New City Initiative

From Magnus Spence, Chairman of The New City Initiative, and CEO of Dalton Strategic Partnership.

The UK's Banking Standards Review is in principle a timely opportunity to try to ensure that egregious mistakes of the past are not repeated.
However, the organisation that may result from this Review is in our view likely to fail in its key mission – to raise stability in banking . The new body being proposed is neither bold enough, nor sufficiently far-reaching, nor will it have teeth to punish those whose behaviour falls below the expected standards. It fails to address a complex failure, one composed of tangible structural elements and intangible ethical factors.

Question 6 of the Review goes to the heart of the matter. It asks: "Do you agree that the new body should initially work with banks and building societies rather than individuals? What are the pros and cons of aspiring to build individual membership?" This question links to an initial statement in the Review regarding qualifications: "Very large numbers of people are employed by banks in the UK – more than 400,000 by the UK banks alone. Their qualifications, where they exist, are far from uniform…Trying to corral such a large and diverse group on a voluntary basis into a single new professional body starting from scratch with no track record would be very difficult."

Yet all the recent past misdeeds in banking stem from individuals who, either independently or encouraged by a culture of financially-incentivised excessive risk-taking, have failed to behave ethically. It may be "difficult", but unless individual bankers who aspire to any senior level become professional, then the proposed new Banking Standards' body will end in failure, and we may one day face a fresh banking crisis.

What do we mean by becoming professional? Other professions, such as accountancy or law, impose extremely stringent qualification requirements on individuals who wish to practise; yet these professions do not pose any financial or economic systemic risk. Accountants are required to undergo the completion of stringent courses, examinations, and practical experience, sanctioned by Charter. A single, unitary body, specifically for bankers, needs to be established, individual membership of which would be regarded as a sine qua non to practise. Those who wish to work as bankers should be required to demonstrate that they aspire to a higher set of cultural and ethical standards; that demonstration needs to be sanctioned by a professional banking Charter.

Individuals occupying important positions within banks should be required to be a member of the Charter. To remain Chartered, those individuals should be required to demonstrate continuous professional development. This professional body would set standards that exceed the minimum required by regulatory authorities, and would have the power to remove Charter status from individuals.

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The numerous failures of the UK's banks ultimately derive from the failure to align the interests of employees with those of their customers. Banks have generally incentivised their staff to take risks with other people's money, risks that usually they would not have taken with their own. This structural error created an 'ethical gap', in which the principle of "customer first, firm second, me last" was inverted. You refer to an EIU global survey of 382 financial services' executives, in which more than half the respondents "felt that career progression at their firm would be difficult without being 'flexible' on ethical standards."

The rot has evidently gone deep, but the proposals that the new Banking Review Commission will "have no statutory powers", and that the banks' involvement "will be on a voluntary basis" do not give cause for optimism. Without a Charter, , the Banking Standards' body will be regarded as toothless. Given that it will be funded by the very institutions that are in the dock, it may also face strong headwinds from a sceptical public.

The New City Initiative is an alliance of asset management firms that are privately-owned and predominantly small-to-medium in terms of assets under management. None of The NCI's members pose a systemic risk, yet they all have voluntarily adopted the principle of aligning the interests of their firms with those of their clients. The common ground of all our members is that – far before any legislative compulsion – they invested their own money into the funds they manage on behalf of clients. In other words, risk is born by both the client *and* the firm; this is a structural encouragement not to behave unethically. This is an important distinction from the banks; it bolsters the necessary ethical principle, "customer first, firm second, me last". The inculcation of ethical behaviour in financial services needs structural underpinning, by aligning the financial interests of employees with those of their customers, and by the establishment of a universally recognised professional body for individual bankers.