Final

Name of author:

Dr Ilias Kapsis,

Senior Lecturer in Law,

Faculty of Management, Law and Social Sciences

University of Bradford,

Bradford,

West Yorkshire,

BD7 1DP

Author biography:

Dr Ilias Kapsis is a Senior Lecturer in the Law School of the University for Bradford, United Kingdom. His research interests include Banking & Finance Law, Law of Sustainable Development and Competition Law.

"Sticks or carrots? How to make British Banks more socially responsible".

Abstract

The relationship between banks and society in UK remains fragile more than 10 years after the financial crisis. The level of public mistrust, though lower than in the aftermath of the crisis, still remains at unsatisfactory levels especially as scandals continue to plague the sector. This raises the question of the effectiveness of reforms adopted in UK during the past 10 years to improve the public oversight of banks and change their culture. The reforms resulted in a significant expansion of the scope of financial regulation through the adoption of large numbers of new rules with binding effect on banks. In addition, new supervisory bodies were created to more closely monitor bank activities. This paper reviews the effects of the reforms on bank culture and concludes that expanded regulation and compulsory norms brought about mixed results and had only moderate effect on repairing the relationship between banks and UK society. The paper argues that more significant cultural change could come only from the banks themselves and therefore, going forward, the scope of compulsory norms should be reduced. The paper contributes to the ongoing dialogue between industry experts, policy makers and lawyers about the optimum levels of financial regulation especially in light of recent calls for rolling back parts of public interventions in the financial sector.

Keywords: Corporate Social responsibility, UK, banks, culture, financial regulation, binding norms, financial crisis, financial institutions, bonus, crisis.

Introduction

More than ten years after the financial crisis of 2008, the British public still does not trust their banks. Several surveys of public opinion in 2018 confirmed that whilst there have been some improvements in UK banks' public image since the crisis, a large part of the UK public still shows negative attitudes towards banks. By way of example, the August 2018 survey of Yougov for Positive Money found that 66% of the British Public do not trust banks to work in the best interests of UK society and 63% fear that UK banks may cause another financial crisis[1]. These findings are consistent with findings of similar surveys in previous years such as the 2017 Populous survey[2], which found that less than half of the UK public trust any bank to do the right thing. A 2013 Report of the Parliamentary Commission on Banking Standards (PCBS) found[3] that the UK public was angry because it felt that the banks took advantage of its members, that bankers took excessive rewards not justified by their work and that they were not accountable for irresponsible and dishonest behaviour. The report and other documents described a culture of greed and corruption which had ruined the relationship between banks and society in UK.[4]

Similarly, a Yougov-Cambridge public survey in 2013 found that 73% of those surveyed described the reputation of banking as bad and only 4% believed that banks observed high ethical and

[1] see Positive Money, "Polling: 10 Years After the Financial Crisis, the British Public Still Don't Trust Banks", 16 August, 2018, available at https://positivemoney.org/2018/08/british-public-dont-trust-banks/
[2] Available at https://www.populus.co.uk/2017/12/trust-banks-went-wrong-fix/
[3] Parliamentary Commission on Banking Standards, (2013) 'Changing Banking for good', Final Report, vol.I, p.15, available at http://www.parliament.uk/documents/banking-commission/Banking-final-report-volume-i.pdf
[4] Ibid.

moral standards [5]. The UK press and various commentators have often branded the bankers "criminals" and the financial institutions "criminal institutions"[6].

A leading reason for the high level of public discontent can be found in the consequences of the financial crisis, which had significant economic and social costs. Several scandals[7], which continued to plague the sector post-crisis, made the situation for banks even worse. Bank leaders have often been forced to acknowledge their level of responsibility for the negative public opinion and several declared their willingness to do whatever it takes to win back public confidence[8] although more pessimistic views refer to negative public perception of banks "for a generation"[9]. Bankers defending their social contributions highlight, between others, the significant work they have done to support the national economy and the local Communities[10].

One of the focal points of criticism based on the surveys of public opinion and government reviews of the sector is the prevailing culture within banks, which is deemed to be generating greed and corruption. Culture has various definitions. A working definition used here is: "learned knowledge, belief, art, morals, law and custom in society"[11].

After the financial crisis UK society targeted particularly the established beliefs of bankers and the moral aspects of banking, whilst seeking the adoption of a new legal framework which would be imposing stricter public controls on banks. However, bringing about the required change in morality is a complex and difficult task requiring long term efforts in order to produce tangible results. There are also serious doubts about the ability of regulation to lead such efforts. Market-driven and banks-led initiatives may be more effective. A central aspect of voluntary activities with focus on the relationship with society is linked to corporate social responsibility (CSR).

CSR is a term with global significance. It refers, broadly speaking, to processes and actions through which corporations voluntarily acknowledge their responsibility to the broader society and not only to their shareholders. CSR is an essential tool in the efforts of corporations to build a posi-

---

[5] YouGov-Cambridge (2013) "Public Trust in Banking - YouGov", Report.
[6] See e.g. Bosworth-Davies R. (2015) "The emergence of the criminal financial institution: can effective measures be implemented to deal with them?" *Comp. Law*. 2015, 36(10), 307-309.
[7] The sector faced negative publicity due to bank collapses resulting in massive taxpayer bailouts and other costly public financial support, the libor scandal, the culture of excessive bonuses, predatory lending scandals (e.g. overdrafts), mis-selling practices (PPI), and other illegal activities (e.g. money laundering).
[8] Stephan Shakespeare of Yougov (op.cit.5) who spoke with industry leaders, found that banks were willing to take the hit if this would help them to regain public trust and promised to carry out root-and-branch reform to change the public image of their institutions.
[9] Tim Wallace "Customers won't trust banks for a generation", The Telegraph, 6 March 2016.
[10] See e.g. the British Bankers' Association report "The Benefits of Banking 2016", which details the initiatives and projects beneficial to local communities and the broader economy supported by UK banks.
[11] A. Freiberg, (2010), *The Tools of Regulation,* The Federation Press, p.104, cited in J. McCalman, A. Young and R. Chan (2017) "Regulating the culture of banks in the United Kingdom: strengthening legal accountability or just better leadership?" *J.I.B.L.R., 32(6), pp: 261-268.*

tive relationship with society and to gain legitimacy[12]. CSR, which was popularized by Bowen (1953)[13], demonstrates significant local variations in regard to its goals and activities. In many countries especially in Europe, there is the so-called implicit approach to CSR, where mandatory and customary rules are used to establish specific CSR requirements to corporations[14] thus limiting the voluntary character of CSR and the companies' freedom.

Financial services is one of the most heavily regulated industries in the world and although the goals of financial regulation are, broadly speaking, different from those of the CSR (regulation primarily focuses on regulating the operation of banks and on preserving market stability, whereas CRS focuses primarily on the relationship between banks and society[15]) they still contain elements, which are common with CSR[16]. The use of compulsory norms in the form of regulation has often been promoted to stimulate and guide the voluntary CSR activities of the banks.

Considering the mix of compulsory and voluntary activities pursued by the reforms which were adopted following the financial crisis it is relatively easy to notice that compulsion on many occasions took the lead. A large number of new sets of rules were adopted to regulate and control individual and bank activities within the sector, new supervisory bodies were created to oversee compliance with the new requirements and heavier penalties were imposed on violators. In addition, financial institutions have been encouraged to take their own voluntary initiatives to restore a spirit of individual and institutional social responsibility within their ranks. As a result, new codes of conduct and ethics for banks and bankers have been adopted by individual banks and bank associations and a number of initiatives aimed at involving the broader UK society, such as the more active involvement of outsiders, civil society and existing stakeholders in the decisions of banks and bank-related organisations have been used all for the purpose of enabling cultural change and of making banks and bankers more responsible.[17].

The key question which this paper seeks to address is if the goal of making banks and bankers more responsible can be achieved primarily through compulsory norms or if voluntary schemes developed by individual banks or banker associations and related bodies can be more appropriate to lead.

---

[12] Meyer et al. (2015) "Legitimating the transnational corporation in a stateless world society" in K. Tsutsui & A. Lim (Eds.), *Corporate Social Responsibility in a Globalizing World* (Business and Public Policy, pp. 25-26). Cambridge: Cambridge University Press.

