‘Senior people somehow manage to keep their fingerprints off the relevant documents’

Is there now a fair and effective system of accountability for senior people in the financial services industry?

On 19 June 2013, the Parliamentary Commission on Banking Standards published its final report. Set up following the 2007-8 financial crisis and subsequent LIBOR scandal, the Commission issued a damning indictment of UK banking standards. ‘Top bankers’, it concluded, ‘dodged accountability for failings on their watch’.[1] Relying on claims of ignorance and collective decision-making, senior management evaded sanctions for the most ‘flagrant’ of abuses.[2] The Commission recommended numerous regulatory reforms, notably a Senior Managers Regime (SMR), to address the accountability vacuum in the UK financial sector. This regime, enacted through the Banking Reform Act 2013 and overseen by the Prudential Regulation Authority (PRA) and Financial Conduct Authority (FCA), forms the focus of the following essay.[3] The analysis will be two-fold: the new regulatory regime will first be analysed comparatively against its predecessor and then be examined in terms of actual and potential impact. It shall be argued that, despite its short existence, the Senior Managers Regime shows signs of being an effective and fair system of accountability but that its success is, as yet, only tentative.

I – Change of Regime

The Senior Managers Regime came into force in March 2016 and was extended in December 2018.[4] It now covers banking institutions, investment firms, building societies, credit unions,

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[1] Parliamentary Commission on Banking Standards *Changing Banking for Good: Volume I* (2013-14, HL 27-I, HC 175-I), Summary.
[2] Ibid.
[3] Financial Services (Banking Reform) Act 2013, pt 4.
[4] Terry Allen, ‘Strengthening the link between seniority and accountability: the Senior Managers Certification Regime’ (2018) *Bank of England Quarterly Bulletin* Q3, 2.

and insurers. It replaces the Approved Persons Regime (APR), which was roundly criticised by the Banking Commission as a 'complex and confused mess'. APR was found to operate only as 'an initial gateway to taking up a post' rather than as a continuing system of individual responsibility at senior levels.[5] Both narrow in scope and vague in its definitions, APR allowed senior individuals to delegate and deflect their responsibilities through complex management structures and opaque decision-making processes. In its construction, SMR is arguably well-suited to rectify the main deficiencies of APR.

SMR is a framework, underpinned by statute, through which named individuals at the highest levels of management are made accountable for specific responsibilities, known as Specified Management Functions (SMFs).[6] Each SMF must be allocated to a Senior Manager, who requires pre-approval by the PRA and/or FCA (depending on the function).[7] Allocations are recorded through individual Statements of Responsibilities and a Management Responsibilities Map, a single document detailing governance structures and reporting lines within the business. Senior Managers are also subject to more stringent Conduct Rules published by the regulatory bodies. Where a regulatory breach occurs, the PRA and FCA can pinpoint the Senior Manager responsible. This individual will be held personally accountable unless they can prove they took "reasonable steps" to prevent the alleged breach from occurring or continuing.[8] The burden of proof is reversed: under SMR, unlike APR, the onus is on senior individuals to rebut the presumption that they are responsible for the breach – rather than on the regulator to prove it. Extreme misconduct may result in criminal liability. Under section 36 of the 2013 Act, senior managers who make or agree to a decision that causes a financial institution to fail may be punished with a fine or up to seven years' imprisonment.[9]

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[5] *Changing Banking for Good: Volume I,* 86.
[6] Financial Services (Banking Reform) Act 2013, s 18.
[7] Bob Penn, 'Banking Regulation in the UK: Overview' (2018) *Practical Law*.
[8] 'Senior Managers Regime: Individual Accountability and Reasonable Steps' (2016) *Deloitte EMEA Centre for Regulatory Strategy.*
[9] Financial Services (Banking Reform) Act 2013, s 36.

Taken together, these measures mark an important departure from collective to individual accountability. Under SMR, high-ranking employees and executives are disincentivised from wilfully blinding themselves or keeping their fingerprints off relevant documents. They can no longer rely on the 'Murder on the Orient Express defence' whereby everyone, and so no-one, is held responsible.[10] The PRA and FCA, in turn, are fortified in their ability to pursue enforcement against individuals. The rigorous documentation of responsibilities provides a starting point for their investigations. It also means that obfuscation of accountability, as highlighted in the Banking Commission, is theoretically no longer possible. Compared to its defective predecessor, SMR offers far more clarity, coherence, and efficacy. Fairness, however, may be more contentious. Without a prescriptive list of what constitutes "reasonable steps", Senior Managers may feel uneasy, even fearful, as to the standards expected of them.[11] However, as highlighted by the former Chief Executive of the FCA the concept of reasonable steps should be 'common-sense': integrity in decision-making, proper delegation, regular communication, up-to-date training, and compliance with legal obligations.[12]

