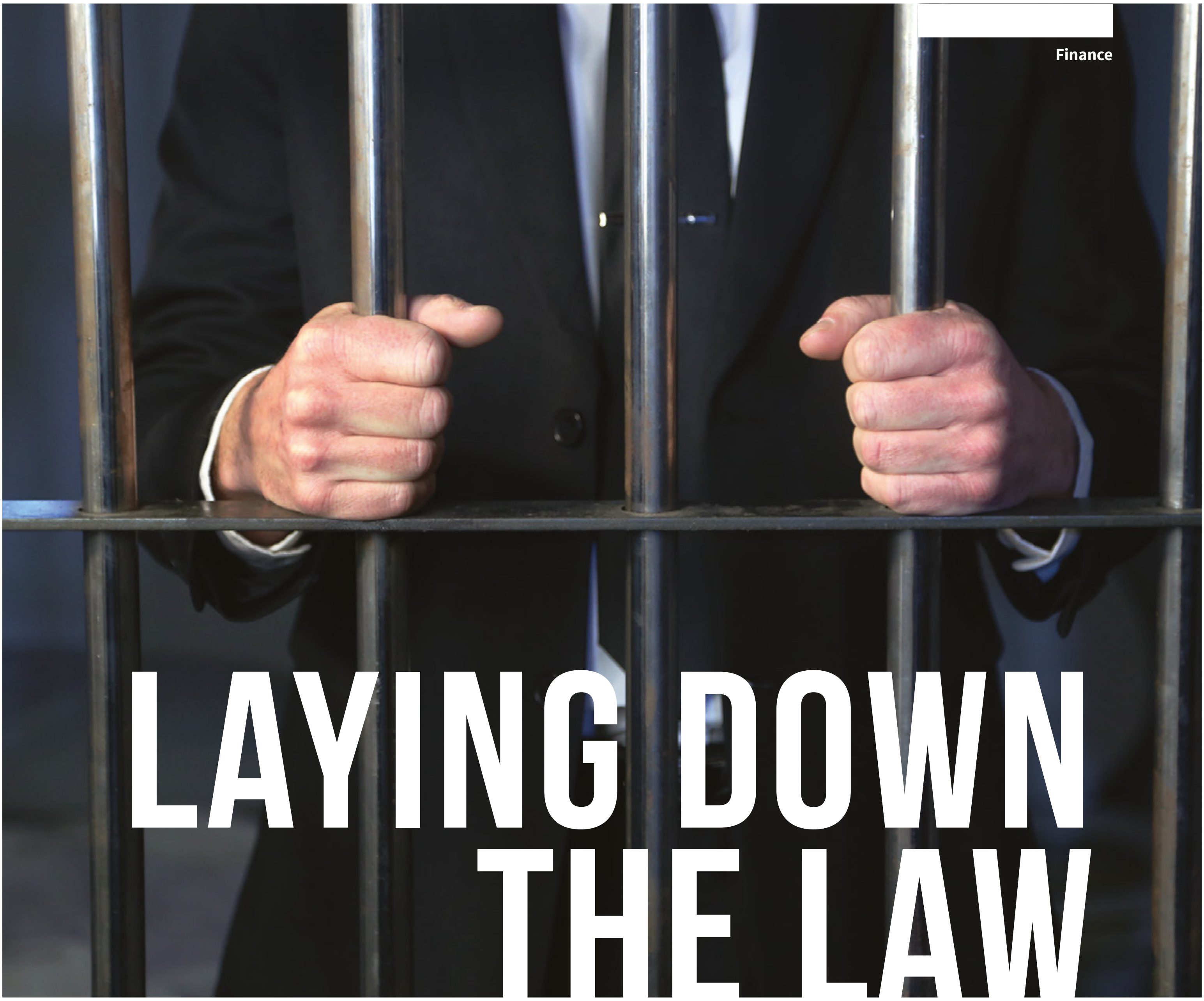

LAYING DOWN THE LAW

INSTITUTIONS AND INDIVIDUALS OFTEN ONLY FACE A FINE FOR THEIR FINANCIAL TRANSGRESSIONS – SO DOES ENFORCEMENT GO FAR ENOUGH OR SHOULD THE PERPETRATORS BE PUT BEHIND BARS?

