Introduction

Public trust in the financial services industry had reached its lowermost point after the financial crisis, LIBOR and EURIBOR rigging scandals and has seen very slow recovery since[1]. Failures in senior management ('SM') oversight and their personal integrity remain recurring themes in investigation and enforcement. The Senior Managers and Certification Regime ('SM&CR') that aims to improve individual accountability is a cornerstone to push for a reform of governance in the industry[2].

The effectiveness of the SM&CR is limited as a legal tool, both due to its design and its potential inhibition on the free market, so it must be read in tandem with the cultural change that regulators and the public seek for the financial services industry to achieve. Fairness for all stakeholders can only be achieved if SM are held accountable for their conduct.

Has much changed?

At first sight, the requirements of the Statement of Responsibility and Prescribed Responsibility under the SM&CR seem to be a sharpened legal tool to finding SM culpable. SM are required to map out organisational charts, roles and responsibilities which may assist regulators in holding them accountable for failings within the organisation. However, once we compare the legal test under the SM&CR against the Approved Persons Regime ('APR'), it is apparent that not much has changed. Reasonableness is still at the core of proving whether a senior manager had been compliant with the Senior Manager Conduct Rules and their Duty of Responsibility; which is very similar to the requirements of the APR[3]. In cases that concern SM's competence to lead, the SM&CR would help investigations through tracing the trail of fingerprints by identifying the accountable manager's lines of responsibilities, but regulators are likely to face the same evidentiary hurdles as they do under the

[1] Edelman, *The Edelman Trust Barometer Global Report* (2019) pg46
[2] FCA, *Extending the Senior managers & Certification Regime to FCA Firms* PS18/14
[3] FSA Final Notice, *Mr Peter Cummings* (2012) PJC01301

APR; unreasonableness is a very high threshold to prove, as shown in the 2012 John Pottage case where the Upper Tribunal sided with Pottage's expert evidence and found that the FSA was unable to prove Pottage's behaviour as falling below a reasonable standard[4]. As the core of the legal test under the SM&CR still hinges on reasonableness, regulators will remain to struggle with the standard of evidentiary proof.

One would hope that the SM&CR will make it easier for regulators to catch SM who wilfully turn a blind eye to malpractice. There was indeed an opportunity to significantly shift the regulatory position under the SM&CR by placing a Presumption of Responsibility over SM, so that SM would bear the burden to prove that they had acted reasonably if a breach occured under their lines of responsibility. However, this would nevertheless be an unfair system of holding SM accountable as they would have to bear a heavyload burden of proof by being presumed guilty. The disproportionate risk of regulatory action also deters individuals from taking up SM roles. In 2016, the FCA finalised a watered-down version of the presumption by placing the burden of proof back with the regulator under the Duty of Responsibility[5]. This again explains how the SM&CR is not significantly different from the APR.

While the Management Responsibilities Maps under the SM&CR may help regulators trace fingerprints and identify the accountable senior manager in a breach, the high evidentiary threshold to the test of reasonableness means that SM&CR will not make it easier for regulators to find SM culpable. Perhaps the real value to tracing fingerprints lies not with the number of successful enforcement cases brought forth, but the message sent that actions are being watched, and SM should act with caution as they are under transparent scrutiny by regulators and the public.

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[4] *John Pottage v FSA* [2012] (FS/2010/33)
[5] FCA, *Guidance on the duty of responsibility* (2017) PS17/9

Undesirable side effect

The second challenge to the effectiveness of the SM&CR is that high fines create undesirable side effects. Under the APR, SM are more likely to cooperate in investigations as it is easier for them to keep their fingerprints off documents. However, under the SM&CR, there is a stronger incentive for SM to conceal information of a breach under their line of responsibility, as reporting a misconduct will likely invite investigation not only of the breach, but also the SM's Duty of Responsibility which they will have to disclaim, thus creating a perverse outcome of a disincentive to report.

