.

No single change, however dramatic, will address the problems of banking standards. Reform across several fronts is badly needed, and in ways that will endure when memories of recent crises and scandals fade.

---

[52] Report of the Parliamentary Commission on Banking Standards, Changing Banking for Good, Vol. 1, HL Paper 27-I, HC 175 -I (Jun. 2013).

Making individual responsibility a reality

The problem

Too many bankers, especially at the most senior levels, have operated in an environment with insufficient personal responsibility. Top bankers dodged accountability for failings on their watch by claiming ignorance or hiding behind collective decision-making. They then faced little realistic prospect of financial penalties or more serious sanctions commensurate with the severity of the failures with which they were associated. Individual incentives have not been consistent with high collective standards, often the opposite.

A new framework for individuals

The Approved Persons Regime has created a largely illusory impression of regulatory control over individuals, while meaningful responsibilities were not in practice attributed to anyone. As a result, there was little realistic prospect of effective enforcement action, even in many of the most flagrant cases of failure. The Commission proposes a new framework for individuals with the following elements:

- a Senior Persons Regime, which would ensure that the key responsibilities within banks are assigned to specific individuals, who are made fully and unambiguously aware of those responsibilities and made to understand that they will be held to account for how they carry them out;
- a Licensing Regime alongside the Senior Persons Regime, to apply to other bank staff whose actions or behaviour could seriously harm the bank, its reputation or its customers;
- the replacement of the Statements of Principles and the associated codes of practice, which are incomplete and unclear in their application, with a single set of Banking Standards Rules to be drawn up by the regulators; these Rules would apply to both Senior Persons and licensed bank staff and a breach would constitute grounds for enforcement action by the regulators.

Incentives for better behaviour

Remuneration has incentivised misconduct and excessive risk-taking, reinforcing a culture where poor standards were often considered normal. Many bank staff have been paid too much for doing the wrong things, with bonuses awarded and paid before the long-term consequences become apparent. The potential rewards for fleeting short-term success have sometimes been huge, but the penalties for failure, often manifest only later, have been much smaller or negligible. Despite recent reforms, many of these problems persist.

The Commission proposes a radical re-shaping of remuneration for Senior Persons and licensed bank staff, driven by a new Remuneration Code, so that incentives and disincentives more closely reflect the longer run balance between business risks and rewards. The main features of the redesign are as follows:

- much more remuneration to be deferred and, in many cases, for much longer periods of up to 10 years;
- more of that deferred remuneration to be in forms which favour the long-term performance and soundness of the firm, such as bail-in bonds;
- the avoidance of reliance on narrow measures of bank profitability in calculating remuneration, with particular scepticism reserved for return on equity;
- individual claims on outstanding deferred remuneration to be subject to cancellation in the light

of individual or wider misconduct or a downturn in the performance of the bank or a business area; and
- powers to enable deferred remuneration to Senior Persons and licensed individuals, as well as any unvested pension rights and entitlements associated with loss of office, to be cancelled in any case in which a bank requires direct taxpayer support.

A new approach to enforcement against individuals

A more effective sanctions regime against individuals is essential for the restoration of trust in banking. The current system is failing: enforcement action against Approved Persons at senior levels has been unusual despite multiple banking failures. Regulators have rarely been able to penetrate an accountability firewall of collective responsibility in firms that prevents actions against individuals. The patchy scope of the Approved Persons Regime, which has left people, including many involved in the Libor scandal, beyond effective enforcement.

The Commission envisages a new approach to sanctions and enforcement against individuals:
- all key responsibilities within a bank must be assigned to a specific, senior individual. Even when responsibilities are delegated, or subject to collective decision making, that responsibility will remain with the designated individual;
- the attribution of individual responsibility will, for the first time, provide for the full use of the range of civil powers that regulators already have to sanction individuals. These include fines, restrictions on responsibilities and a ban from the industry;
- the scope of the new licensing regime will ensure that all those who can do serious harm are subject to the full range of civil enforcement powers. This is a broader group than those to whom those powers currently extend;
- in a case of failure leading to successful enforcement action against a firm, there will be a requirement on relevant Senior Persons to demonstrate that they took all reasonable steps to prevent or mitigate the effects of a specified failing. Those unable to do so would face possible individual enforcement action, switching the burden of proof away from the regulators; and
- a criminal offence will be established applying to Senior Persons carrying out their professional responsibilities in a reckless manner, which may carry a prison sentence; following a conviction, the remuneration received by an individual during the period of reckless behaviour should be recoverable through separate civil proceedings.

Reforming governance to reinforce individual responsibility

The financial crisis, and multiple conduct failures, have exposed serious flaws in governance. Potemkin villages were created in firms, giving the appearance of effective control and oversight without the reality. Non-executive directors lacked the capacity or incentives to challenge the executives. Sometimes those executives with the greatest insight into risks being added to balance sheets were cut off from decision-makers at board level or lacked the necessary status to speak up. Poor governance and controls are illustrated by the rarity of whistle-blowing, either within or beyond the firm, even where, such as in the case of Libor manipulation, prolonged and blatant misconduct has been evident. The Commission makes the following recommendations for improvement:
- individual and direct lines of access and accountability to the board for the heads of the risk,

compliance and internal audit functions and much greater levels of protection for their independence;
- personal responsibility for each individual director for the safety and soundness of the firm and a Government consultation on amending the Companies Act to prioritise financial safety over shareholder interests in the case of banks;
- direct personal responsibility on the Chairman to ensure the effective operation of the board, including effective challenge by non-executives, and on the Senior Independent Director, supported by the regulator, to ensure that the Chairman fulfils this role; and
- individual responsibility for a named non-executive director, usually the Chairman, to oversee fair and effective whistle-blowing procedures, and to be held accountable when an individual suffers detriment in consequence of blowing the whistle....

Reinforcing the responsibilities of the regulators

Serious regulatory failure has contributed to the failings in banking standards. The misjudgement of the risks in the pre-crisis period was reinforced by a regulatory approach focused on detailed rules and process which all but guaranteed that the big risks would be missed. Scandals relating to mis-selling by banks were allowed to assume vast proportions, in part because of the slowness and inadequacy of the regulatory response.

Our proposed emphasis on individual responsibility within banks needs to be matched by the replacement of mechanical data collection and box ticking by a much greater emphasis on the exercise of judgement by the regulators, supported by more effective oversight and empowerment tools. In particular:
- supervisors need to be close enough, and have a detailed enough understanding, of businesses to take swift decisions based on up-to-date information, rather than belated actions with the benefit of hindsight;
- the most senior regulatory staff should be expected to use judgement, rather than relying on procedures, and to take direct personal responsibility for ensuring that their engagement with individual banks, and the CEO, Chairman and the Board in particular, is securing the information required best to assess risk. They should expect to be held accountable, ultimately to Parliament, for this crucial role;
- a new tool proposed by the Commission, "special measures", will provide for the deployment of a broader range of regulatory powers when the FCA and PRA are concerned that systemic weaknesses of leadership, risk management and control leave a bank particularly prone to standards failures;
- regulators need to remove obstacles to a more competitive market in banking, including through steps to support the development of a more diverse banking market;
- regulators should identify the risks to a judgement-based approach from overly prescriptive international rule books and ensure that Parliament is kept fully informed of them; and
- there should be mandatory dialogue between supervisors and external auditors and a separate set of accounts for regulatory purposes.

The responsibilities of Governments and Parliaments

There were many players in the development of the crisis in banking that has unfolded since 2007. The behaviour of bankers was appalling, but regulators, credit ratings agencies,

auditors, governments, many market observers and many individual bank customers in their approach to borrowing created pressures in the same, and wrong, direction. Governments have a particular responsibility, many of them having been dazzled by the economic growth and tax revenues promised from the banking sector. Implementing the recommendations of the Commission would signal a fresh approach....

Banks have a crucial role in the economy. Banking can make an immense contribution to the economic well-being of the United Kingdom, by serving consumers and businesses, and by contributing to the United Kingdom's position as a leading global financial centre. The loss of trust in banking has been enormously damaging; there is now a massive opportunity to reform banking standards to strengthen the value of banking in the future and to reinforce the UK's dominant position within the global financial services industry. A reformed banking industry with higher levels of standards has the potential, once again, to be a great asset to this country...

The restoration of trust in banking is essential not just for banks. It is essential to enable the industry better to serve the needs of the real economy and to contribute effectively to the UK's role as a global financial centre...