Words:
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SINCE THE BANK failures that produced the financial crisis, we've had numerous banking scandals, including HSBC laundering drug money for Mexican drug cartels; manipulation of the Forex markets; LIBOR fixing; the gold price fix; RBS and the actions of its Global Restructuring Group; the Wells Fargo fake accounts scandal; and the HBOS Reading fraud.

In most of these cases, the banks received fines. HSBC paid $1.9bn to the US authorities in settlement for money laundering in 2012; Bank of America, UBS, RBS, JP Morgan, Citigroup and Barclays were fined a total of $9bn by US authorities and the Financial Conduct Authority (FCA) for rigging foreign exchange markets in 2015; and Barclays was fined £26 million by the FCA in 2014 for manipulating the price of gold, with one of its traders banned and fined for inappropriate conduct.

Indeed, banks globally paid $321bn in fines from 2008 to the end of 2016, for an abundance of regulatory failings, from money laundering to market manipulation and terrorist financing, according to recent data from Boston Consulting Group.

In the UK, it was only in the case of the LIBOR scandal, prosecuted by the Serious

Fraud Office (SFO), and the HBOS Reading fraud (prosecuted by Thames Valley Police) that anyone was jailed. Moreover, these weren't senior bank staff but 'foot soldiers', traders, or mid-level managers.

Consequently, there's a feeling among certain groups that the people running financial institutions on both sides of the Atlantic are seemingly above the law and that the penalties imposed for 'misdemeanours' simply aren't sufficient to act as a deterrent.

So why have so few people been jailed? Is there a problem in assigning accountability? Is there a lack of appropriate legislation. Or is it because of a lack of enforcement?

According to Anat Admati, Professor of Finance and Economics at Stanford University: "All of the above are reasons for a fundamental lack of accountability."

In a notable essay entitled *It takes a village to maintain a dangerous financial system*, she wrote: 'In banking, the public interest in safety conflicts with the incentives of people within the industry. Protecting the public requires effective regulations because market forces fail to do so. Without effective regulations, dangerous conduct is enabled and perversely rewarded. Because the harm is difficult to connect to specific policy failures and individuals, it persists.

'Even if a crisis occurs, the enablers of the system can promote narratives that divert attention from their own responsibility… The narrative that crises are largely unpreventable shifts attention to emergency preparedness and away from better rules to reduce the frequency of emergencies in the first place.'

Ian Fraser, an investigative journalist who wrote *Shredded: Inside RBS, the bank that broke Britain*, broadly agrees. He acknowledges that "the way bankers are incentivised – which hasn't really changed that much since the financial crisis – drives them to push the envelope and, in extreme circumstances, to turn a blind eye to, or commit financial crimes.

> **THERE'S A FEELING AMONG CERTAIN GROUPS, THAT PEOPLE RUNNING FINANCIAL INSTITUTIONS ON BOTH SIDES OF THE ATLANTIC ARE SEEMINGLY ABOVE THE LAW**

"The real problem, and the reason you get recidivism in financial services, is because of Deferred Prosecution Arrangements and other settlements between regulators and financial institutions. These give the individuals responsible for the criminal behaviour – which could be LIBOR rigging, false accounting, money laundering, all manner of financial crimes – a 'get-out-of-jail-free' card."

LEVEL OF PUNISHMENT

Responsibility for imposing penalties depends on the nature of the crime. An FCA spokesperson says a distinction must be made between regulatory infractions – where a firm or individual breaches its rules or principles for businesses – and a criminal case, where they break the law.

This spokesperson stresses that the regulator has punished banks with fines, where appropriate, although the FCA also has the power to prosecute some offences through the criminal courts – for example, insider trading.

It's the SFO that generally investigates and prosecutes the most serious or complex cases of fraud, bribery or corruption, where a jail sentence is more likely. But in such criminal prosecution cases, the burden of proof is higher – beyond reasonable doubt – than for civil enforcement.

Still, shouldn't criminal charges be more common, especially for people running these institutions?