SM&CR enforcement

In the Recommendation by the Commission on Banking Standards[6] , the legislative intent was clear that the SM&CR is not to place a rebuttable presumption of guilt over SM whenever misconduct occurs under their supervision. It asks SM to ensure an appropriate form of governance structure is in place. This is a view supported by regulators who echo the idea that the SM&CR is not to draw 'red lines'[7] for enforcement but to create opportunities for better supervision. Bailey highlighted how the SM&CR would be a step forward from the APR, as the APR 'focused on a notion of culpability not responsibility'. Despite this paradigm shift of focusing not only on culpability but accountability and responsibility, we are yet to see this being reflected in enforcement outcomes.

The James Staley case[8] had been an unfortunate start for SM&CR enforcement. Barclays Chief Executive Staley was only found to be lacking due skill, care and diligence under Rule 2 of the Individual Conduct Rules when he disregarded compliance rules and tried to investigate the source of a whistleblowing report. The case failed to drill into the core of the purpose of the SM&CR, which

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[6] Joint Commission on Banking, *Fifth Report-Changing banking for good* (2013) para 239
[7] Sam Woods, *Good cop/bad cop* (2018)
[8] FCA Final Notice*: Mr James Edward Staley* [2018] JXS02208

could have been an opportunity to explore the level of integrity (Rule 1) that SM are required of under the SM&CR. Unless we begin to hold SM accountable for promoting or being oblivious to poor cultures, we will be spinning wheels focusing on culpability and the reasonableness of a particular act or omission, making little or no progress from the previous legislative framework.

There is more to observe from this case. Despite the breach, Barclays made the statement to have 'unanimous confidence' in him. The level of support or even endorsement that the firm has shown to him put the private corporate and regulators in an almost antagonistic relationship. The role of regulators and the use of legal tools are rightfully limited to prevent an intrusive intervention to the free market. Perhaps the private sector should play a more involved role in policing the standard of integrity of SM in order to revamp the culture of the financial services industry.

With the case involving a major UK bank and a senior manager in the CEO position, it was a missed opportunity for the FCA and PRA to set the right tone for the SM&CR. But the full effectiveness of the SM&CR can only be seen when more cases are brought forth, and with more rules tested in court.

Increasing accountability and shaping good culture- a fair responsibility

Decisions that SM make can have a significant impact on the public economic wellbeing, which arguably places a prima facie duty on them to promote good cultures in their firms. The transparency under the SM&CR encourages SM to do so while giving regulators the power to supervise this process.[9]

[9] Andrew Bailey, *Culture in financial services- a regulator's perspective* (2016)

There is a prevalent view of a tradeoff between shareholders' and customers' values in the industry which stands as a major obstacle to changing culture. The financial services industry places a disproportional focus on creating shareholder value, which can easily be evidenced by the exaggerated size of the financial sector[10], and the exorbitant level of financing activities that are not generating real wealth to the economy at large. To survive the ever-evolving economic climates, SM should run their businesses focusing on profit responsibility, which is a progressive view being endorsed and adopted across the businesses world[11]. Whilst we can anticipate this attitude to be gradually promulgated within the financial services industry, the SM&CR will anchor and popularise this change by setting standards and expectations of accountability for SM to follow.

The APR had not offered sufficient scrutiny over SM's accountability, the SM&CR has not drastically changed the legal position, both because of the underlying legal test and the enforcement efforts to date. However, by etching clearer conduct rules, requiring management to outline their responsibility in writing, the SM&CR encourages a healthier lifecycle within financial institutions. Intrusive regulatory intervention will never be sufficient or appropriate in addressing the toxic culture within the industry. The private sector and SM must take on fair roles understanding and prioritising customer value rather than ticking compliance boxes to sustain the long-term success and viability of their institutions.

[10] IMF, *Rethinking Financial Deepening*
[11] Steve Denning, *Making Sense of Shareholder Value* (2017)