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To Restore Trust in Banks, Build Ethics into Business Decisions

By Jeremiah Buckley And Thomas Sporkin

Trust is the bedrock upon which the banking business is built. However, revelations of unethical conduct at some banks have put that trust at risk. Senior officers of the Federal Reserve and other financial regulators recently met with management at leading banks to emphasize the need for a stronger ethical culture in the wake of activities like Libor manipulation, front running in high-frequency trading and money laundering cover-ups. William Dudley, the president of the Federal Reserve Bank of New York, said in a recent speech that there should be a "consistent application of 'should we' versus 'could we' in business decisions." The Financial Conduct Authority in the United Kingdom has expressed similar concerns.

Bank leaders understand the importance of trust and the need to demonstrate their commitment to maintaining an ethical infrastructure at their institutions. In this regard, bankers can take personnel and policy initiatives to put ethics front-and-center and show they "get it."

One approach would be to explicitly place the responsibility for ethics compliance — not just rule-checking compliance — with one or more employees. Another is adopting guidelines requiring that major business initiatives include an ethics component in the decision process. We are not suggesting that any specific structure or personnel is right for all banks, and variation in approaches is appropriate. But in light of the unfolding revelations of ethical lapses, a clear signal that a bank has a focus on ethics will help to restore faith in the integrity of these institutions that form the fabric of our financial services sector.

In some banks, general counsels are considered de facto ethics officers (and sometimes even hold the title of chief ethics officer). In other banks, a chief ethics officer or similarly-titled individual is designated outside the legal department and is often paired with the chief compliance officer role, but the authority of such officers varies.

If a bank decides to have a formally designated individual with principal ethics responsibility, what steps should it consider to make the role effective? He or she should have tangible responsibilities and specific authority to sanction ethical lapses, the commitment of the board of directors, buy-in from the CEO and senior management, and adequate resources. Such an executive, working with a board committee, could update and promulgate the company's ethics policy and be responsible for training employees about their ethical responsibilities. He or she could help to illuminate decisions about what is "right or wrong," even where there may be a legal argument to justify an institution's proposed products, pricing or conduct. He or she also could be the senior officer to whom whistleblower complaints would be directed.

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The ethics officer might also be charged with identifying and investigating wrongdoing involving individual conduct to help ensure that the institution's ethical culture is grounded in ethical behavior and not simply an abstract policy. In addition, he or

she could be an advisor on products, services and programs, evaluating them in the light of fairness to their intended users.

One alternative or supplement to appointing a single officer to champion ethics is to require that bank decision processes explicitly incorporate ethics — whether the bank "should" as opposed to whether it "can" — into major decisions on products, programs and business initiatives. Especially given the subjective nature of ethical requirements, making ethics decisions part of a process that will incorporate the views of multiple executives may assist in capturing a broader corporate consensus.

In addition to facilitating improved ethical culture, a focus on ethics could benefit banks in other ways. When faced with an enforcement action, a bank with an ethics executive or other ethics-oriented process that has uncovered problems and corrected them should be given credit by regulators when it comes to imposing sanctions. Moreover, federal and state regulators should form an explicit policy of promoting self-regulation by encouraging, rather than punishing, internal corporate initiatives to root out ethical lapses.

The role of an ethics executive is a sensitive one, requiring both good judgment and fortitude. An overzealous ethics executive can do as much harm as a weak one. To assure a proper balance, any ethics officer should operate under the direction of an institution's board of directors. In the end, regardless of the processes that a bank uses to incorporate ethics into its decision-making, it is the bank's board, with its policy and management oversight responsibilities, that must assure that the institution maintains its most valuable asset: public trust.

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