The UK is a global financial centre, but a medium-sized economy. The benefits of being a global financial centre are very important in terms of jobs, investment, tax revenue and exports. In finance, the UK is a world leader. But being a global financial centre with a medium-sized wider economy also poses risks, as was seen in the bail-outs and huge injections of taxpayers' money which took place during the financial crisis. It is essential that the risks posed by having a large financial centre do not mean that taxpayers or the wider economy are held to ransom. That is why it is right for the UK to take measures, some already taken or in prospect, which not only protect the UK's position as a global financial sector, but also protect the UK public and economy from the associated risks....

Banking history is littered with examples of manipulative conduct driven by misaligned incentives, of bank failures born of reckless, hubristic expansion and of unsustainable asset price bubbles cheered on by a consensus of self-interest or self-delusion. An important lesson of history is that bankers, regulators and politicians alike repeatedly fail to learn the lessons of history: this time, they say, it is different. Had the warnings of past failures been heeded, this Commission may not have been necessary.,,,

One of the most dismal features of the banking industry to emerge from our evidence was the striking limitation on the sense of personal responsibility and accountability of the leaders within the industry for the widespread failings and abuses over which they presided. Ignorance was offered as the main excuse. It was not always accidental. Those who should have been exercising supervisory or leadership roles benefited from an accountability firewall between themselves and individual misconduct, and demonstrated poor, perhaps deliberately poor, understanding of the front line. Senior executives were aware that they would not be punished for what they could not see and promptly donned the blindfolds. Where they could not claim ignorance, they fell back on the claim that everyone was party to a decision, so that no individual could be held squarely to blame—the Murder on the Orient Express defence. It is imperative that in future senior executives in banks have an incentive to know what is happening on their watch—not an incentive to remain ignorant in case the regulator comes calling....

The professions may not be paragons, but they do at least espouse a strong duty of

trust, both towards clients and towards upholding the reputation of the profession as a whole. In contrast, bankers appear to have felt few such constraints on their own behaviour. Few bankers felt a duty to monitor or police the actions of their colleagues or to report their misdeeds. Banking culture has all too often been characterised by an absence of any sense of duty to the customer and a similar absence of any sense of collective responsibility to uphold the reputation of the industry....

That regulation is well-intentioned is no guarantee that it is a force for good. Misconceived and poorly-targeted regulation has been a major contributory factor across the full range of banking standards failings. Regulators cannot always be expected to behave as disinterested guardians who will pursue the "right" approach. They are faced with complex challenges to which the appropriate solutions are ambiguous and contested. They have not in the past always risen to those challenges satisfactorily. They need to resist the temptation to retreat into a comfort zone of setting complex rules and measuring compliance. They also need to avoid placing too much reliance on complex models rather than examining actual risk exposures. Regulators were complicit in banks outsourcing responsibility for compliance to them by accepting narrow conformity to rules as evidence of prudent conduct. Such an approach is easily gamed by banks, and is no substitute for judgement by regulators....

The favourable treatment of banking by regulators and governments has not merely been the consequence of smooth lobbyists seducing naive politicians. The economic growth and tax revenues promised by a booming sector over the relatively brief political cycle dazzled governments around the world. This encouraged excess and undermined regulators. Public anger with bankers has now dimmed this effect, but its possible revival in calmer economic times, when bankers are off the front pages, should remain a deep concern...

The distorted incentives in banking are nowhere more apparent than in the asymmetry between the rewards for short-term success and costs of long-term failure for individuals. Many bankers were taking part in a one-way bet, where they either won a huge amount, or they won slightly less and taxpayers and others picked up the tab, even if some individuals paid a large reputational price. Many have continued to prosper while others, including the taxpayer, continue to foot the bill for their mistakes. There have been a few isolated instances of individual sanction, but these have rarely reached to the very top of banks. This sanctioning of only a few individuals contributes to the myth that recent scandals can be seen as the result of the actions of a few 'rotten apples', rather than much deeper failings in banks, by regulators and other parts of the financial services industry...

Banking has been a great British strength, but for that reason is also an important source of risk to Britain. A series of factors, considered below, combine to give the UK an inherent advantage as a place to do financial business. Properly harnessed, finance can greatly add to nationwide prosperity. However, recent history has demonstrated that, whether or not the benefits of a large banking sector have been overstated, the risks were certainly understated. Given the huge size of the banking sector in the UK relative to the overall size of the economy, it is important that policy-makers and regulators balance support for the sector with proper safeguards to limit the potential damage it can do to the UK economy and to taxpayers if things go wrong. The banking collapse of 2008 shows these risks are very real...

Policy-makers should be aware of the risks of relocation, but should not be held hostage by them. Around the world there is a move to stronger regulation and to learning the lessons of

what happened in the run up to 2008. The UK must not be intimidated out of making the changes necessary to protect the public by threats of bank relocation. ..

The UK should do what is necessary to secure London's position as a pre-eminent and well-regulated financial centre in order to make sure that it represents an attractive base for whatever tomorrow's financial sector may look like. High standards in banking should not be a substitute for global success. On the contrary, they can be a stimulus to it...

Policy-makers in most areas of supervision and regulation need to work out what is best for the UK, not the lowest common denominator of what can most easily be agreed internationally. There is nothing inherently optimal about an international level playing field in regulation. There may be significant benefits to the UK as a financial centre from demonstrating that it can establish and adhere to standards significantly above the international minimum. A stable legal and regulatory environment, supporting a more secure financial system, is likely to attract new business just as ineffective or unnecessarily bureaucratic regulation is likely to deter it...

... Peer-to-peer and crowdfunding platforms have the potential to improve the UK retail banking market as both a source of competition to mainstream banks as well as an alternative to them. Furthermore, it could bring important consumer benefits by increasing the range of asset classes to which consumers have access. This access should not be restricted to high net worth individuals but, subject to consumer protections, should be available to all. The emergence of such firms could increase competition and choice for lenders, borrowers, consumers and investors....

Making a choice

Poor standards in banking and the public's response to them have generated an impetus within the banking industry to make proposals for professional banking standards. This impetus is welcome and must be harnessed. Some progress can be achieved through the emergence of a credible professional body in banking...

However, it is questionable whether the business of banking possesses sufficient characteristics of a profession to lend itself to direct control through a professional body. "Banking" involves a wide range of activities and lacks the large common core of learning which is a feature of most professions. It is a long way from being an industry where professional duties to customers, and to the integrity of the profession as a whole, trump an individual's own behavioural incentives. A professional body alone does not guarantee high standards, as illustrated by the varied scandals in a range of other sectors where such bodies exist.

There are also very substantial risks of duplication between the powers and role of a professional standards body and those of regulators, as well as risks that the creation of such a body could become a focus of public policy, diverting attention from the changes that are urgently needed within the existing regulatory framework.

Milestones for a professional body

If a unified professional body for banking in the UK is to emerge, the onus should lie on the industry itself to maintain the impetus for its development. Such a body needs first and foremost to be created through the will, and with the resources, of banks and those who work in the UK banking sector. The Commission's aim in this section is to identify milestones for its

development and to assist in fostering its establishment and growth. However, the emergence of a professional body should be consistent with the wider regulatory and legislative reforms needed in banking. It must not be seen as a necessary precursor to those reforms, still less as a substitute for them.

Banks maintain that there would be benefits if they were to adopt, implement and commit to enforce a single code of conduct prepared by a unified professional body, which reflected a higher set of standards and expectations for individual behaviour than those required by the regulator. Providing statutory powers to a professional body would mean either stripping away many powers from the regulators, including the new powers that we propose in this and subsequent chapters, or risking double jeopardy for individuals. No proponents of a professional body have come forward with a plan which the Commission believes is credible for how to address this problem.

While we support the creation of a professional standards body to promote higher professional standards in banking, the case for it to share or take over formal responsibility for enforcement in banking will only gradually be able to prove itself and so we do not recommend the establishment of such a body as an alternative to other regulatory measures. However, preliminary work to establish a professional body should begin immediately as a demonstration that commitment to high standards is expected throughout banking and that individuals are expected to abide by higher standards than those that can be enforced through regulation alone. On the basis of our assessment of the nature of the banking industry, we believe that the creation of an effective professional body is a long way off and may take at least a generation. It is therefore important that the trajectory towards professionalisation is clearly signalled immediately and that initial practical proposals for such a body are tabled at an early stage. Work can begin immediately on bodies for the most readily identifiable parts of banks which would benefit from professional standards. These include retail banking, the most senior levels and specialist areas such as insolvency and debt recovery.