II – Impact

In the past three years the UK financial services sector has inaugurated a major new accountability framework. In intention – and detail – it significantly enhances individual responsibility within senior ranks of banking institutions. However, intention is not implementation and the regime may well work differently in practice. The Banking Commission in 2013 foresaw this possibility. It warned of the 'disaster' that would ensue if SMR 'were to

[10] Martin Wheatley, 'Nothing to Fear from High Standards' (*FCA* Bloomberg Speech, London, 2015).
[11] Ibid.
[12] Ibid.

relapse back into a one-off exercise' like APR.[13] While perhaps too early for definitive conclusions, the evidence so far suggests this is not the case.

The positive effects of the Senior Manager Regime were publicised in a recent Bank of England Bulletin. Experience 'to date' revealed that SMR was 'providing a positive discipline on firms and their key decision-makers'. According to the bulletin, banking institutions, especially larger groups, have benefitted from increased clarity of responsibility, better-documented governance arrangements, and more effective board oversight.[14] These comments are echoed in interviews with banking leaders published in 2019 on the FCA website.[15] Jon Symonds, Deputy Group Chairman of HSBC, notes that SMR gives regulators 'a much easier hook to put people on when things go wrong'. However, he stresses that SMR has been 'beneficial' for business: it 'improves' internal decision-making by providing an impetus for clarifying who is responsible for what and when. Jayne-Anne Gadhia, CEO of Virgin Money, also remarked that SMR is not 'trying to trip us up'. Instead, it 'codifies and professionalises' the sector, structuring boards and senior managers as they 'should have been behaving all along'.

So far, there exists only one example of enforcement under SMR. In May 2018 the FCA and PRA jointly fined James Staley, Barclays Group CEO, £642,430 for failing to act with due skill, care, and diligence in response to anonymous letters from a whistleblower.[16] Jonathan Ford, in the *Financial Times*, dismissed this as a mere 'slap on the wrist'.[17] However, it should be noted that the fine constituted 10% of annual income (minus 30% deduction for early settlement). Additionally, for the next two years Barclays must report to the regulators on its internal whistleblowing procedures. These sanctions seem to corroborate the statements made by bank

[13] *Changing Banking for Good: Volume I,* 104.
[14] Terry Allen, *Bank of England Quarterly Bulletin* Q3, 6.
[15] 'Banking Leaders' Experiences of Adopting the Senior Managers and Certification Regime' (*FCA*, Video Transcript, 7 January 2019).
[16] 'FCA and PRA jointly fine Mr James Staley' (*FCA Press Release,* 11 May 2018).
[17] Jonathan Ford, 'UK financial regulators are not as tough as they pretend' *Financial Times* (17 March 2019).

leaders above. In short, that SMR stimulates cultural change within financial institutions and, where these changes do not materialise, misconduct will be punished at an individual level.

III – Conclusion

The problem of accountability in financial institutions is not a new phenomenon. British bankers, legislators, and lawyers have grappled with such issues for over two centuries, responding, often haphazardly and with delay, to the teething problems caused by London's rise as an international financial hub.[18] Nonetheless, issues of accountability are particularly acute in the present day due to the global systemic risk posed by the failure of financial institutions. As a mechanism for imposing individual responsibility and accountability, the Senior Managers Regime is a significant improvement on the Approved Persons Regime. It has potential, which it is starting to realise, to perform a dual function: deterrence and enforcement.[19] This is evidenced at a technical level, in terms of how the regulation is constructed; and in reality, through the feedback that is starting to emerge as to its implementation. The more effective the regime is at embedding clearer lines of communication and higher standards of responsible decision-making, the less it will be needed in terms of enforcement. However, for this dual function to work effectively, the PRA and FCA must be rigorous in pursuing individuals when regulatory transgressions arise. If regulators become complacent in the face of misconduct they risk undermining the efficacy of the whole endeavour. If this occurs, SMR may be reduced to a glorified variant of APR. Whether it *does* occur will only be evident with time.

[18] Anthony Hotson, *Respectable Banking* (Cambridge: Cambridge University Press, 2017), 2-3.
[19] As discussed by Martin Wheatley, 'Nothing to Fear from High Standards' (*FCA* Bloomberg Speech, London, 2015).

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