



LORD CHIEF JUSTICE
OF ENGLAND AND WALES

THE RT HON. THE LORD THOMAS OF CWMGIEDD

OPENING REMARKS

WORTHY OF TRUST? LAW, ETHICS AND CULTURE IN BANKING
BANK OF ENGLAND

Tuesday, 21 March 2017

1. It is a great pleasure to join the Governor of the Bank of England, Mark Carney, and the President of the Federal Reserve Bank of New York, William C Dudley, on a subject that is so important. It is the greatest pleasure to do so with Dame Colette Bowe as our chair. She has done so much to lead the Banking Standards Board and get us to where we are today.

The role of a culture of ethics and integrity

2. A way of looking at a viable financial system is to see it as built on four pillars:
 - (1) Expertise.
 - (2) Innovation.
 - (3) Law, and its much younger cousin, regulation.
 - (4) Ethics and integrity.
3. What I think has become increasingly clear is that these pillars are not isolated; they are interconnected. We depend on all four. The global financial crisis revealed first that the pillar of law and regulation needed strengthening; second that the pillar which consists of ethics and integrity is far too weak.

The limited role of law and regulation

4. Law and regulation now by and large operate, though with exceptions that need ironing out, as a coherent whole. However, prior to 1982, apart from statutory regulation directed largely at solvency, and save where the criminal law intervened, or in the few disciplinary proceedings that took place, the power of regulation was effectively the ability of the chairs of City institutions, such as Lloyd's or the Stock Exchange, and the Governor of the Bank, to remove from the system those whose conduct

5. There was certainly a perception that this comprehensive structure for regulation would control the risks in the financial markets to a much greater extent than the system it was replacing. It would operate in such a way as to make those actually responsible accountable, whatever their seniority; it was no use having a system of regulation that simply acted against those at the bottom of the pyramid. However, the system of law and regulation established between 1980 and 2000 was shown, by the financial crisis, to be inadequate. Much essential work has been done to address the inadequacies and to make the system work more effectively. The courts and the regulators respectively have, for example, been tough on those who have broken the law or regulatory regimes, but only the few that have been brought before them.
6. However, law and regulation on their own will never be enough. Even when we are agreed on the principles that should apply, it has never been enough. As reflected in the basic principles on which our law was developed, everyday business life is conducted on the assumption that you choose carefully the person with whom you do business and enter into business only with a person in whom you believe you can trust. That is so because it is quite impossible to devise a legal or regulatory regime that can supervise the conduct of another party to a bargain. Unless you wish to buy yourself a dispute, you would never contemplate entering into a contract with someone whom you did not trust; it is perhaps a marked feature of a failure to understand this principle that has led many to believe a good contract can solve all the problems. That is to misunderstand the limited role that a legal or regulatory regime can achieve. The better view is that expressed by Bowen LJ in 1883:

“Mercantile genius consists principally in knowing whom to trust and with whom to deal.”

7. Let me take the late Mr Robert Maxwell as an example of the importance of trust and the limits of regulation. In a report published in 1971, Inspectors appointed by the predecessor of the Department of Business had concluded that he was not a person who could be relied upon to exercise proper stewardship of a publicly quoted company. In 1988, when Mr Maxwell applied to the then regulator to be the chairman of the investment managers of the pension fund, he was approved. The distinguished chairman of the regulator was recorded as observing that it was “a pity that we could not exclude that crook”. He was in effect driven to that view because Mr Maxwell was the kind of man who would have challenged the regulator in court and a regulator cannot act without hard evidence. As my co-Inspector and I concluded in 2001 in the Report into Mirror Group Newspapers:

“An approval is more in the nature of a negative clearance rather than a positive approval.”

8. Given the limited effectiveness that law and regulation can ever hope to achieve in the fair and proper operation of markets and commerce, we cannot afford to leave work on the pillar of integrity and ethics underdeveloped. As is obvious, work on this pillar is difficult; it is systemic and long term. It is not made easier by the fact that not everyone believes that the pillar can or need be strengthened.
9. But strengthened it must be, for, as I have explained, law and regulation are not enough. There is a further imperative: markets are increasingly driven by innovation. Gone are the days when the practice of a business or market was something learnt at 18 or 21, and you could happily work with that knowledge for the rest of your life without needing to learn anything new. A by-product of innovation is that it takes time for law and regulation to catch up. In our common-law world (and I cannot stress enough the importance of the Common Law), we can move forward more rapidly through our case law, but such development must await disputes which may take time to arrive in the courts. Were we to depend on regulation, it is inevitable that time is needed to agree on the principles applicable to an innovative product. Over-zealous or premature regulation can stifle innovation. There is therefore a second reason for the development of ethical standards.

Building ethical standards

10. How are we to do this? As many know, I have strongly supported the engagement of the judiciary with the finance sector and with leading academics through the Law and Ethics in Finance Project. May I draw some parallels with the law?
11. The same four pillars underpin the law. No amount of expertise, innovation or regulation can make the legal system work acceptably if ethics and integrity are not also present, constantly valued and encouraged. We could not run a case well without them, let alone a system.
12. At the core are:
 - (1) The fostering of a vocation.
 - (2) A clear but simple code of ethical standards. The spirit should triumph over the letter. There must be an appreciation that ethical standards go beyond what is to be found in any code and the focus must be on professionalism.
 - (3) Proactive development and education in ethical standards from the start of a professional career. Senior leaders must instil this culture and set an example.
 - (4) A culture of adherence to those standards. In the courts, we can give effect to this culture through the duty owed by all who practise before the court - a duty which overrides any duty to the client.

- (5) Accountability for adherence to those standards with clear transparency. We have developed in the courts processes for explanatory accountability. We will expose to public criticism those who fall below those standards; we have done this because we have found that disciplinary proceedings under regulation have not been as effective as they should and the courts cannot operate without the highest standards of integrity.
 - (6) Public recognition and appreciation of those who abide by standards. It is those who act with integrity in performance of their duty who are trusted by the courts and by their professional colleagues. They win the highest accolade – universal respect.
 - (7) The interaction of these actions provides the necessary incentives and the necessary deterrence.
13. We are realistic and appreciate that there will be some who will never act in accordance with these standards. Our objective is to ensure that these are few and do not damage the reputation of the system.
14. Thank you.