This is certainly the view of Jonathan Fisher, a barrister who specialises in fighting corporate wrongdoing. "It's unacceptable that companies bearing a responsibility for their contributing conduct – for their failure to supervise and have adequate systems in place to prevent economic crime – haven't been required to answer for that failure in a criminal court."

The direction of travel seems to be increasing corporate liability for failure to prevent financial crime. With the UK *Bribery Act* (aimed at bribery and corruption) and the recently introduced *Criminal Finances Act* (aimed at tax evasion), prosecutors must only prove a corporation failed to prevent a crime, rather than direct complicity. Under these acts, any penalties for a criminal offence are imposed by the court and there are no statutory minimums.

RAISING THE BAR

The SFO appears to be more bullish on amending corporate criminal liability law to ensure the people at the top are punished for financial crimes. It's been arguing that, apart from bribery and tax evasion, the law should encompass fraud, theft, false accounting, and acquiring and concealing the proceeds of crime.

Hannah von Dadelszen, Joint Head of Fraud at the SFO, was quoted in the *Financial Times* as saying: "Increasing the scope of corporate criminal liability would have a massive impact on the way we are able to prosecute."

David Cadin, Managing Partner of law firm Bedell Cristin, doesn't think regulators need more powers. "They need more structure," he says. "We should decide what we want to achieve and what the rules should be, so that the regulators have a transparent framework within which to work."

Others, however, are much more critical. Indeed, Ian Fraser argues: "To an extent, they don't fully use the powers they have. But there's also a widespread view that the FCA, in particular, is a 'captured' regulator, to the extent that a lot of the senior people from there go through a revolving door to much higher paid jobs in banks, then come back again."

> A DISTINCTION MUST BE MADE BETWEEN REGULATORY INFRACTIONS AND A CRIMINAL CASE WHERE FIRMS BREAK THE LAW

Naturally, the FCA rigorously disputes this, with their spokesperson stating: "The FCA is aware of both the potential risks and benefits of this movement. As part of our Code of Conduct, the FCA actively manages possible conflicts of interest when an individual accepts a new role outside of the FCA. We will move an individual to a role that removes any conflict of interest during their notice period."

The SFO comes out only slightly better in Fraser's estimation. "The SFO is definitely under-resourced and it is pretty incompetent," he claims.

Cadin agrees that, given the events of 2008, the current system is evidently not working. His solution appears enticingly straightforward. "To improve, all institutions should lay down internal rules, which need to be clearly defined and regularly measured against."

Others are convinced that the laws must be changed and enforced. Anat Admati explains: "There isn't a 'silver bullet' answer to get corporations to act on behalf of society. We probably need to change laws to create more accountability."

Ian Fraser adds: "I think the solution is to apply the law as you do in other areas of human activity. Why should there be a two-tier justice system, whereby bankers appear still to be able to commit crimes with impunity and just walk away with their pensions and their past bonuses? It is just wrong."

Clearly, some feel strongly that financial enforcement needs to go much further to deal with financial wrong-doing in the UK if corporations and the people running them are to be properly accountable. Choosing the way forward might not be so straightforward. ■

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THE VIEW FROM THE CHANNEL ISLANDS

Enforcing financial regulation is a mammoth task and David Cadin, Managing Partner at Bedell Cristin, believes it's easier to regulate in the Channel Islands. "We have more engaged regulators in the islands who are closer to the businesses and have a better understanding of their activities," he says. "We also have a shorter regulatory chain and people who work to ensure that the islands' reputations remain strong by being at the forefront of regulatory standards and transparency."

This is also the view of John Harris, Director General of the Jersey Financial Services Commission. "It's a lot easier in a small place like Jersey. As the regulator, we take regulatory action when offences are committed, we work hand in hand with our investigation and criminal prosecution colleagues. We share information, intelligence and evidence according to standard protocols, and we work out who is best placed to take a case forward.

"The key message I would like to get across is that obviously Jersey is a different ecosystem than the UK. The legal structure and apparatus are simpler. The regulator is the sole regulator and works with counterparts in the island's sole criminal prosecution authority and the police authorities. In this small jurisdiction, the liaison, the delineation and demarcation lines relative to an active case are easier to manage."