[13] Bowen H. (1953), *Social Responsibilities of the Businessman.*

[14] Matten D. Moon J. (2008) "Implicit" and "Explicit" CSR: a Conceptual Framework for a comparative understanding of Corporate Social Responsibility" *Academy of Management Review*, Vol. 33, No. 2, 404–424.

[15] See also Armour *et al.* (2016) *Principles of Financial Regulation*, Oxford University Press, 51.

[16] See for example below the discussion of the new individual accountability rules adopted by regulators, which aim at making bankers more responsible.

[17] For more details see the references elsewhere in the article to the role of bodies such as the Banking Standards Board, a private independent body, created in 2015 with the involvement of outsiders and civil society, to support cultural change in the industry.

The paper contributes to the ongoing dialogue in the literature and between policymakers on whether the significant expansion of mandatory rules introduced in the UK and internationally in the aftermath of the financial crisis can be effective in making financial institutions more socially responsible and in preventing future crises. An additional, but related, objective is to discuss whether culture, which is one of the key drivers behind bank behaviour, can be changed using compulsory norms or through voluntary schemes. The focus is on UK financial services since the country experienced a strong impact from the financial crisis with major bank failures, which resulted in significant costs for the national economy and a very tense relationship between the country's banks and the UK society. The paper emphasizes the need for more explicit, voluntary participation of banks in the efforts to create a more resilient and reliable financial system, which will regain the trust and confidence of UK society.

The paper is structured as follows: the first section considers the definition and standards of corporate social responsibility (CSR) in the literature and in some key legal instruments; the second section focuses on a discussion of the standards of social responsibility expected of UK banks and of the level of compliance of the UK financial sector with its social obligations; the third section looks for reasons for the failure of UK banks to meet social expectations; the fourth section discusses what has been done to address the breakdown in the relationship between banks and UK society; the fifth section debates the utility and limits of laws and regulations; the sixth section looks to the issue whether reconciliation between banks and society can be achieved through voluntary means or through regulation; the seventh section discusses the implications of CSR and success stories; the eighth section discusses the way forward and the ninth section summarizes the key issues arising from the paper.

1. **The definition and standard of corporate social responsibility in theory and the law.**

a. Definition of CSR

Broadly speaking, CSR suggests that corporations should recognize their responsibilities to a larger set of actors beyond the corporation's shareholders and that they should act to advance the welfare of all these actors (Prakash 2015[18]). Generally acceptable elements of CSR include economic, legal, ethical and discretionary activities (Carroll 1991). Matten and Moon (2008)[19] characterize CSR as "nationally contingent, essentially contested, and dynamic" term. This is explained partly

---

[18] Prakash A. (2015) "Corporate Social Responsibility as Social Regulation" in K. Tsutsui, A. Arbor,.A. Lim (Ed.), *Corporate Social Responsibility in a Globalizing World,* Cambridge University Press, 430-454.
[19]Op.cit.14.

on grounds of CSR being a contested and internally complex term with open-ended rules of application (Moon, Crane, & Matten, 2005[20]), a term which is an umbrella one covering a number of other terms with often synonymous and overlapping meanings (Matten & Crane, 2005[21]). The concept of CRS is constantly evolving in a dynamic way (Carroll 1999[22]) in response to the evolving nature of the relationship between corporations and the societies in which these corporations operate[23]. Thus, from an initial emphasis on environmental issues, the concept gradually incorporated in its content economic and social issues with emphasis on human rights (Rosamund 2015[24]).

Although multinational corporations (MNCs) have helped to spread CSR around the world to gain global legitimacy and to fill the governance gap currently existing at an international level (Meyer et al. 2015[25]), this does not mean that CSR has an exclusively global focus. Kinderman (2015[26]) suggests that national-level CSR is particularly important and is used by corporations to minimize public backlash to deregulation or to gain legitimacy. This seems to be the case particularly for the financial sector, which despite significant expansion beyond national borders during the past decades has maintained its strong national character and focus.

At policy level, in the European Union, the above reality of CSR is reflected in official policy documents and in legislation. The European Commission has defined CSR as "a concept whereby companies integrate social and environmental concerns in their business operations and in their interaction with their stakeholders on a voluntary basis"[27]. The term covers voluntary, business-led actions by companies "over and above their legal obligations towards society and the environment"[28]. In 2011 the United Nations Human Rights Council (UNHRC) adopted the United Nations Guiding Principles on Business and Human Rights (UNGPs[29]), which further expanded the scope of CSR to the area of human rights. The UNGPs will gradually become part of national law and policy around the world.

[20] Moon, J., Crane, A., & Matten, D. (2005) "Can corporations be citizens? Corporate citizenship as a metaphor for business participation in society", *Business Ethics Quarterly*, 15: 427–451.
[21] Matten, D., & Crane, A. (2005) "Corporate citizenship: Toward an extended theoretical conceptualization", *Academy of Management Review***,** 30: 166–179.
[22] Carroll, A. B. 1999. Corporate social responsibility— Evolution of a definitional construct. *Business and Society*, 38: 268–295.
[23] UK Department for Business Innovation and Skills, (2014) "Good for Business & Society: Government Response to call for Views on Corporate Responsibility", April.
[24] Rosamund T. M. (2015), *Business Ethics and Corporate Social Responsibility*, Ethics International Press, p.53.
[25] Meyer et al. (2015) "Legitimating the transnational corporation in a stateless world society" in K. Tsutsui & A. Lim (Eds.), *Corporate Social Responsibility in a Globalizing World* (Business and Public Policy, pp. 25-26). Cambridge: Cambridge University Press.
[26] D. Kinderman (2015) "Explaining the rise of national corporate social responsibility: The role of global frameworks, world culture, and corporate interests" in K. Tsutsui & A. Lim (Eds.), *Corporate Social Responsibility in a Globalizing World* (Business and Public Policy, pp. 73-106).
[27]Commission of the European Communities (2001), Promoting a European framework for Corporate Social Responsibility, Green Paper, Brussels, 18.7.2001, COM (2001) 366.
[28] Communication from the Commission to the European Parliament, the Council, the European Economic and Social Committee and the Committee of Regions, Brussels, 25.10.2011, COM (2011) 681.
[29] HR/PUB/11/04.

It is notable that although CSR is voluntary, the use of compulsory norms, in the form of the adoption of laws and regulations is often seen as necessary in order to create an environment "more conducive to enterprises voluntarily meeting their social responsibility" as the European Commission[30] has put it. As a result, provisions with CSR elements appear in various types of legislation, which have a compulsory nature (e.g. financial regulations[31]).

Further, law is usually split into hard and soft law. Hard law contains specific, legally building requirements, whose violation is often associated with sanctions to violators. Soft law is not legally binding, but can exert significant influence by guiding public expectations. Declarations, guidelines and related documents are used as part of soft law. Both types of law seek to limit individual freedom with hard law seeking to achieve it in a more explicit way: compliance with hard law, unlike soft law, is not discretionary. Regulation employs both hard and soft law instruments.

The laws related to CSR usually introduce broadly phrased guidance for companies to engage in "socially responsible" activities and to report on these activities but they leave to the companies to determine how they are going to engage society and how to report their activities. By way of example, Principle 14 of UNGPs reads: *"The responsibility of business enterprises to respect human rights applies to all enterprises regardless of their size, sector, operational context, ownership and structure. Nevertheless, the scale and complexity of the means through which enterprises meet that responsibility may vary according to these factors and with the severity of the enterprise's adverse human rights impacts".*

In other occasions, when society wants to send a clear message, hard law is used for setting out specific requirements. For example, EU Directive 2014/95 requires from large companies to disclose non-financial and diversity information. Additional sets of guidelines and advice are produced by various organizations public or private such as example the guidelines issued by GRI[32], an international independent organization helping companies to comply with their sustainability obligations or the Banking Standards Board (BSB), an independent, non-statutory, voluntary membership body, which was established in UK in 2015 "with the aim of helping to raise standards of behaviour and competence across the UK banking sector"[33]. These guidelines are soft (non-binding) law documents, which though are widely used by the companies to design their CSR policies and to report on them.