An important milestone on the road to the successful development of a professional standards body would be that it could claim comprehensive coverage of all banks with operations in the UK. If banks were to decline to assist in a body's development, or to seek to resile from participation in due course, the credibility and effectiveness of the body would be significantly damaged.

A unified professional body for banking should have no need of public subsidy, either directly or indirectly. We would expect such a body to be funded by participating banks and individual qualified members. However, it would also need to establish independence from the outset, through its forms of governance, its disciplinary procedures and through the personnel at senior levels. The body must never allow itself to become a cosy sinecure for retired bank chairmen and City grandees. Just as importantly, it must eschew from the outset and by dint of its constitution any role in advocacy for the interests of banks individually or collectively...

The Senior Persons Regime

...The Commission recommends that the Approved Persons Regime be replaced by a Senior Persons Regime. The new Senior Persons Regime must ensure that the key responsibilities within banks are assigned to specific individuals who are aware of those responsibilities and have formally accepted them. The purposes of this change are: first, to encourage greater

clarity of responsibilities and improved corporate governance within banks; second, to establish beyond doubt individual responsibility in order to provide a sound basis for the regulators to impose remedial requirements or take enforcement action where serious problems occur. This would not preclude decision-making by board or committee, which will remain appropriate in many circumstances. Nor should it prevent the delegation of tasks in relation to responsibilities. However, it would reflect the reality that responsibility that is too thinly diffused can be too readily disowned: a buck that does not stop with an individual stops nowhere.

The Senior Persons Regime should apply to all banks and bank holding companies operating in the UK. The Commission would expect that the Senior Persons Regime would cover a narrower range of individuals than those currently in Significant Influence Functions. Many of the people in these functions are not really senior decision-takers. Taking them out of scope, though still subject to the Licensing Regime that we propose below, would allow the Senior Persons Regime to focus much more clearly on the people who really run banks and who should stand or fall by their role in decision-making. Beyond board and executive committee members, who should always be within scope, primary responsibility for identifying which individuals fall within the regime and how their responsibilities are defined should rest in the first instance with the banks themselves. We would expect such responsibilities to cover both prudential and conduct issues, such as product design. It should not be for the regulator to prescribe how banks structure their management, because it is important that banks retain the flexibility to do this in the most appropriate way for their business.

The Commission recommends that regulators set out in guidelines how responsibilities are to be identified and assigned, and should have the power to take action against firms when it is satisfied that they are not following these guidelines...

Regulators will need to show judgement and realism in exercising their enhanced powers. The Commission recommends that the regulators also be given a power to designate time-limited or remedial responsibilities that must be assigned to an individual within or thereby brought within the Senior Persons Regime.

It would be a mistake to prescribe a one-size-fits-all approach to the assessment of fitness and properness to assume a position as a Senior Person. What matters more is that the checks are geared to the responsibilities proposed for the individual and reflect supervisory judgement by senior regulators with involvement in the supervision of the bank concerned, rather than a box-ticking exercise by an isolated unit. The stated intention of regulators to focus more rigorous pre-approval checks on a smaller number of key individuals is to be welcomed.

The Commission considers that it would be unduly onerous for both the regulators and the regulated to make Senior Person status subject to periodic review. However, the Commission recommends that the regulators be given clear discretionary powers to review the assignment of responsibilities to a particular individual and require the redistribution of certain responsibilities or the addition of certain conditions. We would expect these powers to be exercised where, for example, a bank undergoes rapid expansion or where the regulators have reason to question a bank's approach to the allocation of responsibilities. We also recommend that the regulators be able to make approval of an individual Senior Person subject to conditions, for example where it is felt that they need to acquire a certain skill to carry out the job well. It is essential that the regime evolve and adapt over time. It would be a disaster if it were to relapse back into a one-off exercise that applied, in practice, only on entry, as with the

Standards and culture

Profound cultural change in institutions as large and complex as the main UK banks is unlikely to be achieved quickly. Bank leaders will need to commit themselves to working hard at the unglamorous task of implementing such change for many years to come.

Poor standards in banking are not the consequence of absent or deficient company value statements. Nor are they the result of the inadequate deployment of the latest management jargon to promulgate concepts of shared values. They are, at least in part, a reflection of the flagrant disregard for the numerous sensible codes that already existed. Corporate statements of values can play a useful role in communicating reformist intent and supplementing our more fundamental measures to address problems of standards and culture. But they should not be confused with solutions to those problems.

The appropriate tone and standard of behaviour at the top of a bank is a necessary condition for sustained improvements in standards and culture. However, it is far from sufficient. Improving standards and culture of major institutions, and sustaining the improvements, is a task for the long term. For lasting change, the tone in the middle and at the bottom are also important. Unless measures are taken to ensure that the intentions of those at the top are reflected in behaviour at all employee levels, fine words from the post-crisis new guard will do little to alter the fundamental nature of the organisations they run. There are some signs that the leaderships of the banks are moving in the right direction. The danger is that admirable intentions, a more considered approach, and some early improvements, driven by those now in charge, are mistaken for lasting change throughout the organisation.

We believe that the influence of a professional body for banking could assist the development of the culture within the industry by introducing non-financial incentives, which nonetheless have financial implications, such as peer pressure and the potential to shame and discipline miscreants. Such a body could, by its very existence, be a major force for cultural change and we have already recommended that its establishment should be pursued as a medium to long term goal alongside other measures such as new regulatory provisions.

There is little point in senior executives talking about the importance of the customer and then putting in place incentive and performance management schemes which focus on sales which are not in the interests of the customer. As long as the incentives to break codes of conduct exceed those to comply, codes are likely to be broken. Where that gap is widest, such as on trading floors, codes of conduct have gained least traction. This betrays a wider problem with stand-alone programmes to raise standards and improve culture. Attempts to fix them independently of the causes are well-intentioned and superficially attractive, but are likely to fail.

The culture on the trading floor is overwhelmingly male. The Government has taken a view on having more women in the boardroom through the review carried out by Lord Davies of Abersoch and his recommendations that FTSE 100 companies increase the number of women directors who serve on their boards. If that is beneficial in the boardroom so it should be on the trading floor. The people who work in an industry have an impact on the culture of that industry. More women on the trading floor would be beneficial for banks. The main UK-based banks should publish the gender breakdown of their trading operations and, where there is a significant imbalance, what they are going to do to address the issue within six months of the

publication of this Report and thereafter in their annual reports.

In order for banks to demonstrate to the public that they have changed their standards and culture, they will need to provide clear evidence of such change. Banks are well aware of their past failings. They should acknowledge them. Further opportunity to demonstrate change is offered by ongoing concerns, such as approaches taken to customer redress or involvement in activities inconsistent with a customer service ethos. The clearest demonstration of change will come with the avoidance of further standards failings of the sort that led to the creation of the Commission.

Driving out fear

The Commission was shocked by the evidence it heard that so many people turned a blind eye to misbehaviour and failed to report it. Institutions must ensure that their staff have a clear understanding of their duty to report an instance of wrongdoing, or 'whistleblow', within the firm. This should include clear information for staff on what to do. Employee contracts and codes of conduct should include clear references to the duty to whistleblow and the circumstances in which they would be expected to do so.

In addition to procedures for formal whistleblowing, banks must have in place mechanisms for employees to raise concerns when they feel discomfort about products or practices, even where they are not making a specific allegation of wrongdoing. It is in the long-term interest of banks to have mechanisms in place for ensuring that any accumulation of concerns in a particular area is acted on. Accountability for ensuring such safeguards are in place should rest with the non-executive director responsible for whistleblowing.

A non-executive board member—preferably the Chairman—should be given specific responsibility under the Senior Persons Regime for the effective operation of the firm's whistleblowing regime. That Board member must be satisfied that there are robust and effective whistleblowing procedures in place and that complaints are dealt with and escalated appropriately. It should be his or her personal responsibility to see that they are. This reporting framework should provide greater confidence that wider problems, as well as individual complaints, will be appropriately identified and handled.

The Commission recommends that the Board member responsible for the institution's whistleblowing procedures be held personally accountable for protecting whistleblowers against detrimental treatment. It will be for each firm to decide how to operate this protection in practice, but, by way of example, the Board member might be required to approve significant employment decisions relating to the whistleblower (such as changes to remuneration, change of role, career progression, disciplinary action), and to satisfy him or herself that the decisions made do not constitute detrimental treatment as a result of whistleblowing. Should a whistleblower later allege detrimental treatment to the regulator, it will be for that Board member to satisfy the regulator that the firm acted appropriately.

