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UK Banks Brace For Greater Manager Accountability This Year

By **William Shaw**

Law360, London (January 9, 2017, 6:30 PM GMT) -- The U.K.'s Financial Conduct Authority last year served notice that senior bankers will face closer scrutiny of their accountability for misconduct at their institutions, but lawyers today say the full force and sweep of the new measures are still emerging and could change how financial bosses and in-house counsel operate by 2018.

The Senior Managers Regime kicked in last March, aimed at letting the regulator trace responsibility up to the highest levels within banks and insurers when something goes wrong

As FCA investigators' scope under the Senior Managers Regime expands to include traders, investment managers and perhaps even in-house counsel, many believe the rules will make it harder for top bosses to make decisions without worrying about legal consequences. (AP)

The year closed without major prosecution, but legal experts now expect that to change as FCA investigators pursue leads and their scope expands to include traders, investment managers and perhaps even in-house counsel.

Attorneys have growing concerns that the rulebook will dramatically alter the role of counsel, and pile on legal fees and administrative costs for new safeguards. Many believe the new rules will make it harder for top bosses to make decisions without worrying about legal consequences.

"We have heard anecdotally that some banks now have a lawyer present at every meeting and that as a result decision-making is becoming increasingly bureaucratic," said Adrian Crawford, an employment partner at Kingsley Napley specializing in financial services clients.

"This may be good and necessary for the protection of individual senior bankers, but not so good ultimately for agile decision-making and the efficiency and competitiveness of the City," he said of London's financial center.

The SMR is part of a wide-ranging overhaul of financial regulation in the wake of the 2008 financial crisis and a barrage of market manipulation scandals, including efforts to rig the London-Interbank Offered Rate, a key interest rate benchmark.

Manager accountability became a hot political topic in the U.K. after taxpayer funds were used to prevent a number of major institutions from going under in the crisis, including Royal Bank of Scotland Group PLC and Lloyds Bank PLC.

Similar scandals shook public faith in financial markets, and regulators on both sides of the Atlantic faced fierce pressure to hold top bankers to account.

For the U.K., the regime involves firms submitting detailed maps outlining who is in charge of what, along with individual statements spelling out each senior manager's responsibility. Executives are left liable to a fine unless they can prove they took adequate steps to prevent wrongdoing. Critically, firms must hold detailed paperwork on who made what decision and how.

On Monday, the FCA closed a consultation on one of the most controversial parts of the regime: whether the rules apply to in-house lawyers. The regulator has not decided whether to force senior company lawyers to disclose conversations with the firm's directors, but the prospect has sent shivers through the legal profession.

The Law Society itself, which represents Britain's solicitors, fears a threat to client confidentiality that could deter banks from seeking legal advice. The group has urged the FCA to grant an exemption, warning that firms could be deterred from consulting lawyers at all.

“It is important that [the privilege] is not compromised and that our justice system is not undermined by the unintended consequences of regulatory change,” Law Society chief executive Catherine Dixon told the FCA in a statement last month.

The FCA acknowledges the industry's concerns. The watchdog wants to balance lawyers' independence and their ability to offer privileged and confidential advice with the regime's principles and expectations.

Back in January 2016, it conceded there was a lack of clarity on the status of senior in-house counsel.

“We now recognize that some confusion exists in this area and our communications have not necessarily been sufficient to ensure that firms have full clarity,” the FCA said at the time.

By 2018, lawyers expect the rules to be extended across the financial sector, potentially netting investment managers, brokers and dealers as well as bankers and insurers. The FCA was tight-lipped about its plans on Monday, but said it plans to consult this year on extending the regime to all firms authorized under the Financial Services and Markets Act 2000.

“Going forward, it will extend to all financial services regulated firms, so it will have a much wider impact,” said Peter Snowdon, a partner at law firm Norton Rose Fulbright LLP. “At the moment, we don't know the full scope of it because we have yet to see anything from the FCA.”

Snowdon says the regime will pose particular challenge to so-called “certified persons,” including individual investment managers and traders. These staff will no longer need FCA approval, but every year firms will have to reassess whether they are still fit and proper. This will require much tougher procedures and paperwork around appraisals, training, references and disciplinary action.

Costs could spiral as firms prepare their compliance, with accounting giant Ernst & Young predicting “significant impact” on the industry this year, when it comes to governance, risk management frameworks and individual liability.

"Firms will have to be much more closely aligned to what employees are doing. It’s a lot more work than people appreciate,” Snowdon said. Some bigger firms may have up to 150 traders who all need to be processed individually. Companies could struggle, for example, if an employee misses a key training session while at home on paternity leave.

“It’s not something you can put in a drawer and leave somewhere,” he added. “It’s got a lot of day-to-day administration attached … If their function changes, their job changes, and you have to go through the whole thing again.”

But it isn’t just financial services lawyers who have concerns. Guy Wilkes, a financial services, regulatory and enforcement partner at Mayer Brown, says the FCA has been unimpressed by the way some firms have drafted maps of executive responsibility. These maps are supposed to let regulators establish where the buck stops.

“In producing the map, the FCA has not been entirely happy about how they have done it,” said Wilkes, previously head of an enforcement department at the regulator.

“The FCA wants to see a few high-placed individuals who carry the can,” he said. “Some banks have been pushing responsibility too low down through the food chain. The FCA and [Prudential Regulation Authority] have been pushing back against that and some banks have had to rethink.”

The FCA said on Sept. 28 that on the whole it had been pleased with banks' efforts to comply with the new rules so far. FCA Chief Executive Andrew Bailey said the watchdog had "seen genuine engagement on this from the board down."

At the same time, however, the FCA cautioned that in some cases firms had "overlapping or unclear allocation of responsibilities." In others, it warned, financial institutions seemed to be "sharing responsibility amongst more junior staff, obscuring who is genuinely responsible."

--Additional reporting by Melissa Lipman. Editing by Ed Harris and Rebecca Flanagan.