---

[30] Op.cit.31.
[31] See e.g. the Conduct Rules, introduced by FCA and PRA in 2016 in UK to impose individual rules of conduct to employees of UK banks.
[32] GRI has set out Global Standards for Sustainability Reporting which can be used by companies (https://www.globalreporting.org/Pages/default.aspx).
[33] https://www.bankingstandardsboard.org.uk/ BSB carries out annual assessment of UK banks standards of behavior.

The extent to which rules and norms are used to define and drive CSR activities often gives rise to a distinction between "explicit" and "implicit" CSR. "Explicit" CSR leaves responsibility for CSR decisions and policies to individual companies using voluntary activities, whereas "implicit" CSR refers to a more collective approach usually driven by rules and norms (Matten and Moon 2008[34]), with which companies must comply.

The combined effect of the nexus of laws and regulations linked to CSR is that companies enjoy certain freedom when designing their CSR activities, but this freedom is guided by rules setting out contexts and goals, which have to be met. Companies have no freedom to completely ignore their social responsibilities.

b. Standards of CSR

An obvious question which emerges from the precedent analysis is about the acceptable standard of CSR. Existing laws in UK and internationally do not provide clear answer to this important question. Social responsibility can be manifested in myriads ways and at different levels and though local laws often set specific goals for various areas of bank activity they do not always set measurable standards, which could be used to assess if banks achieved these goals. Public perceptions of corporate social responsibility also demonstrate significant local variations. Due to these limitations it is sometimes prudent to seek to extract CSR goals and standards by looking to the identified problems which law and society expects from banks to address.

By way of example, PCBS report[35] recorded serious complaints from small and medium UK business about access to loans in the early years following the financial crisis. UK public expected banks to reciprocate for the bailouts by increasing support for the UK economy. Yougov (2013) survey[36] confirmed this public perception and added that UK public wanted banks to stop greed, stop being a public risk, stop putting profits before people and improve compliance with government regulations. PCBS report recorded public demands for UK banks to offer better service to consumers, for example by avoiding mis-selling practices.

BSB, which carries out annual assessments of UK bank standards of behaviour and culture, has identified nine characteristics against which banks are assessed: honesty, respect, openness, accountability, competence, reliability, responsiveness, personal and organisational resilience, and shared purpose[37] . Although BSB provides definitions and guidance to its members on each each of

[34] Op.cit.14.
[35] Op.cit.3
[36] Op.cit.5
[37] Available at https://www.bankingstandardsboard.org.uk/assessment-results-2017/

these characteristics, the definitions are broad and the standards can be assessed though qualitative evidence.

At law level, UK adopted a variety of laws since the financial crisis, which one way or another seek to control and improve conduct of banks and bankers. For example, in 2016 UK enacted[38] a new senior Managers and Certification Regime, which is aimed at increasing individual responsibility and accountability of senior managers. It requires banks to seek regulators' approval when appointing senior managers. The process requires a clear statement of responsibilities for the appointed person. The certification regime requires banks to check and certify that employees in important positions (other than senior managers) are fit and proper for these positions. While increasing individual responsibility and accountability is part of the efforts to make UK banks more socially responsible, it is not clear how banks can meet the standard of responsibility: gaining authorities' approval for senior management appointments does not guarantee socially responsible behaviour by the appointed senior bankers.

At EU level, several initiatives exist to improve the CSR records of companies operating in EU, such as disseminating good practices, enhancing market rewards for CSR, incorporating CSR into education, training and research and others[39]. A significant Commission initiative is to promote implementation of the UN Guiding Principles for Business and Human Rights[40]. Again, measuring success in implementation, despite the Commission's efforts, remains a challenge.

Similar uncertainty may be expected for the Global Code of Good Practice for Foreign Exchange Markets issues in 2017 by the Bank of International Settlements (BIS)[41]. The Code requires market participants to "…strive for the highest ethical standards", citing that they should act honestly, fairly and with integrity.

The above indicative examples show that the best way to evaluate the social behaviour of banks is through a case-by-case consideration using definitions and objectives relevant to each case.

2. Compliance with the standards of CSR in the UK financial sector

---

[38] The new regime was introduced by the Financial Services (Banking Reform) Act 2013, which amended the Financial Services and Markets Act 2000. It is also discussed elsewhere in the article.

[39] More information on EU's policies can be found on the Commission's CSR website: https://ec.europa.eu/growth/industry/corporate-social-responsibility_en

[40] In 2015 the Commission published a Staff Working Document on "Implementing the UN Guiding Principles on Business and Human Rights - State of Play" SWD(2015) 144.

[41] Bank of International Settlements (2017) "Global Code of Good Practice for Foreign Exchange Markets", available at https://www.globalfxc.org/docs/fx_global.pdf

From the previous section it emerged that CSR has four main features: an umbrella term, voluntary, constantly evolving, with local significance. It also emerged that there are no clear standards or methods of measuring CSR performance except in specific, narrowly defined, cases. A potential solution is therefore, to record CSR progress of UK banks in various areas and identify current issues.

Herzig and Moon (2012[42]) claim that prior to the financial crisis, the sector had made significant progress in incorporating CSR into their operations citing as an example, between others, the broader acceptance that banks are often well-regarded because of their involvement in philanthropy and charities, the equal treatment of their employees, diversity and job creation. Banks also played a prominent role in significant CSR activities and organizations in the UK and in community projects. A British Bankers Association Report[43] claimed that in 2015 British Banks opened £9 million basic bank accounts to most vulnerable people, that they now offer a bank account to 99% of UK adults over the age of 15 and that they lent £58 billion of new loans to small businesses. Such claims are particularly aimed at addressing expressed concerns that the UK banking system leaves outside of its services the most vulnerable people and without enough access to finance many small and medium enterprises[44]. In addition, the institution of mutualized Building societies, which have a long history in the UK offers support to community and individual development projects whereas in regard to CSR itself it seems that there is evidence that the concept has become institutionalized in the UK at least since the recession of the 1980s[45].

UK society, though, is still not convinced. For the level of public discontent Herzig and Moon (2012) offered the straightforward explanation that the last financial crisis had such grave consequences that rendered all bank efforts in the CSR field less significant. They claim that the crisis revealed that CSR had not been incorporated into core bank businesses, those which led to the bank failures. Andrews (2016)[46] offers a different explanation slightly more comforting for the banks: the benefits from the operation of banks to society are difficult to see because: "… one cannot easily envisage the so-called counterfactual: what our society would be like without modern finance". Society doesn't seem to be looking to the right place. McDermott of FCA, (2015[47]) focuses on the disconnection existing between financial institutions and society blaming the former for it:

[42] Herzig C. and Moon J. (2012) "Corporate Social Responsibility, the Financial Sector and Economic Recession", International Centre for Corporate Social Responsibility, Nottingham University Business School.
[43]British Bankers' Association, "The Benefits of Banking 2016", Report.
[44] See also the findings of PCBS report, op.cit.3.
[45] A. Mullineux, (2011) "The public duties and social responsibilities of big British banks" *International Advances in Economic Research, 17*(4), 436-450.
[46] P. Andrews (2016), "Culture in UK banking – regulatory priorities" Speech to Westminster Business Forum, available at https://www.fca.org.uk/insight/speech-culture-uk-banking-regulatory-priorities
[47] McDermott, T. (2015) "Personal Accountability", Speech delivered at the City & Financial conference on Personal Accountability in the Financial Services Industry, 2 December 2015, London.

"*...[F]inance too often became disconnected from the world in which it operated and the people it was supposed to serve...The culture had become one of short termism. In some cases this was compounded by greed and a sense of impunity. And in many different ways, that led to the issues that have occurred, and which seemed to keep on occurring*."

The above views seem to be bringing to light another problem: that banks and society do not seem to fully agree on the standards and priorities of social responsibility for the financial sector. Society seems to have broader demands, which have not been met.

The Yougov-Cambridge survey (2013[48]) considering the issue found that the UK public wants: a) Utility: banks are not perceived as working hard enough to support economic growth for the UK or their customers and are actually holding the economy back; b) Safety: banks are considered unsafe, a public risk, and not in compliance with government regulations; c) fairness: bankers continue to be seen as greedy and untrustworthy, putting profit before people. These demands show that funding more community projects or improving access to finance for poor and disadvantaged or small and medium enterprises, do not go far enough to satisfy the demands of society. Traditional CSR activities, even if reinforced, are not enough.