Whistleblowing reports should be subjected to an internal 'filter' by the bank to identify those which should be treated as grievances. Banks should be given an opportunity to conduct and resolve their own investigations of substantive whistleblowing allegations. We note claims that 'whistleblowing' being treated as individual grievances could discourage legitimate concerns from being raised...

The regulator should periodically examine a firm's whistleblowing records, both in order

to inform itself about possible matters of concern, and to ensure that firms are treating whistleblowers' concerns appropriately. The regulators should determine the information that banks should report on whistleblowing within their organisation in their annual report.

All Senior Persons should have an explicit duty to be open with the regulators, not least in cases where the Senior Person becomes aware of possible wrongdoing, regardless of whether the Senior Person in question has a direct responsibility for interacting with the regulators.

The FCA's evidence appeared to show little appreciation of the personal dilemma that whistleblowers may face. The FCA should regard it as its responsibility to support whistleblowers. It should also provide feedback to the whistleblower about how the regulator has investigated their concerns and the ultimate conclusion it reached as to whether or not to take enforcement action against the firm and the reasons for its decision. The Commission recommends that the regulator require banks to inform it of any employment tribunal cases brought by employees relying on the Public Interest Disclosure Act where the tribunal finds in the employee's favour. The regulator can then consider whether to take enforcement action against individuals or firms who are found to have acted in a manner inconsistent with regulatory requirements set out in the regulator's handbook. In such investigations the onus should be on the individuals concerned, and the non-executive director responsible within a firm for protecting whistleblowers from detriment, to show that they have acted appropriately.

We note the regulator's disquiet about the prospect of financially incentivising whistleblowing. The Commission calls on the regulator to undertake research into the impact of financial incentives in the US in encouraging whistleblowing, exposing wrongdoing and promoting integrity and transparency in financial markets.

We have said earlier in this Report that the financial sector must undergo a significant shift in cultural attitudes towards whistleblowing, from it being viewed with distrust and hostility to one being recognised as an essential element of an effective compliance and audit regime. Attention should focus on achieving this shift of attitude.

A poorly designed whistleblowing regime could be disruptive for a firm but well designed schemes can be a valuable addition to its internal controls. The regulator should be empowered in cases where as a result of an enforcement action it is satisfied that a whistleblower has not been properly treated by a firm, to require firms to provide a compensatory payment for that treatment without the person concerned having to go to an employment tribunal....

Sanctions and enforcement

Enforcement against banks

Effective enforcement action against firms represents an important pillar of the overall approach to enforcement. In many cases, it serves as the gateway to enforcement action against responsible individuals, which is also necessary. It can draw wider attention to a failure, providing incentives for firms to strive to maintain high standards, and establishes penalties when banks depart from those standards. The record of the regulators in enforcement against firms is patchy at best. It is notable that both significant prudential failures, for example at RBS, and some widespread conduct failures in the selling of PPI did not lead to successful enforcement against banks. In the investigations those at the top often absolved themselves by attesting their ignorance about the organisation of which they were in charge. It would run contrary to the public interest if the idea were to gain currency that banks can be too big or

complex to sanction.

It is to be hoped that the LIBOR investigations have set a pattern for the future. In relation to prudential failings, formal action will assist in determining what went wrong and help to provide the basis for pursuing responsible individuals. In relation to conduct failings, a visible and costly redress process may not be enough: enforcement has the benefit of more clearly setting out where failures occurred and that rules were broken, so that culpability is not obfuscated and so that lessons can be learned.

It is right that an element of the fine should fall on shareholders, to provide a continuing incentive for them to monitor standards of conduct and supervision within the banks they own. However, our recommendations on recovery of deferred payments in Chapter 8 are designed to ensure that, in future, a significant proportion of fines on firms may be met from deductions from the remuneration of staff of the bank at the time of the misconduct, thereby making the prospect of fines on firms a more direct incentive on individuals to prevent it. There should be a presumption that fines on banks should be recovered from the pool of deferred compensation as well as current year bonuses. The recovery should materially affect to different degrees individuals directly involved and those responsible for managing or supervising them, staff in the same business unit or division, and staff across the organisation as a whole. The impact and distribution of fines on deferred compensation should be approved by the supervisors as part of a settlement agreement.

Firms cannot be permitted to regard enforcement fines as a "business cost". The FSA recognised that in the past the level of its fines was too low to prevent this. The reforms to its penalty policy are supposed to address this, but they have yet to be properly tested, and the credibility of enforcement has been damaged by a legacy of fines that were pitiful compared to the benefits banks gained from the misconduct. To provide greater incentives to maintain high levels of professional standards, both the FCA and the PRA should be prepared to review again their penalty setting framework in the future to allow for a further substantial increase in fines. They should ensure that in responding to any future failures they make full use of the new rules for calculating fines and build on the encouraging examples set by the LIBOR fines. If regulators believe that the current legal framework still inhibits them from imposing the necessary level of penalties, they should tell Parliament immediately.

In its Report on LIBOR, the Treasury Committee concluded that "the FSA and its successors should consider greater flexibility in fine levels, levying much heavier penalties on firms which fail fully to cooperate with them". We agree. Cooperation by firms in bringing issues to regulators' attention and assisting with their investigation should be a given. Regulators should make full use of the flexibility in their penalty policy to punish cases where this does not occur. However, regulators should also make it clear to firms that the same flexibility will be used to show leniency where inadvertent and minor breaches are swiftly brought to their attention and rectified, so that the fear of over-reaction does not to stifle the free flow of information.

A protracted process of enforcement with a firm can delay enforcement against individuals, weakening the prospect of its success and of meaningful penalties, particularly if the delay means that the individual can continue lucrative work for several more years and approach retirement. The Commission recommends that the regulators bear in mind the advantage of swift resolution of enforcement action against firms, in particular in cases where

settlement with the firm is a precursor to action against responsible individuals.

Civil sanctions and powers of enforcement over individuals

Faced with the most widespread and damaging failure of the banking industry in the UK's modern history, the regulatory authorities seemed almost powerless to bring sanctions against those who presided over massive failures within banks. Public concern about this apparent powerlessness is both understandable and justified, but the need for a more effective enforcement regime does and should not arise from a public demand for retribution. It is needed to correct the unbalanced incentives that pervade banking. These unbalanced incentives have contributed greatly to poor standards. Redress of these is needed not merely as a step to restoring public confidence, but also to create a new incentive for bankers to do the right thing, and particularly for those in the most senior positions fully to fulfil their duties and to supervise the actions of those below them.

Later in this chapter, we consider the case for a new criminal offence specific to the banking sector. However, in the context of civil sanctions, the Commission has not heard the case advanced for a range of penalties which go beyond those already available. The problems, and the proposals for change which follow, reflect the fact that the sanctions already available to the regulators, such as very large fines and permanent disbarment from the UK financial services sector, have so rarely been applied.

The foundations for a new approach are laid in the Commission's recommendations ... [for] Banking Standards Rules designed to ensure that the full range of enforcement tools could be applied to a wider range of individuals working in banking. This would be supported by a system of licensing administered by individual banks, under the supervision of the regulators, to ensure that all those subject to the Banking Standards Rules were aware of their obligations. This approach would prevent one barrier to effective enforcement that we identified, namely that regulators lacked effective powers to sanction misconduct by bankers who were not Approved Persons.

... one of the most dismaying weaknesses that we have identified, whereby a combination of collective decision-making, complex decision-making structures and extensive delegation create a situation in which the most senior individuals at the highest level within banks, like Macavity, cannot be held responsible for even the most widespread and flagrant of failures. We proposed the establishment of a Senior Persons Regime to replace the Approved Persons Regime in respect of banks, whereby all key responsibilities within a bank would be assigned to a specific, senior individual. Even where certain activities in pursuance of the responsibility were either delegated or subject to collective decision-making that responsibility would remain with the designated individual. The Senior Persons Regime would be designed to ensure that, in future, it should be possible to identify those responsible for failures more clearly and more fairly. This should provide a stronger basis for the use of enforcement powers in respect of individuals.

These changes would also need to be accompanied by a change of approach from the regulators. In respect of insider trading, the increased effectiveness of criminal enforcement owes less to changes in the law than changes in the approach of the regulators, in particular to a realisation that a large-scale commitment of time, effort and resources to seeing cases through is both necessary and worthwhile. The same determination has not been so apparent

in enforcement action relating to bank failures, LIBOR or mis-selling. At the root of this failure has been what the regulators themselves have characterised as a bottom-up approach. A key to success in the future is likely to be a top-down approach, drawing on the clarity that the Senior Persons Regime is intended to provide about who is exercising responsibility at the highest levels, what they knew and did, and what they reasonably could and should have known and done.

