HM Treasury

Financial Services (Banking Reform) Bill

Government Amendments: Criminal sanction

Briefing for Peers **October 2013**

Criminal sanction

Serious bank failure results in severe economic disruption and considerable losses for taxpayers. In the wake of the financial crisis, £65 billion of taxpayers' money was used to bail out banks on the brink of failure,[1] and the annual cost of financial crises to the UK economy as a whole has been estimated by the Independent Commission on Banking at approximately 3 per cent of GDP, or around £40 billion in 2010 terms.[2]

Despite the severity of these consequences, the existing range of financial crimes does not cover the kind of mismanagement by bankers at senior levels which can contribute to such catastrophic failures.

In its final report, *Changing Banking for Good*, the Parliamentary Commission on Banking Standards (PCBS) concluded that, "there is a strong case in principle for a new criminal offence of reckless misconduct in the management of a bank." Following the publication of the Commission's report, the Prime Minister announced his support for the introduction of criminal penalties against bankers who behave irresponsibly. This was confirmed in the Government's response to the Commission, published on 8 July.

These clauses introduce a new criminal offence for reckless misconduct in the management of a bank. The new offence will strengthen individual accountability for senior bankers, and act as a deterrent against misconduct.

In its report, the Commission stated that it would expect the new offence to be pursued

> "in cases involving only the most serious of failings, such as where a bank failed with substantial costs to the taxpayer, lasting consequences for the financial system, or serious harm to customers. The credibility of such an offence would also depend on it being used only in the most serious cases, and not predominantly against smaller operators where proving responsibility is easier, but the harm is much lower."

In light of this, the offence will cover banks and building societies, but not credit unions.

In line with the PCBS's recommendations, the new offence will be applicable only to individuals covered by the new Senior Managers Regime. Senior managers could be liable if they take a decision which leads to the failure of

[1] National Audit Office, *The Comptroller and Auditor General's Report on Accounts to the House of Commons: The Financial Stability Interventions*, July 2011.
[2] Independent Commission on Banking, *Final Report*, September 2011, paragraph 5.8 and 5.67.

the bank, or fail to take steps available to them to prevent such a decision being taken. The offence will only apply to behaviour which falls far below the standard that could reasonably be expected of a person in that position – this is similar to the test for corporate manslaughter. In addition, at the time the decision was taken, the senior manager must have been aware of a risk that its implementation may cause the failure of the bank.

Limiting application of the offence to individuals who are covered by the Senior Managers Regime, and the precise definition of when a bank has failed for the purposes of the offence, mean that those affected should be in no doubt as to their potential criminal liability.

The maximum sentence for the new offence is seven years in prison and/or an unlimited fine. This is in line with the recommendation of the PCBS, which argued that the offence must carry the possibility of a prison sentence to be effective, and with other offences of similar gravity in the context of financial services. For example, the three new offences created in Part 7 of the Financial Services Act 2012 (dealing with misleadingly causing someone to enter agreements or deal with investments, and misleadingly manipulating benchmarks like LIBOR) all carry this maximum penalty on indictment.

Further Enquiries

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2. For access to publications please go to http://www.gov.uk/government/policies/creating-stronger-and-safer-banks