The PCBS Report (2013[49]) revealed that public demands are based on the knowledge that the taxpayer paid a lot of money to save the banks during the financial crisis, so the public expects the banks to reciprocate something which they do not feel they can see happening.

3.Why do banks fail to meet the standards of social responsibility?

The previous section provided already a potential answer: society and banks have diverging views on standards and priorities of CSR and therefore UK banks fail to meet public expectations. But there are other potential explanations.

Boatright (2014[50]), analysing the problem of chronic misconduct in the sector, notes that "…ethical misconduct is not always a matter of bad people doing bad things but often of good people who stumble unwittingly into wrongdoing". He claims that most people working in finance are decent, dedicated, people who fall victims of the sector's focus on profits. He also claims that scan-

[48] Op.cit.5.
[49] Ibid.
[50] Boatright, J.R. *Ethics in Finance*, Wiley, 2013; also, PCBS report op.cit.3, p.82.

dals do not require deliberate misconduct. Staere (2018[51]), citing Milgram et al. (Levilee 2011[52]) suggests that good people can do bad things if they belong to a group or community which has "a coercive culture that enforces compliance and conformity". If a culture of fear exist in an organization then even good people could react badly. Staere cites as examples, the mis-selling (PPI) and market manipulation (LIBOR) scandals, which happened in an area with strong rules-based regulation. According to Staere, the scandals "have been perpetrated by people working within cultures driven by a coercive focus on short-term profit maximization, demanded by analysts, investors, boards and senior management" (citing also Wheatley, 2014[53]).

Yougov-Cambridge UK survey (2013[54]) found that 67% of the UK public trust "staff at my local bank" to tell the truth. This is as high as the proportion of the public which trusts judges. So, the public seems to be sharing Boatright's the view that most individuals working in banks are good and trustworthy. However, in the same survey only 13% trust investment bankers indicating the problem posed by investment banking, which was one of the key causes of the financial crisis. It seems that the public points the finger at investment bankers as "bad guys" in the sector.

Mullineux (2011[55]; 1987) reinforces the argument about the focus on profits as a leading cause arguing that the social compact between the sector and the government broke down in the 1980s when the big UK banks shifted their focus on maximizing the value for their shareholders. This may imply that deregulation of the 1980s and 1990s, which gave UK banks more freedom from government controls and allowed them to increase risk-taking and seek profit maximization, which generated the crisis a few decades later.

The above views bring to light the role of ethics and culture both individual and institutional. According to Bailey of PRA (2016[56]), "culture has thus laid the ground for bad outcomes, for instance where management are so convinced of their rightness, that they hurtle for the cliff without questioning the direction of travel". Andrews of FCA (2016[57]) refers to a culture of tolerance of non-compliance prevailing in the banking sector, by pointing out that there is a long history of apparently clear principles of financial conduct regulation (e.g. 'treating customers fairly') and of firms signing up for these principles but showing limited evidence of compliance: "the level of tolerance

---

[51] R. Steare "Character, culture and conduct: why good people do bad things in a fear-driven culture" in Financial Conduct Authority "Transforming Culture in Financial Services", Discussion Paper 18/2, March 2018, available at https://www.fca.org.uk/publication/discussion/dp18-02.pdf

[52] N.P. Levilee, (2011), "The role of obedience in society", *Inquiries Journal*, 3(5), 1-1.

[53] M.Wheatley, former Chief Executive of the FCA (2014) "Historic link between ethics and economic success", Speech to the Worshipful Company of International Bankers, London 4 March 2014.

[54] Op.cit.5.

[55] Mullineux, A. (2011) op.cit.35; Mullineux, A. W. (1987), *UK Banking after Deregulation*. Beckenham: Croom Helm.

[56] A. Bailey, "Culture in financial services—a regulator's perspective", Speech at the at the City Week 2016 Conference (London: 9 May 2016),

[57] Op.ct.43.

of non-compliance in financial services regulation…is very striking"[58]. MacDermott of FCA (2014[59]) reinforces this view by reporting the response FCA enforcing teams often receive when visiting the banks: "We are still told that misconduct is the work of a few errant individuals within large organizations".

However, and despite the frequent references to culture as a source of the problem, it remains notoriously difficult to define and measure culture. A 2018 paper of FCA[60], citing the views of various stakeholders, claims that now there is a broad consensus in the industry that culture is about behaviour,'the way things are done around here' and includes "the norms, values and practices which are revealed by how people think and behave, as well as our behaviour when no-one is looking"[61].

The above definition to be a workable one though, requires identification and measurement of the components of culture. This would help to understand how and why culture has led to bank failure. Banker remuneration (the "bonus culture") and ineffective governance, are often cited[62] as key drivers of a failing culture in banking. PCBS report found greed and corruption as two other elements of a failing culture, whilst FCA above referred to widespread tolerance of non-compliance in the sector.

Bailey of FCA (2017[63]) touches upon the problem that culture does not have a single or unified form. He claims that culture is not the same for each company neither should it be. Each organization has its own, unique culture shaped by inputs unique for each organization. Banking Standards Board annual review for 2016/17 reinforces this by highlighting that understanding and managing culture is a core responsibility of the bank's board which "…cannot be delegated to regulators, policy makers or a specific function within the firm, such as compliance, risk or human resources"[64]. BSB also emphasizes "the significance of size and inter-connectedness of the UK banking sector".

This leads us to the conclusion that whilst referring to an overall bad culture in the sector offers a good start, identifying the individual level of bank cultural failure is a much more complex task. Some banks are serial violators of norms when others are not and when looking for the cause of bank failures you will have to dig deep into each bank separately rather than take a sector approach.

The problem of culture does not seem to concern only the financial institutions but also those, who were tasked with ensuring that these institutions complied with the requirements of the society.

[58] Ibid.
[59] T. McDerrmott (2014) "Learning the lessons of the past as an industry", Speech delivered at the FCA's Enforcement Conference, London.
[60] Financial Conduct Authority, op.cit.48.
[61] Ibid.
[62] e.g. A. Bailey (2017) "Culture in financial institutions: it's everywhere and nowhere". Speech at the HKMA Annual Conference for Independent Non-Executive Directors, 16 March.
[63] ibid.
[64] Banking Standards Board, "BSB Annual Review 2016/2017", p.7 available at https://www.bankingstandardsboard.org.uk/pdf/banking-standards-annual-review-2016-2017.pdf

Regulation in the past demonstrated on many occasions spectacular failures to identify the problems and prevent them from happening in the financial sector. The PCBS report[65] cited Wheatley of FCA stating that the regulatory failure "[...] was a failure of philosophy" indicating the in addition to banks, regulators also face their own problem of culture. Lord Turner, who in 2009 led the review of the causes of the financial crisis, argued that long periods between banking crises tend to breed complacency[66]. Regulation faces additional challenges from information gaps, lack of resources, fragmentation, regulatory arbitrage and the failure to catch up with market speed[67]. In addition, markets move in real time, something which regulators cannot often do. As a result, regulators, whose role is between others to protect the public and society from harmful bank activities and to help banks meet their social obligations, went through their own soul searching after the financial crisis.

4. What has been done to address the problem

A consensus emerged, as a result of the crisis in the UK and internationally, that banks cannot be trusted to behave responsibly on their own. Many felt that the freedom the banks enjoyed during the three decades prior to the financial crisis, when the wave of deregulation and bank privatizations reduced public scrutiny and control of the financial sector, was not used by financial institutions to advance the public good. Banks' freedom had to be restricted and, in many areas, voluntary compliance had to be replaced by mandatory rules through the introduction of relevant legislation.

As a result, massive reforms were introduced in the UK and internationally, aimed at expanding the scope of public scrutiny to new areas. These reforms resulted in the UK in 13,000 pages (and growing) of rules, guidance and supervisory statements published by the Financial Conduct Authority (FCA) and Prudential Regulation Authority (PRA), two of the new regulators[68]. The administrative costs of the new regulators have been claimed to be over £1.2 billion a year – six times what they were in 2000[69]. Thousands more pages of rules were produced by other UK and International regulators all aimed at making the financial system more stable and accountable and on tackling the cultural problem. What differentiates the latest efforts on regulation from previous ones is that they place emphasis on holding accountable not only the financial institutions but also key individuals (middle and senior managers) within them. The focus on the role of individuals is central in the ef-

[65]p.142.
[66]Ibid.
[67] Armour e*t al.* op.cit.17.
[68] New City Agenda (2016) "Cultural Change in the FCA, PRA and Bank of England: Practising What They Preach?".
[69]Ibid.

forts to tackle the problem of culture. There is also for the first time strong emphasis on more proactive regulation by identifying and tackling sector risks before they become systemic problems.