The proposal to create a rebuttable presumption that directors of failed banks should not work in such a role again is a well-intentioned measure for addressing the difficulty of proving individual culpability, but it is a blunt instrument with several weaknesses. The blanket imposition of a rebuttable presumption risks having perverse and unfair effects; it will act as a disincentive for new directors to come to the aid of a struggling bank; it could encourage power structures in which key decision-makers eschewed the title and responsibility of director. Furthermore, the Government proposal as it stands is too narrow to be of significant use. Notably, it would probably not have been triggered in most of the recent scandals ranging from the bail-outs of RBS and HBOS to PPI mis-selling and LIBOR manipulation. We have concluded that a more effective approach than the blanket imposition of a rebuttable presumption would be one which reverses the burden of proof in a wider, but clearly defined, set of circumstances covering both prudential and conduct failures.

Greater individual accountability needs to be built into the FCA's and PRA's processes. The Commission recommends that legislation be introduced to provide that, when certain conditions are met, the regulators should be able to impose the full range of civil sanctions, including a ban, on an individual unless that person can demonstrate that he or she took all reasonable steps to prevent or mitigate the effects of a specified failing. The first condition would be that the bank for whom the individual worked or is working has been the subject of successful enforcement action which has been settled or upheld by tribunal. The second condition is that the regulator can demonstrate that the individual held responsibilities assigned in the Senior Persons Regime which are directly relevant to the subject of the enforcement action.

The FSA made the case for a power to impose an interim prohibition on individuals against whom enforcement action has been commenced. The case made by the FSA was not clearly targeted on banks. An interim prohibition could cause serious harm if used unfairly or arbitrarily. In the case of very small financial firms in particular, having a key individual prohibited for even a short period might cause irreparable damage to their reputation and see clients leave never to return, even though the case might be dropped or not upheld. Given that the FSA has only rarely taken public enforcement action against senior individuals in large banks, it may be that the cases through which they have identified the need for a suspension power involve smaller firms or non-bank financial institutions. Based on our consideration of issues relating to banking standards, the Commission has concluded that the case has not been made for providing the regulators with a general power to impose interim prohibitions on individuals carrying out controlled functions in the financial services sector.

The current time limit of three years between the regulator learning of an offence and taking enforcement action against individuals could act as a constraint on the regulators' ability to build credible cases. This could be a particular barrier to the regulators' ability to place greater priority on pursuing senior individuals in large and complex banks, as we are

recommending. In view of our proposal that enforcement action against a firm must be completed before the regulator can deploy the new tool of a reversed burden of proof, more than three years may well be required to complete this process and make the new tool usable. The Commission recommends that the Government should address this problem by allowing for an extension of the limitation period in certain circumstances. However, swift enforcement action should be the priority. Regulators should be required retrospectively to provide a full explanation for the need to go beyond three years. They can expect to be challenged by Parliament if it were to transpire that they were using this measure as an excuse for delaying enforcement action.

A new criminal offence?

The Commission has concluded that there is a strong case in principle for a new criminal offence of reckless misconduct in the management of a bank. While all concerned should be under no illusions about the difficulties of securing a conviction for such a new offence, the fact that recklessness in carrying out professional responsibilities carries a risk of a criminal conviction and a prison sentence would give pause for thought to the senior officers of UK banks. The Commission recommends that the offence be limited to individuals covered by the new Senior Persons Regime, so that those concerned could have no doubts about their potential criminal liability.

The Commission would expect this offence to be pursued in cases involving only the most serious of failings, such as where a bank failed with substantial costs to the taxpayer, lasting consequences for the financial system, or serious harm to customers. The credibility of such an offence would also depend on it being used only in the most serious cases, and not predominantly against smaller operators where proving responsibility is easier, but the harm is much lower. Little purpose would be served by the creation of a criminal offence if the only punishment available to the courts were the imposition of a fine, because substantial fines can already be levied as a civil sanction with a lower burden of proof. We would expect the determination of the available sentences to have regard to relevant comparable offences.

It is inappropriate that those found guilty of criminal recklessness should continue to benefit from remuneration obtained as a consequence of the reckless behaviour. Fines may not claw back the full amount. The Commission recommends that the Government bring forward, after consultation with the regulators and no later than the end of 2013, proposals for additional provisions for civil recovery from individuals who have been found guilty of reckless mismanagement of a bank.

The Commission's support in principle for a new criminal offence is subject to an important reservation. Experience suggests that, where there is the possibility of a criminal prosecution, public disclosure of failings might be greatly limited until the criminal case is finished. It is important to expedite any civil sanctions against individuals and to publish information into banking failures in a timely manner. The Commission recommends that, following a successful civil enforcement action against a bank, the decision on whether to bring criminal proceedings against relevant Senior Persons must be taken within twelve months.

The chairmen of Barclays, HSBC, Lloyds Banking Group, Royal Bank of

Scotland, Santander, Standard Chartered and Nationwide,[53] subsequently asked Sir Richard Lambert to work on the development of a new self-regulatory regime for banking in a Banking Standards Review. The Review led to the establishment of the Banking Standards Board, converted into the Financial Services Culture Board (FSCB) to include non-bank firms, in 2021.[54] This body has carried out regular evaluations of culture, assessing the behavior of firms that sign up for assessment. The characteristics against which firms are assessed are honesty, respect, openness, accountability, competence, reliability, resilience, responsiveness, and shared purpose.[55] In 2022 the FSCB adopted a new focus on inclusion.[56] It is not clear how effective this body has been.

In addition to the BSB there is also a Senior Managers and Certification Regime administered by the Financial Conduct Authority, which is meant to make individuals more accountable.[57] The FCA has also taken a broader approach to the issue of culture in finance, and published a discussion paper on this issue in 2018 - **Transforming Culture in Financial Services (FCA)**:

Two fundamental concepts underpin our thinking about culture and regulation. The first is that regulation has to hold the individual as well as the firm to account. This is why we consider it so important to define the 5 Conduct Rules[58] and have them apply to all financial services individuals in the firm.
The second concept is that leaders can manage culture even if they can't measure it very well. This is deeply embedded in the Accountability Regime too. The regime aims to hold firms' leadership to account for their own behaviour and for taking reasonable steps to manage the behaviour of those in their areas of responsibility. It also aims to ensure that leaders have clearly articulated what they are accountable for and that key responsibilities neither slip through the cracks nor end up too diffused. It provides a robust framework for a culture of accountability, bringing much needed clarity to the accountability of all individuals and a focus on behaviour that goes beyond simply complying with the rules
From start-ups to large corporations, clear accountability for individuals is fundamental. Our

---

[53] Banking Standards Review, Consultation Paper, 2 (Feb. 2014).

[54] https://financialservicesculturebord.org.uk/who-we-are/our-history/.

[55] https://financialservicesculturebord.org.uk/assessment-results-2021/.

[56] Financial Services Culture Board & Financial Services Skills Commissio, Inclusion across financial services: Piloting a common approach to measurement (Feb. 2022).

[57] https://www.fca.org.uk/firms/senior-managers-certification-regime .

[58] 1: You must act with integrity; 2 You must act with due skill, care and diligence; 3 You must be open and cooperative with the FCA, the PRA and other regulators; 4 You must pay due regard to the interests of customers and treat them fairly; 5 you must observe proper standards of market conduct.

intention through the Accountability Regime isn't to change how firms organise themselves or impose a defined culture, but rather to develop a standard of accountability and conduct at all levels within a firm. Many firms have informally reported that this clarity of accountability has noticeably improved the effectiveness of their leadership...
.. the question remains – how can firms go beyond rules and standards to achieve real culture change? ...
Understanding the dynamics of culture facilitates progress, but firms' behaviour will only transform for the better if change is chosen rather than imposed. A focus on culture is the responsibility of everyone in a firm. It should be a collaborative effort, by all areas and at all levels – and industry must take responsibility for delivering the standards it aspires to. By doing so, firms help to mitigate the risk that old habits of behaviour will repeat themselves, and so play a vital role in reducing harm to consumers, markets, and themselves.
Given the complexity of human dynamics it is unlikely there will ever be a 'quick fix' for change at an organisational, much less a societal, level. However, the importance of generating a meaningful debate on this topic reinforces the interdependence between the impact of effective cultures and restoring public trust. That debate is central to this Discussion Paper.[59]