5. The utility and limits of laws and regulations

When assessing the utility of laws and regulations one should consider two aspects: first, the rules themselves which are introduced to regulate a specific issue and, second, the effectiveness of the enforcement mechanism with public supervision having a prominent role. Simply speaking, rules can be effective not only when they are well targeted but also when there is in place an effective mechanism of supervision and enforcement, which ensures the implementation of the rules and the effective detection and punishment of any violators. This is where things start to get complicated.

First, compulsory rules as those introduced by law and regulations, by establishing an ever-expanding web of legal obligations tend to pass the duty of enforcing social responsibility to regulators, who must ensure that these responsibilities are met. Those, on whom the obligations are imposed, in this case the financial institutions, tend to take a back seat and let the regulators lead the way. Steare, cited by Wheatley 2014[70], submits that "…[A]t their worst, laws, regulations […] remove our responsibility for deciding what's right". Is this the best way though to enforce change of culture?

Rosamund (2015) considering the advantages and disadvantages of using binding norms highlights that the norms offer clarity about what must be done, clarity about the sanctions to be suffered by the violators and an impartial tribunal which will decide on the sanctions and any dispute arising from the application of the norms. However, the risk of compliance becoming a ticking-box exercise, lacking much substance is real. Along similar lines, Filabi (2018)[71] adds that there is a danger that people will focus narrowly on rules and underweight ethical considerations. She submits that regulation is largely dependent upon a hypothesis of rational behaviour on behalf of those who are subject to regulation. The threat of punishment would drive rational behaviour leading to compliance. However, as she notes, individuals do not always act rationally as there are other factors influencing behaviour such as individual or organizational principles and goals. The latter could motivate individuals to ignore compliance with regulation.

Adding credibility to the above argument, experience on the effectiveness of sanctions mechanisms shows that even heavy penalties are not always capable of deterring widespread violations of

---

[70] R. Steare. *Ethnicability, 2009;* M. Wheatley, Chief Executive of the FCA (2014) "Historic link between ethics and economic success", Speech to the Worshipful Company of International Bankers, London 4 March 2014.
[71] See A. Filabi "Carrot or Stick? Culture as a Regulatory Approach", in FCA op.cit.55, p.12.

the norms (Ischenko et al 2016[72]). This has been attributed to entrenched perception within banks that breaches of the rules will not be detected or punished. But even in those cases where detection was improved, and punishment became tougher through higher fines, the effect on deterrence on many occasions was not promising. Ischenko et al 2016, cite the case of Barclays, which in recent years has been subject to several fines for various violations of the rules as an example of a situation where tougher regulation has failed to produce the desired deterrence. In 2017 the FCA, imposed on Deutsche Bank a £163 million fine, the "largest financial penalty for anti-money laundering controls failings ever imposed by the FCA, or its predecessor"[73]. The same bank between 2016 and 2018 was involved in a number of high profile violations of the rules in the UK and US which resulted in significant fines and settlements including a $425 million fine by US regulators for anti-money laundering violations, a massive £7.2 billion settlement with US regulators for mortgage-backed securities, a $205 million settlement for manipulating forex and a $70 million settlement for rigging a benchmark for interest-rate derivatives and other financial instruments. Bloomberg estimated that since 2008 Deutsche Bank paid more than $17 billion in fines[74]. Many of the Deutsche Bank cases involved also other major banks including Barclays which had, equally, to pay significant fines for violations of legislation. More recently Goldman Sachs senior managers had involvement in a major of scandal known as "1MDB", which concerned mismanagement of Malaysian sovereign investment fund.

Putting these cases in a broader perspective it is easy to see that many of the serious violations concerned actions occurred after the financial crisis and in the presence of a web of "comprehensive" regulations and supervisors. Whilst someone could treat these cases as evidence of the success of the new regulatory regime, someone else would equally willingly see the failure of the new approach to bring about the desired cultural change in the financial sector.

Voluntary schemes, the alternative to regulation, have the advantage that they are driven by the banks themselves which are, thus, encouraged to demonstrate their "best practices", not only to show their commitments to society, but also as a way to enhance the reputation of their company. Showing themselves to be socially responsible has become part of the competitive game for companies, including the banks, but as Rosamund (2015) notes, the risk here is that company directors focus more on the form rather than on the substance of their CSR claims, an outcome pretty much

[72] Z. Iscenko, C.Pickard, L. Smart and Z. Vasas (2016) "Behaviour and Compliance in Organizations", Financial Conduct Authority Occasional Paper No.24, December, available at https://www.fca.org.uk/publication/occasional-papers/op16-24.pdf [Last accessed 17 April 2018]

[73] See Financial Conduct Authority "Annual Report" for 2016/17 p.9.

[74] citied by financemanates.com in "Deutsche Bank Fined $205 Million by NY Regulator over Forex Violations", 20 June 2018, available at https://www.financemagnates.com/institutional-forex/regulation/deutsche-bank-fined-205-million-ny-regulator-forex-violations/ [last accessed June 30, 2018]

similar to the case of binding legislation. Would banks, such as Barclays and Deutsche Bank, which are willing to break the rules and pay the huge fines, be more effectively deterred by voluntary action for reputational enhancement which does not carry any fine with it? Many would raise serious doubts about it.

However, even if one assumes that compulsory norms in the form of legislation offer a better solution they should not ignore the legal barriers, often formidable placed on law enforcers by the legislation itself. A good example is the introduction in The Financial Services (Banking Reform) Act 2013 of a new criminal offence targeting senior managers of financial institutions.

The offence imposes criminal sanctions on senior managers who, while aware of the risks, take decisions which cause failure of the financial institution. To meet the requirements of the Act the conduct must fall “far below”[75] what would be reasonably expected of them. The offence covers also cases where senior managers fail to act[76].

The initial proposal for the introduction of criminal sanctions was made by the Treasury in 2012[77]. The justification was that the existing legal framework at the time did not cover matters such as negligence, incompetence or recklessness or other forms of purely managerial misconduct. The issue was particularly important because earlier investigation into the causes of the financial crisis had showed that one of the reasons that no senior bank manager was jailed for the crisis was the absence of any legal provision providing for such a punishment[78]. The new criminal offence was aimed at filling this vacuum.

Some early problems created by the proposal appeared already in the Treasury document, which proposed it: the new offence would be hard to prove, the persons to be prosecuted would be hard to identify and the criminal investigation would be time-consuming and very expensive. The public consultation, which followed[79] revealed additional problems: most of the respondents opposed the proposal citing as reasons that it would deter people from becoming Bank Directors and that it would add little to the existing legal framework.

Despite opposition, the UK government went ahead and included the new criminal offence in the Financial Services (Banking Reform) Act 2013. The offence was finally enacted in March 2016 but

[75] s36(1)(c)
[76] Ibid.
[77] HM Treasury (2012) “Sanctions for the directors of failed banks” p.7; findings of PCBS report op.cit.3
[78] Ibid.
[79] See “Summary of consultation responses to sanctions for the directors of failed banks” published by the UK government in 2012.

the question to be answered in the coming years is if this offence is a meaningful one especially as proving a causal link between a senior manager's conduct and the bank failure and that the senior manager was aware of the risk and that the manager's conduct fell "far below" the required standard may be a particularly onerous task for prosecutors[80].

In March 2016 the UK government enacted also the new Senior Managers Regime, the Certification Regime and the Conduct Rules[81] and in May 2016 the "duty to responsibility" requirement. The package of new rules seeks to establish clear identification (through mapping) of senior management responsibilities within financial institutions, clear statement of the responsibilities of each senior manager, and clearer Codes of Conduct. The duty of responsibility includes action which regulators may take if a senior manager fails to take steps to prevent the violation of prescribed rules.