Meanwhile, the Federal Reserve Bank of New York has also been thinking about the misconduct issue. Here's a speech by **Kevin Stiroh, FRBNY**:

... the issue of conduct and culture reform in the financial services industry is a "complex" problem and not simply a "complicated" one. Complicated problems have clear and relatively stable cause-and-effect patterns so that outcomes are largely predictable with the appropriate expertise and analysis. By contrast, complex problems are typically marked by interconnectedness of a large number of factors, constant evolution, feedback loops, "unknown unknowns", and unpredictable outcomes. Culture reform is that type of problem.
A firm's culture can be defined as the shared set of norms that influences decision-making and is evidenced through behavior. Now consider a global systemically important bank with trillions of dollars of assets; with operations that span diverse business lines, customers, counterparties, investors and regulators across multiple jurisdictions; and that competes in a global industry against similar firms. Add in tens, or even hundreds, of thousands of employees with a wide range of motivations and goals who interact in varied but interconnected operating environments with different regional, corporate and individual values, incentives, regulations, and laws, and the inherent complexity becomes clear.
This complexity makes it virtually impossible to fully comprehend the drivers of culture or predict its behavioral consequences. An implication is the need for a long-term, sustained commitment to addressing conduct and culture reform using a wide range of tools that are suitable for a complex problem.

Evolution of New York Fed's Effort

[59] Financial Conduct Authority, Transforming Culture in Financial Services, DP 18/2 (Mar. 2018). The DP contains a number of different essays by different authors.

In the ten years that followed the financial crisis, we have continued to see a stream of misconduct scandals and cultural failures, and a corresponding increase in significant litigation and enforcement activity, with costs estimated at an aggregate of $320 billion worldwide.

At the New York Fed, our work in advocating culture and behavior reform in the financial sector started in late 2013 when our former President, Bill Dudley, delivered a speech on the "too-big-to-fail" problem. In that speech, he argued that "there is evidence of deep-seated culture and ethical failures at many financial institutions." More recently, our current President John Williams concluded that "we have not yet fully addressed the root causes of many of the problems that have plagued the financial sector" and that there was still a "sense of urgency in addressing banking culture."

Over the past five years, the New York Fed has focused on shining a spotlight on culture, behavior and conduct concerns, and pushed the industry to address these issues through a range of activities:

Engaging with diverse thinkers on governance, culture and organizational behavior to better understand the complexity of culture reform;

Convening academic experts, and leaders in finance and the official sector through conferences and workshops on culture and behavior reform;

Facilitating discussions among the supervisory community on assessing and influencing industry culture-related efforts;

Building a platform for a partnership between business schools and industry representatives to influence culture reform through training of future leaders in finance; and

Publishing a white paper on "Misconduct Risk, Culture and Supervision" that discussed a range of market failures that provide a conceptual rationale for intervention by bank supervisors.

Our white paper also summarizes work of supervisors from multiple jurisdictions around the world who are increasingly focused on the risks posed by poor culture and misconduct, and have developed a broad assortment of new tools and practices for identifying and supervising for misconduct risk. International efforts range from the creation of specialized units of behavioral risk experts to risk culture assessment frameworks to supervisory guidance that directs supervised institutions to develop and promote a sound corporate culture.

I view this variation in approach as a feature and not a bug of the official sector focus on culture reform. There is rarely a single solution to a complex problem with many interdependencies and deep uncertainty. Rather, the official sector must experiment and innovate; probe and adapt; and try new approaches to foster a healthy culture that promotes appropriate conduct.

One common thread of the recent innovations, however, is that supervisors can provide a horizontal perspective on culture reform that reflects broad social goals in a way that the private sector cannot. To be clear, it is not the supervisors' job to dictate the internal culture of a firm, but when there are market failures such as externalities or information asymmetries, then there is a role for the official sector to push firms to do more to address these issues and mitigate misconduct risk.

We should be cautious, however, about our ability to influence precisely and predictably. Public health studies, for example, document "policy resistance" where interventions are defeated by the system's response to an intervention. As an example, a rules-based regime that focuses on reducing conduct risk by prescriptive regulatory fiat runs the risks of creating a "check-the-box culture" where everything not explicitly banned is considered acceptable behavior. This has the

potential to facilitate exactly the wrong type of culture, conduct and risk-taking.

Challenges Related to Complexity

While I have spoken so far about work by the official sector, progress has also been made over the past few years by the industry in terms of senior management focus and commitment to culture reform. Some firms have created Board-level committees looking at culture, others have introduced behavioral risk into their audit programs, and still others have developed dashboards with a range of quantitative and qualitative factors to track their efforts and outcomes. Progress has been uneven, however, and there is still more to do. Let me identify several areas where I think additional work is needed—assessment, technology, and influence.

Assessment

Given the complexity of the problem, measuring and assessing progress is not straightforward. Assessment of culture and the factors needed to change it are difficult, but this should not deter us. Managers, investors, and the official sector all want to know what is changing and whether misconduct risk has been mitigated. The question then is, how will we really know whether change is happening and whether progress is sustainable?

I don't believe that there is a "silver bullet" for assessing culture change—no single solution, approach, or template will work for every firm in every circumstance. That said, standardized metrics will help in assessing changes over time and across firms. The UK Banking Standards Board (BSB), for example, provides one lens on assessing culture change for a broad cross-section of financial service firms operating in the U.K. I believe diagnostic tools like this are an important part of the cultural assessment toolkit.

Moreover, firms and the official sector need to evaluate a wide range of behaviors, signals, and outcomes to draw the most robust conclusions about the depth and pace of culture reform. I think it is critical for both firms and the official sector to continue to experiment with new approaches to assessing culture change, to collect and build new forms of data and measurement, to develop qualitative assessments to complement quantitative ones, to use new techniques and technology to understand how a firm's culture and conduct are changing, and to continue adapting and course correcting to a sustainable business strategy as the operating environment evolves.

Influence

Fostering productive behavioral change is at the heart of culture reform. Behavior, in turn, is driven by a multifaceted set of factors including incentives, cues from peers, observations about leaders, and formal policies and procedures. Most of us are not experts in human behavior, so I believe we should be open to incorporating lessons from behavioral economics and other social sciences into programs to mitigate conduct risk and promote cultural change.

Behavioral economics blends psychology and economics to provide insight into why individuals may behave in a certain way and make decisions that may not be in their own economic best interest. For example, individuals often make choices that provide immediate recognition or satisfaction—higher status within a peer group, for example—often at the cost of a potentially better financial outcome in the long term.

This type of human behavior is at the core of the complexity of culture reform. Lessons from the

field have increased understanding of where decision-making can depart from economic expectations. Sometimes, these lessons have been used to create circumstances and environments that positively influence individual outcomes by “nudging” individuals to better choices. These nudges, in turn, help reinforce acceptable behavioral norms, and ultimately a firm’s culture. How can we nudge in order to reduce misconduct risk? More broadly, how can the financial services sector, including firms and supervisors, leverage insights from the social sciences to promote environments that foster healthy group behavioral patterns with better decision-making?

Technology

The promise of new technology and big data for financial institutions is everywhere we look. From artificial intelligence to machine learning to natural language processing, there seems to be unlimited potential for more efficient operations, better analytics and more accurate predictions, and more personalized product development. But, how will advances in technology, particularly the adoption of new technologies, such as artificial intelligence, influence the behavioral risks associated with human decision-making? And how does technology introduce new risks that prompt a rethinking of responsibility and customer relationships—especially with regard to privacy and information security?

Moreover, the disruptive potential of innovation is likely to exacerbate an already complex environment as decision-making becomes more opaque and new roles and responsibilities are introduced. For example, what will effective governance and risk management look like? Do artificial intelligence and machine learning introduce new model risk? Or operational risk? Or conduct risk? What does it mean to supervise or regulate conduct if decisions are made by self-learning algorithms? More broadly, what culture and conduct risk will be embedded in technology-driven financial services in the future? These are hard questions for financial firms and for the official sector, and our approach to the reform of financial industry culture will need to address them.

Conclusions

To return to the beginning of this discussion, culture reform in finance is a complex problem. Causal relationships are difficult to isolate, linkages are constantly changing, and accurate prediction is impossible. That does not mean that we are powerless, or that we should accept complexity as an excuse for not trying to foster change. Rather, we need a long-term commitment that brings the appropriate tools and approaches to bear. The costs and potential consequences of market failures associated with misconduct risk and culture suggests that it is vitally important that we do so.