These rules may be offering more reassurance to the public, but will they help resolve the cultural problem in the sector or will they be viewed as another tick-box exercise where affected individuals will seek only nominal compliance? The problem with nominal compliance is that it does not touch the culture. Individuals do what they can to comply in order to avoid the sanctions but nothing more.

6. Discussion: can we create more socially responsible banks by regulating their behaviour and culture?

Those pointing to the need to use laws and regulations with binding force to create an environment that will encourage banks to voluntarily become more socially responsible have a strong argument, but there is a need for a serious debate about the size and extent of reach of the binding norms especially as the opposition to the waves of new laws and regulations by proponents of deregulation have become increasingly vocal more recently especially in the US. In the latter, the Trump administration and Republicans raised strong opposition to the "overregulation" of US banks and in 2018 the US Congress passed a law watering down a significant part of the Dodd-Frank Act, which was the key law passed by the Obama administration in the aftermath of the financial crisis to strengthen the regulation of banks. One of the key arguments against Dodd-Frank was that its restrictions were hurting significantly the small and medium level banks, which had significant activity in local

[80] On the issue see also Cranston et. al (2018) *Principles of Banking Law, (3rd Ed.)* Oxford University Press, p.105.
[81] The rules about the new regime were introduced through the Financial Services (Banking Reform) Act 2013. For an explanation of these policies see FCA's guidance at https://www.fca.org.uk/firms/senior-managers-certification-regime

communities[82]. Another key argument was that the strict rules of Dodd-Frank protected the big banks, which had the necessary resources to meet the strict requirements of legislation, from competition by smaller banks, which were facing market obstacles raised by the same legislation[83].

In the UK there has been considerable debate about the reasons behind the slow economic and productivity growth in the country in the decade following the financial crisis. Underperformance of the financial services sector is often cited as a reason. Particular focus is on very weak productivity gains in the economy, which helps to explain the slow growth in wages and salaries during the decade following the crisis. Tenreyro (2018)[84], external member of the MPC, Bank of England referred to a major contribution of financial services to the slow productivity growth. Although financial services themselves occupy a relatively small part of the UK economy they have a comparably higher spillover effect on the economy for example by keeping the provision of credit to the economy tight undermining investments and economic growth[85]. Tanreyro indirectly accepted that role of regulation, which, *inter alia*, forces banks to keep more capital and reduce risky activities, for the poor financial sector performance but defended those measures as necessary to avoid future financial crises. Tenreyoro's admittance and views from other economists and the banks themselves who have attributed the poor performance to over-regulation causing weaker lending, less investment and lower productivity[86] indicate that the extensive use of regulation can have significant social costs in addition to significant economic costs associated with each operation.

The past record of regulation as well as the signs sent more recently by Barclays, Deutsche Bank and other high-profile violation cases, which are reminiscent of pre-crisis recklessness, do not offer adequate guarantees that society can feel protected from financial crises. Someone could even argue also that the possibility of bringing about the desired cultural change is already remote and unlikely to happen.

Policymakers and regulators openly admit the obvious that they cannot prevent all misconduct. Mark Steward (2017[87]), the Director of Enforcement and Market Oversight at the FCA accepted that "…[o]ne of the challenges of conduct regulation is to recognize squarely that not all miscon-

[82] See e.g. New York Times (2018) "*Congress Approves First Big Dodd-Frank Rollback",* May 22, available at https://www.nytimes.com/2018/05/22/business/congress-passes-dodd-frank-rollback-for-smaller-banks.html
[83] Ibid.
[84] S. Tenreyro, "The fall in productivity growth: causes and implications", Speech at Peston Lecture Theatre, Queen Mary University of London, 5 January 2018.
[85] Ibid.
[86] See e.g. C. Papadopoulos "Financial services productivity held back by over-regulation", City A.M. 18 February 2016, available at http://www.cityam.com/234963/financial-services-productivity-held-back-by-over-regulation
[87] Stewart M (2017) "The expanding scope of individual accountability for corporate misconduct", speech delivered at the New York University Program on Corporate Compliance and Enforcement on March 31.

duct can be prevented". McDermott of the FCA (2014[88]) claimed that *"[i]t is not the job of the regulator alone to weed out and punish wrongdoers. Firms need to think about where risks might arise and how to control them: the need to understand the culture of the subsets of their organization, how they differ and what that means*".

This approach raises the critical question whether the current balance between compulsory norms and voluntary activities is appropriate or whether there is overregulation as many claim. Carney, the head of the Bank of England and of the Financial Stability Board (FSB), the G-20 Regulatory body[89], has defended the achievements of the efforts of public authorities in the UK and internationally claiming that the financial system is safer, simpler and fairer. But is it more socially responsible? In literature, McCalman et al (2017[90]) citing the results of empirical research by Simpson (2002[91]) claim that the proliferation of laws failed to deter corporate misconduct. They claim that culture is a social phenomenon, a non-tangible concept, and as such it may be difficult to draft a set of rules to regulate it. A similar view was expressed by the Group of Thirty, an expert group which in 2015 published a report on Banking Conduct and Culture[92]. A FSB 2018 report on financial misconduct[93] cited estimates that bank paid globally 320 billion of US dollars in fines since the financial crisis. Carney admits that these fines are insufficient and inefficient to reduce misconduct claiming that if the resources spent on fines were retained by banks they could result in 5 trillion US dollars in lending to households and businesses.

Supporters of civil society often dismiss the role of regulators as being too close to the industry[94]. They also claim that regulators do not represent the interests of those parts of society affected by the financial crisis[95]. According to them, civil society can play a more effective role. BSB[96] is an example of an effort to incorporate civil society into the process of setting the banking standards. It is an industry-driven initiative which brings together industry experts but also outsiders including civil society. However, one of the problems with the appointment of non-experts is their lack of

---

[88] T. McDerrmott (2014) "Learning the lessons of the past as an industry", Speech delivered at the FCA's Enforcement Conference, London.
[89] Carney M. (2017) "The high road to a responsible, open financial system", Speech, Thomson Reuters, Canary Wharf, 7 April.
[90] J. McCalman, A. Young and R. Chan (2017) "Regulating the culture of banks in the United Kingdom: strengthening legal accountability or just better leadership?" *J.I.B.L.R., 32(6), pp: 261-268.*
[91]Simpson S.,(2002) *Corporate Crime, Law and Social Control,* Cambridge: Cambridge University Press, pp.45–60.
[92] Group of Thirty (2015), "Banking Conduct and Culture: A Call for Sustained and Comprehensive Reform", available at http://group30.org/publications/detail/166
[93] Financial Stability Board (2018) "Strengthening Governance Frameworks to Mitigate Misconduct Risk: A Toolkit for Firms and Supervisors", April 20.
[94] McDaniel, Jr., Charles.(2015) *Civil Society and the Reform of Finance*, McDaniel, Taylor and Francis.
[95] Ibid.
[96] http://www.bankingstandardsboard.org.uk/

knowledge of the technical and complex issues facing the financial sector, which could make their contribution less effective.

7. CSR implications and potential success stories

Being socially responsible is important not only for UK banks but also for the broader UK society, which currently faces several challenges from Brexit and globalisation. A wide range of problems from income inequality, poverty and unemployment to climate change and sustainability cannot be addressed without banks behaving in a more responsible way. For example, banks could reduce funding on projects resulting in environmental damage and increase funding an projects creating employment in deprived areas. Consideration of financial returns should not be the primary concern is such cases.

While all UK banks highlight in their annual reports and press releases their positive contributions to the national economy and local communities, reality shows that these contributions do not belong between the top priorities of most UK banks. There is only a small number of banks, which have incorporated social contributions into their core businesses.

A leading such example is the Co-operative Bank, a bank whose business model is customer-led based around principles of the so-called ethical banking, which includes for example investing only in environmentally and ethically acceptable projects. Ethical banking has been around since the 1990s and the business model in its essence gives priority to socially responsible projects over profit-maximising ones[97]. Co-operative Bank follows ethical banking since 1992. Its case can serve as an example of both the contribution and the challenges facing banks with exclusive commitments to socially responsible projects: Co-op faced several significant challenges in recent years, as it struggled to keep pace with competitors with profit-maximising priorities, and even faced collapse and exit from the market. The bank also faced internal misconduct issues, which resulted in FCA banning the bank's former chairman from the financial services industry[98]. There are other smaller UK banks (e.g. Triodos) operating (partly or wholly) on principles of ethical banking without though managing to break ground on the mainstream. UK banking sector like in the rest of the world is dominated by traditional, profit-maximising banks.

8. **The way forward**

[97] For more details see F. Barigozzi and P. Tedeschi (2015) "Credit Markets with Ethical Banks and Motivated Borrowers" *Review of Finance*, 19: pp.1281–1313; E. Paulet et.al (2015) "Banking with Ethics: Strategic Moves and Structural Changes of the Banking Industry in the Aftermath of the Subprime Mortgage Crisis", *J. Bus. Ethics* 131:199–207.
[98] The relevant FCA Order, was published on 1 March, 2018 and is available at https://www.fca.org.uk/publication/final-notices/paul-john-flowers-2018.pdf

Any efforts to effect the cultural change required in order to make UK banks more socially responsible has to accept two hard realities. First, that the task will have to last for a generation. It took decades for bankers to abandon their old more socially responsible culture and to fully embrace, during the period of deregulation, the new, profit-maximising one. Bringing bankers back will take as long and the task will be even more difficult due to the fact that objective reality such as the widespread use of technological innovation, which currently generates new profit opportunities through dubious methods, for example, cryptocurrencies, virtual currencies and new complex financial products, will keep provoking adventurism and pursue of personal wealth for individual bankers and market dominance for banks[99]. The efforts therefore to alter bank culture will have to be consistent and persistent with any positive results expected within decades. Second, the reality of ethical banks, which despite their socially beneficial nature have only marginal presence in the financial sector indicates that it is unrealistic to expect UK banks to fully abandon their profit-maximising priorities.

A more realistic goal would be to convince them that it is in their own interest to have a positive relationship with society. Almost all UK banks seem to accept that already: all in their CSR reports highlight the benefit for their businesses and brands from positive engagement with the local communities and the CSR society. The problem with the current situation is that they do not engage enough. They need to act more on this acceptance.

To do so, this author takes the view that UK banks need to act on two different fronts:

The first front is an *external* one, which concerns their interaction with the communities and the broader society. To achieve a better relationship with society banks need to increase significantly the level of day-to-day engagement with all stakeholders and support more projects beneficial to the community.

The second front is an *internal* one, which concerns the way the banks view their relationship with society and the way the individuals working in the financial sector understand the level of their personal responsibility to ensure that society is protected from harmful activities by the banks.

Acting on the external front will help to repair part of the damage caused to the industry's social profile from the financial crisis and the continuous scandals and will help to maintain in the longer term a more positive view of the sector, while acting on the internal front will help to check the ex-

[99] Cryptocurrencies and virtual currencies are privately created currencies which are not issued by central banks. They have experienced worldwide growth during the past decade especially for payments through the internet. Although their relevant market size is still small, public authorities around the world consider them as an emerging risk to both consumers and to the financial system and have placed them under monitoring. for more details see the FSB 2018 report to G-20 on cryptocurrencies (Financial Stability Board, “Crypto-assets”, Report to the G20 on work by the FSB and standard-setting bodies, 16 July 2018, available at http://www.fsb.org/wp-content/uploads/P160718-1.pdf).

istence of bad elements of culture which contribute to crises, offering opportunities for crisis prevention and for longer term peace between banks and society.

Improving engagement with the community and broader society is easier to achieve because it is visible and tangible. Compulsory norms setting quantitative targets for community engagement or achievement of social objectives (e.g. improve access to finance for poor and disadvantaged through setting of specific numerical targets) can be potentially more effective in achieving the desired outcome of convincing society that banks engage more constructively with it.

Improving the way bankers view their relationship with society on the other hand is more difficult as it requires a top-down cultural change within the industry, which is harder to achieve. For such change compulsory laws and regulations, given their limitations, are less likely to be effective[100]. How can you make a greedy banker who cares only about his personal profit and career development to consider the impact of his actions on the broader society? Can such a person be forced to change using compulsory norms dictating a specific course of action and threatening serious punishment in case of non-compliance? There are serious doubts about this especially if the banker thinks that they can escape punishment or if they do not think that what they do is a bad thing. In addition, and as financial markets evolve there is always the case that current norms do not effectively capture all the new types of potentially harmful banking activity.

The reforms of financial regulation after the financial crisis made, though, a major contribution to effecting internal change by setting in place rules which help direct the spotlight on individual responsibility and accountability within banks. Greedy and irresponsible bankers can no longer hide behind the anonymity offered by the enormous size of modern financial institutions to escape punishment for opportunistic behaviour causing losses to their banks. The absence of clarity about the exact duties and responsibilities, which was used as an excuse by bankers to avoid shouldering the burden of duty they deserved is no more available to them. This should on its own initiate an internal process of cultural change within individuals, which if it reaches a significant number of them could bring about the desired cultural change within the organization as well.

However, the process of using increased regulation to enforce change has side effects which if they are not addressed could offset any potential benefits. The problem of slow economic growth and of the slow rise in salaries and wages in UK, which is causing broader dissatisfaction in society has in part to be blamed on regulation. Proponents may argue that this is a price society will have to pay to be protected by future crises or in order to tackle the culture of greed and corruption in the financial sector, but these arguments become less and less convincing as the economy continues to grow slowly and the banking scandals continue to hit the news on a regular basis. After all, there

[100] This view is also supported between others by the Group of Thirty op.cit. who argue that culture cannot be regulated.

are no adequate guarantees that the UK financial system is currently sealed from crisis by regulation.

9.**Conclusion**

Wheatley (2014) of FCA, argued that the financial sector was "…confronting a world with fewer advocates than it would like: but, also, perhaps fewer advocates than it deserves"[101]. The statement demonstrates the nature of the problem facing the relationship between banks and society in the UK: the UK public does not have great confidence and trust in its banks and has potentially a more negative view of this sector than the facts would justify. CSR where all UK banks have long presence and has a strong voluntary nature, should be reinforced and used to help improve the public image of the banks especially on the issue of culture, but the enactment of a vast number of new compulsory rules in the latest reforms to financial regulation may be hindering these efforts by limiting bank freedom too much. In such an environment, any positive change in the banks may be interpreted by the public as a result of the compulsion of law rather than of bank voluntary actions. A better balance between compulsory rules and voluntary schemes is needed.

According to Boatright (2014, p.2) there are three critical ethics finance questions: a) what are our ethical obligations or duties? b) What rights are at stake? c) what is fair or just? The ultimate question is: how should we live? The answers to these questions should apply to the whole sector and help to shape the culture within financial institutions but they have to be provided by the individuals working there and not by the law. Most importantly the answers have to be communicated to the public by those producing them and not by regulators.

Bibliography:

-Andrews, P. (2016), "Culture in UK banking – regulatory priorities" Speech to Westminster Business Forum, available at https://www.fca.org.uk/insight/speech-culture-uk-banking-regulatory-priorities

-Armour. J., Awrey D., Davies. P., Gordon J., Mayer C. Payne, J., (2016) *Principles of Financial Regulation*, Oxford University Press, pp.81-98.

[101] Wheatley, M., Chief Executive of the FCA, "Historic link between ethics and economic success" Speech to the Worshipful Company of International Bankers, London 4 March 2014, available at https://www.fca.org.uk/news/speeches/ethics-and-economics [accessed March 31, 2017].

-Bailey, A. (2016) "Culture in financial services—a regulator's perspective", Speech at the at the City Week 2016 Conference, London, 9 May.

Bailey, Al. (2017) "Culture in financial institutions: it's everywhere and nowhere". Speech at the HKMA Annual Conference for Independent Non-Executive Directors, 16 March.

-Bank of International Settlements (2017) "Global Code of Good Practice for Foreign Exchange Markets", available at https://www.globalfxc.org/docs/fx_global.pdf

-Banking Standards Board, "BSB Annual Review 2016/2017", available at https://www.bankingstandardsboard.org.uk/pdf/banking-standards-annual-review-2016-2017.pdf

-Barigozzi F. & Tedeschi, P. (2015), "Credit Markets with Ethical Banks and Motivated Borrowers", *Review of Finance*, 19: pp.1281–1313.