Both financial firms and the official sector should focus attention on investigating and asking questions to better understand the underlying drivers, motivations and risks behind the behaviors of individuals and groups. We should ensure that we look at behaviors and outcomes from multiple perspectives, so we can gain a more robust understanding of the operating environment as a whole. No single perspective is likely to provide all of the insights. Experimentation and iteration, use of narrative and story-telling, and innovative methods for harnessing diversity of perspective are thought to be effective ways of tackling complex problems and we all need to innovate, adapt and seek new approaches.

I think this focus on conduct and culture is entirely consistent with a traditional supervisory focus on resilience, both for individual firms and the financial system as whole. This can be resilience of a firm's balance sheet in response to financial risk or an unexpected loss that depletes a firm's equity capital or resilience of a firm's culture in response to conduct risk or an unexpected fraud that depletes its cultural capital. In all of these cases, a resilient firm will be better able to adapt and evolve in order to continue to function and provide the critical financial services necessary to support a growing and stable economy.

As part of its work the **Financial Stability Board** has focused on "Risk Culture."[60] Here is an excerpt from the FSB's Guidance on Risk Culture:

Weaknesses in risk culture are often considered a root cause of the global financial crisis, headline risk and compliance events. A financial institution's risk culture plays an important role in influencing the actions and decisions taken by individuals within the institution and in shaping the institution's attitude toward its stakeholders, including its supervisors.
A sound risk culture consistently supports appropriate risk awareness, behaviours and judgements about risk-taking within a strong risk governance framework. A sound risk culture bolsters effective risk management, promotes sound risk-taking, and ensures that emerging risks or risk-taking activities beyond the institution's risk appetite are recognised, assessed, escalated and addressed in a timely manner.
A sound risk culture should emphasise throughout the institution the importance of ensuring that:
(i) an appropriate risk-reward balance consistent with the institution's risk appetite is achieved when taking on risks;
(ii) an effective system of controls commensurate with the scale and complexity of the financial institution is properly put in place;
(iii) the quality of risk models, data accuracy, capability of available tools to accurately measure risks, and justifications for risk taking can be challenged, and
(iv) all limit breaches, deviations from established policies, and operational incidents are thoroughly followed up with proportionate disciplinary actions when necessary.
Risk culture, as well as corporate culture, evolves over time in relation to the events that affect the institution's history (such as mergers and acquisitions) and to the external context within which the institution operates. Sub-cultures within institutions may exist depending on the different contexts within which parts of the institution operate. However sub-cultures should adhere to the high -level values and elements that support the institution's overall risk culture. First and foremost, it should be expected that employees in all parts of the institution conduct business in a legal and ethical manner. An environment that promotes integrity should be created across the institution as a whole, including focusing on fair outcomes for customers. Supervisors should consider whether an institution's risk culture is appropriate for the scale,

[60] Financial Stability Board, Guidance on Supervisory Interaction with Financial Institutions on Risk Culture: A Framework for Assessing Risk Culture (Apr. 7, 2014) at http://www.financialstabilityboard.org/publications/140407.pdf .

complexity, and nature of its business and based on sound, articulated values which are carefully managed by the leadership of the financial institution. In this regard, supervisors should set expectations for the board to oversee management's role in fostering and maintaining a sound risk culture. This requires supervisors to effectively articulate these expectations to the board and senior management and ensure ongoing follow-up on whether these expectations are being met....

Assessing risk culture is complex. But given its importance attention must be paid to it. There are several indicators or practices that can be indicative of a sound risk culture. Institutions and supervisors can build awareness of the institution's balance between risk-taking and control by considering such factors. These indicators can be considered collectively and as mutually reinforcing; looking at each indicator in isolation will ignore the multi-faceted nature of risk culture....

These indicators include:

• Tone from the top: The board and senior management are the starting point for setting the financial institution's core values and expectations for the risk culture of the institution, and their behaviour must reflect the values being espoused. A key value that should be espoused is the expectation that staff act with integrity (doing the right thing) and promptly escalate observed non-compliance within or outside the organisation (no surprises approach) The leadership of the institution promotes, monitors, and assesses the risk culture of the financial institution; considers the impact of culture on safety and soundness; and makes changes where necessary.

•Accountability: Relevant employees at all levels understand the core values of the institution and its approach to risk, are capable of performing their prescribed roles, and are aware that they are held accountable for their actions in relation to the institution's risk-taking behaviour. Staff acceptance of risk-related goals and related values is essential.

• Effective communication and challenge : A sound risk culture promotes an environment of open communication and effective challenge in which decision - making processes encourage a range of views; allow for testing of current practices; stimulate a positive, critical attitude among employees ; and promote an environment of open and constructive engagement.

• Incentives: Performance and talent management encourage and reinforce maintenance of the financial institution's desired risk management behaviour. Financial and non -financial incentives support the core values and risk culture at all levels of the institution....

Supervisors are in a unique position to gain insights on risk culture at financial institutions given their access to information and individuals across the institution, as well as the results of supervisory work. This unique view and the ability to gather observations across multiple institutions enable peer analysis and suggest issues that both supervisors and institutions should look at.

Supervisors should adopt a process to synthesise periodically supervisory findings, look for common themes, aggregate informal observations they have about the institution and apply high -level judgement in deciding whether culture or undesired behaviour is a root cause of supervisory findings. Supervisors should recognise that every supervisory activity can add information that informs these periodic assessments, but that single supervisory results are rarely a definitive indicator of culture issues that need to be addressed. Evidence should be gathered from the full range of supervisory activities so as to avoid the assessment of risk

culture being perceived and managed as a compliance - driven exercise. The lists of possible indicators should be treated as a starting point for those assessments. Supervisors should avoid supervisory methodologies that treat these indicators as a checklist....
Discussions with boards and senior management will help form the supervisory view of the institution's risk culture. Supervisory observations on culture issues should be further discussed with members of the board and senior management so as to promote and develop a shared understanding of the institution's risk culture. Identification of a practice or attitude that is not supportive of sound risk management should be brought to the attention of the board or senior management, as appropriate, who have ultimate responsibility for outlining and overseeing the financial institution's risk culture, to influence change in a positive direction. The supervisor raising, and the financial institution acting early to address, the root causes of the behavioural weakness will aid in preventing (or mitigating the impact of) particular undesired cultural norms from taking root and growing.

In 2018 the FSB published **Strengthening Governance Frameworks to Mitigate Misconduct Risk: A Toolkit for Firms and Supervisors**:[61]

The FSB conducted further work in three...areas... that were considered particularly important for mitigating misconduct risk from a financial stability perspective: (i) cultural drivers of misconduct; (ii) individual responsibility and accountability; and (iii) the "rolling bad apples" phenomenon, which refers to individuals who engage in misconduct but are able to obtain subsequent employment elsewhere without disclosing their earlier misconduct to the new employer.
The goal of this work has been to develop a toolkit that firms and national authorities can use to mitigate misconduct risk in these three areas.Given the interplay between cultural drivers of misconduct, individual responsibility and accountability, and the "rolling bad apples" phenomenon, it is important to look at these aspects of governance frameworks together. A firm's culture plays an important role in influencing the actions and decisions taken by employees within the firm and in shaping the firm's attitude toward its stakeholders, including supervisors and regulators. It also may allow or encourage misconduct by individuals, or large numbers of employees, particularly if instances of misconduct are overlooked. Insisting on clarity in individual responsibilities reflects the priority that the firm places on a culture of good conduct and the need for accountability. By contrast, a lack of clarity in individual responsibilities can make it difficult to hold individuals accountable for their actions and decisions, as well as for reasonably managing the actions and behaviours of those in their area of responsibilities. In some cases, individuals who are not held accountable for their misconduct at one firm surface at another firm (or another division of the same firm) and repeat their misbehaviour – the rolling bad apples phenomenon. ...
... To help give impetus to efforts underway, the FSB has developed a list of tools as options that firms and authorities can use, taking into account jurisdictions' legislative, judicial

[61] Financial Stability Board, Strengthening Governance Frameworksto Mitigate Misconduct Risk: A Toolkit for Firms and Supervisors (Apr. 20, 2018), at http://www.fsb.org/wp-content/uploads/P200418.pdf .

and regulatory frameworks. There is no one-size-fits-all approach; some tools may not be relevant for certain authorities and firms, and some jurisdictions or authorities may not have the authority to implement some of these tools. The toolkit provides some points of consideration and does not represent an end-point for mitigating misconduct risk. While the onus is on firms to establish governance frameworks that take into account their business models as well as domestic legislative and regulatory regimes, authorities can play a role in addressing basic incentive problems (e.g. gaps between socially-desired outcomes and firms' private incentives) and assessing whether a firm's governance framework and processes are adequate and effective to support the sustained provision of financial services. As such, the toolkit is aimed at both firms and authorities.The toolkit will evolve as industry and supervisors alike learn from their experiences. For example, while some elements of approaches developed by supervisors and firms in response to recent instances of misconduct are included in the toolkit, many of them have not been in place long enough to establish a clear record of success.The tools do not constitute guidance and are not a recommendation for any particular approach. Nor are the tools meant to be taken as a package; firms and authorities may apply them separately or in combination to best conform to their business or supervisory approach and their legal and regulatory frameworks. They may also find that other tools are preferable. In sum, firms and authorities can decide whether and how to draw on this body of work to tackle the causes and consequences of misconduct. ..