-Boatright, J.R. (2013), *Ethics in Finance*, Wiley.

-Bosworth-Davies R. (2015) "The emergence of the criminal financial institution: can effective measures be implemented to deal with them?" *Comp. Law*. 2015, 36(10), 307-309.

-Bowen H. (1953), *Social Responsibilities of the Businessman.*

-British Bankers' Association report "The Benefits of Banking 2016".

-Carney M. (2017) "The high road to a responsible, open financial system", Speech, Thomson Reuters, Canary Wharf, 7 April.

-Carroll, A. B. (1999) "Corporate social responsibility— Evolution of a definitional construct", *Business and Society,* 38: 268–295.

-Commission of the European Communities (2001), Promoting a European framework for Corporate Social Responsibility, Green Paper, Brussels, 18.7.2001, COM(2001) 366.

-Communication from the Commission to the European Parliament, the Council, the European Economic and Social Committee and the Committee of Regions, Brussels, 25.10.2011, COM(2011) 681.

-Cranston R., Avgoulea E., Van Zwieten K., Hare C., Van Sante T. (2018) *Principles of Banking Law, (3rd Ed.)* Oxford University Press.

-Filabi A. “Carrot or Stick? Culture as a Regulatory Approach”.

-financemanates.com, ”Deutsche Bank Fined $205 Million by NY Regulator over Forex Violations”, 20 June 2018, available at https://www.financemagnates.com/institutional-forex/regulation/deutsche-bank-fined-205-million-ny-regulator-forex-violations/

-Financial Conduct Authority “Annual Report” for 2016/17.

-Conduct Authority (2018) “Transforming Culture in Financial Services”, Discussion Paper 18/2, March, available at https://www.fca.org.uk/publication/discussion/dp18-02.pdf

-Financial Stability Board (2018) “Crypto-assets”, Report to the G20 on work by the FSB and standard-setting bodies, 16 July, available at http://www.fsb.org/wp-content/uploads/P160718-1.pdf

-Financial Stability Board “Strengthening Governance Frameworks to Mitigate Misconduct Risk: A Toolkit for Firms and Supervisors”, April 20.

-Freiberg, A. (2010), *The Tools of Regulation*, The Federation Press cited in J. McCalman, A. Young and R. Chan (2017) “Regulating the culture of banks in the United Kingdom: strengthening legal accountability or just better leadership?” *J.I.B.L.R.*, 32(6), pp: 261-26*8.*

-Group of Thirty (2015), “Banking Conduct and Culture: A Call for Sustained and Comprehensive Reform”, available at http://group30.org/publications/detail/166

-Herzig C. and Moon J. (2012) “Corporate Social Responsibility, the Financial Sector and Economic Recession”, International Centre for Corporate Social Responsibility, Nottingham University Business School.

-HM Treasury (2012) “Sanctions for the directors of failed banks”.

-Iscenko, Z., Pickard, C., Smart L., and Vasas Z. (2016) "Behaviour and Compliance in Organizations", Financial Conduct Authority Occasional Paper No.24, December, available at https://www.fca.org.uk/publication/occasional-papers/op16-24.pdf

-Kinderman, D. (2015) "Explaining the rise of national corporate social responsibility: The role of global frameworks, world culture, and corporate interests" in K. Tsutsui & A. Lim (Eds.), *Corporate Social Responsibility in a Globalizing World* (Business and Public Policy, pp. 73-106).

-Levilee, N.P. (2011), "The role of obedience in society", *Inquiries Journal*, 3(5), 1-1.

-Matten, D., & Crane, A. (2005) "Corporate citizenship: Toward an extended theoretical conceptualization", *Academy of Management Review***,** 30: 166–179.

-Matten D. Moon J. (2008) "Implicit" and "Explicit" CSR: A Conceptual Framework for a Comparative Understanding of Corporate Social Responsibility" *Academy of Management Review*, Vol. 33, No. 2, 404–424.

-McCalman, J., Young A. and Chan R. (2017) "Regulating the culture of banks in the United Kingdom: strengthening legal accountability or just better leadership?" *J.I.B.L.R., 32(6), pp: 261-268.*

-McDaniel, Jr., C., (2015) *Civil Society and the Reform of Finance*, McDaniel, Taylor and Francis.

-McDerrmott T. (2014) "Learning the lessons of the past as an industry", Speech delivered at the FCA's Enforcement Conference, London.

-McDermott, T. (2015) "Personal Accountability", Speech delivered at the City & Financial conference on Personal Accountability in the Financial Services Industry, 2 December 2015, London.

-Meyer, J., Pope, S., and Isaacson, A. (2015), "Legitimating the transnational corporation in a stateless world society" in K. Tsutsui & A. Lim (Eds.), *Corporate Social Responsibility in a Globalizing World*. Cambridge: Cambridge University Press.

-Moon, J., Crane, A., & Matten, D. (2005) "Can corporations be citizens? Corporate citizenship as a metaphor for business participation in society", *Business Ethics Quarterly*, 15: 427–451.

-Mullineux, A. (2011) “The Public Duties and Social Responsibilities of Big British Banks”, *International Advances in Economic Research, 17*(4), 436-450.

-Mullineux, A. W. (1987), *UK Banking after Deregulation*. Beckenham: Croom Helm.

-New City Agenda (2016) “Cultural Change in the FCA, PRA and Bank of England: Practising What They Preach?”.

-New York Times (2018) “*Congress Approves First Big Dodd-Frank Rollback”,* May 22, available at https://www.nytimes.com/2018/05/22/business/congress-passes-dodd-frank-rollback-for-smaller-banks.html

-Papadopoulos C., “Financial services productivity held back by over-regulation”, City A.M. 18 February 2016, available at http://www.cityam.com/234963/financial-services-productivity-held-back-by-over-regulation

-Parliamentary Commission on Banking Standards, (2013) ’Changing Banking for good’, Final Report, vol.I, p.15, available at http://www.parliament.uk/documents/banking-commission/Banking-final-report-volume-i.pdf

-Paulet E., Parnaudeau, M., Relano F., (2015) “Banking with Ethics: Strategic Moves and Structural Changes of the Banking Industry in the Aftermath of the Subprime Mortgage Crisis”, *J. Bus. Ethics* 131:199–207.

-Populus, “Trust in Banks: What went wrong and how to fix it” available at https://www.populus.co.uk/2017/12/trust-banks-went-wrong-fix/

-Positive Money, “Polling: 10 Years After the Financial Crisis, the British Public Still Don't Trust Banks”, 16 August, 2018, available at https://positivemoney.org/2018/08/british-public-dont-trust-banks/

-Prakash A. (2015) “Corporate Social Responsibility as Social Regulation” in K. Tsutsui, A. Arbor,.A. Lim (Ed.), *Corporate Social Responsibility in a Globalizing World*, Cambridge University Press, 430-454.

-Rosamund T. M. (2015), *Business Ethics and Corporate Social Responsibility*, Ethics International Press.

-Simpson S., (2002) *Corporate Crime, Law and Social Control*, Cambridge: Cambridge University Press.

-Steare, R. (2018) "Character, culture and conduct: why good people do bad things in a fear-driven culture" in Financial Conduct Authority "Transforming Culture in Financial Services", Discussion Paper 18/2, March, available at https://www.fca.org.uk/publication/discussion/dp18-02.pdf

-Steare. R. *Ethnicability*, 2009.

-Stewart M (2017) "The expanding scope of individual accountability for corporate misconduct", speech delivered at the New York University Program on Corporate Compliance and Enforcement on March 31

-Tenreyro, S. (2018) "The fall in productivity growth: causes and implications", Speech at Peston Lecture Theatre, Queen Mary University of London, 5 January.

-UK Department for Business Innovation and Skills, (2014) "Good for Business & Society: Government Response to call for Views on Corporate Responsibility", April.

-YouGov-Cambridge (2013) "Public Trust in Banking - YouGov", Report.

-Wallace T. "Customers won't trust banks for a generation", The Telegraph, 6 March 2016.

-Wheatley, M. (2014) "Historic link between ethics and economic success", Speech to the Worshipful Company of International Bankers, London, 4 March.