Mitigating cultural drivers of misconduct

Firms

Tool 1: Senior leadership of the firm articulate desired cultural features that mitigate the risk of misconduct. A firm's senior leadership could articulate a clear cultural vision that will guide appropriate behaviour within the firm. To inform the cultural vision, leaders could adopt a risk-based approach that evaluates and prioritises the most significant cultural drivers of misconduct risk that may be inherent to their firm.

Tool 2: Identify significant cultural drivers of misconduct by reviewing a broad set of information and using multidisciplinary techniques. The senior leadership of the firm could strengthen its approach to mitigating misconduct risk by promoting the identification of significant cultural drivers of misconduct that are in conflict with the cultural vision articulated by the firm's leadership. The identification process could first involve collecting data and other information (from various sources and perspectives) that provide insight on behaviours that could lead to misconduct. Second, firms could apply multidisciplinary analytical techniques on the information gathered to obtain a more complete understanding of the drivers of these behaviours.

Tool 3: Act to shift behavioural norms to mitigate cultural drivers of misconduct. Senior leadership could take actions to shift attitudes and behaviours within the firm toward its cultural vision and to reinforce the governance frameworks designed to mitigate misconduct risk. Actions could be selected with reference to the most significant cultural drivers of misconduct identified by the firm (Tool 2) and based on the firm's operations. Such actions could include relevant informal and formal measures. Informal measures could include deliberate efforts by leaders to respond constructively to mistakes in order to create a safe environment for a candid dialogue and escalation of issues; more formal measures might include enhanced

whistle blower protection, escalation procedures andeffective compensation and related performance management mechanisms. Actions could also include monitoring the impact of interventions and making adjustments as necessary.

National authorities

Tool 4: Build a supervisory programme focused on culture to mitigate the risk of misconduct. National authorities could consider building a programme with a focus on supervising culture. Supervisory reviews of culture could be led by either firm-specific or subject-matter expert teams. Where an authority has governance or culture specialists, those specialists could work jointly with line supervisors to link observations related to culture with other supervisory issues at the firm.

Tool 5: Use a risk-based approach to prioritise for review the firms or groups of firms that display significant cultural drivers of misconduct. A risk-based approach to reviews could prioritise firms according to a comparative assessment of the cultural drivers of misconduct risk present within each firm. The depth of review could depend upon both the size and complexity of a firm or groups of firms under review, as well as the authority's own resources and the magnitude of misconduct.

Tool 6: Use a broad range of information and techniques to assess the cultural drivers of misconduct at firms. Qualitative and quantitative information that supervisors obtain from a firm could not only help supervisors understand how governance processes work, but could also provide insight into the behavioural norms and culture of the firm. The information could be shared through the firm's documentation, supervisory dialogue, specific meetings on the topic and/or meetings on other topics, as all supervisory interactions can provide supervisors with insight and information on a firm's culture.

Tool 7: Engage firms' leadership with respect to observations on culture and misconduct. Supervisors could engage in a range of methods to convey supervisory observations on behaviour and culture to the firms they supervise. A dialogue between a firm's leadership and supervisors could be useful to understand and bolster a firm's proposed actions to strengthen culture, where necessary, to mitigate misconduct risk. Engaging in a dialogue about culture could encourage firms to consider the issue more seriously.

Strengthening individual responsibility and accountability

Firms and/or national authorities

Tool 8: Identify key responsibilities, including mitigation of the risk of misconduct, and assign them. Identifying key responsibilities and clearly assigning them to the holders of various positions within a firm promotes individual accountability and increases transparency both within a firm and to relevant stakeholders. The identification and assignment of keyresponsibilities may be achieved through legislative or regulatory requirements, firm-driven decisions on their preferred structure, or both.

Tool 9: Hold individuals accountable. Individuals could be held accountable through a combination of (i) legislative/regulatory provisions; (ii) a firm's internal processes, including employee contracts; (iii) supervisory action; and (iv) regulatory enforcement. Clearly assigning responsibilities reinforces individual accountability and allows authorities to identify the functions and business activities for which individuals are accountable.

Tool 10: Assess the suitability of individuals assigned key responsibilities. Firms and/or national authorities could undertake assessments of the suitability of individuals (integrity and professional competency, including qualifications and experience) who have been assigned key responsibilities. Such assessments could take place at the time thoseindividuals first assume their responsibilities and periodically thereafter. National authorities

Tool 11: Develop and monitor a responsibility and accountability framework. National authorities could assess the implementation of a framework for responsibility and accountability that includes, inter alia, (i) the identification of key responsibilities for individuals in the firm, (ii) allocation of those responsibilities to specific individuals; and/or (iii) holding individuals accountable for the responsibilities to which they have been assigned.

Tool 12: Coordinate with other authorities. Supervisory techniques that aim to strengthen individual accountability through clearly assigned responsibilities could be deployed by more than one authority in the same jurisdiction. Approaches applied by one authority may have consequences for approaches that other authorities are considering. As such, national authorities could engage and coordinate with those authorities to understand their approaches to individual accountability.

Addressing the rolling bad apples phenomenon

Firms

Tool 13:Communicate conduct expectations early and consistently in recruitment and hiring processes.Firms have many opportunities during the recruiting and hiring processes to address potential employee conduct issues. Communicating clear, consistent messages about conduct expectations could deter some bad apples from pursuing employment at a firm that emphasises both high integrity and high performance. Silence as to expected employee conduct could signal that the issue is less important to the firm.

Tool 14:Enhance interviewing techniques. In addition to assessing the technical competency, experience and qualifications of candidates, the recruitment process could consider their behavioural competency and conduct history as well as their potential for adhering to the firm's values. This broadened review could be accomplished by asking particular questions or even by conducting a separate interview focused entirely on behavioural and conduct matters. Training in interviewing techniques to assess behavioural characteristics and spot "red flags" could add value to the interview process.

Tool 15:Leverage multiple sources of available information before hiring. Firms could search both publicly available and proprietary data sources for information about candidates. Current employees could have personal knowledge of a candidate's conduct at a previous employer. Previous employers are another possible source of information, though the extent to which firms are allowed, required or willing to share such conduct information could differ. Such information could require subsequent verification, depending on the number and credibility of the sources.

Tool 16:Reassess employee conduct regularly. Firms could update or renew background checks on regular schedules; for example, after three months or a year of employment or at career milestones, including promotions or lateral moves within a firm. In some jurisdictions,

institutions have to (re)assess the fitness and propriety of employees in functions deemed capable of causing significant harm to the firm or its customers.
Tool 17:Conduct “exit reviews”. Without prejudice to applicable legal requirements, firms could implement “exit reviews” and maintain appropriate records on former employees for their own potential future benefit as well as for prospective employers.

National authorities
Tool 18:Supervise firms’ practices for screening prospective employees and monitoring current employees. An assessment of firms’ employment and disciplinary policies and practicescould be embedded in the supervisory process. Supervisors could also require institutions to regularly reassess and revalidate the conduct or suitability of employees or a subset of them deemed to pose the greatest risk to the firm or its customers (see Tool 16).
Tool 19:Promote compliance with legal or regulatory requirements regarding conduct-related information about applicable employees, where these exist. Authorities could provide methods for firms to exchange meaningful information on employees. This could include promoting consistent and more comprehensive information in databases of financial services professionals, where they exist.

Questions

Do you think that the documents quoted here have the same ideas about risk culture, or different ideas?
To the extent that you see differences, what might explain them?
Do you think it is a good idea for supervisors of financial institutions to examine risk culture?
Is there a difference between thinking about controlling risk culture to improve the relationships between financial institutions and customers and thinking about misconduct in terms of misconduct risk for a financial firm?