



The Law Society

## **Legal breakfast summary**

**Managing risk and regulation: advising corporate clients in  
uncertain times**

March 2009

supporting  
solicitors

The Law Society Legal Breakfast Series was launched in May 2008 with the aim of exploring the opportunities for legal business operating in the regulatory environment created by the Legal Services Act.

The fifth Legal Breakfast event was held on 31 March 2009 to address the challenges facing the financial and legal sectors in their management of risk and the changed regulatory climate in the current economic downturn.

The speakers were (in order of appearance):

- Rick Haythornthwaite, Chairman, Risk and Regulatory Advisory Council
- Mark Harding, Group Counsel, Barclays plc

Each speaker gave a ten minute address, after which questions were taken from the audience and a lively debate ensued.

### **Policy maker's perspective**

Rick Haythornthwaite explained that the priority of policy-makers is now less on 'better regulation' and more on 'risk management'. Many instances of disproportionate policy response can be traced back to poor government reaction to matters of public risk. He explained that influential players in the public debate about risk include the media, local authorities, insurers, academics, single issue lobby groups and others. It is not in their interest to minimise the perception of risk, which leads the public to disengage and pass that risk management across to the government. Government is consequently faced with a public that is increasingly intolerant of failure and falls victim to the 'Something Must Be Done' syndrome. He emphasised the danger of the propagation of the view that it is acceptable to push for zero risk tolerance across government and society.

### **Regulation - principle or outcome based?**

There was extensive debate about the definitions and desirability of the prevailing form of financial services regulation (i.e. principles-based) and the potential for transition to an outcomes-based system. Mark Harding suggested that the UK financial sector is anticipating such a move. He also expressed scepticism that the failure of the financial regulatory system was a problem of design - instead he felt that the necessary powers existed but were used ineffectively. He questioned whether principles-based regulation had ever existed. One contributor from the floor concurred, arguing that the phrase principles-based regulation had become confused with light-touch regulation and had become undesirable by association. Mark Harding opined that the problem with outcomes-based regulation is not the principle, but more the problem of agreeing what those outcomes should be.

There was agreement on the panel and in general discussion that a clear indication of outcomes and indicators is required. The lack of clarity makes it increasingly difficult for Compliance Departments to fill in the gaps and effectively second-guess the regulators. Rick Haythornthwaite felt it would be wrong to switch completely to rules-based regulation, but that there needs to be more 'rule' than 'guidance' and a better shared definition of what a rule constitutes.

A contribution from the floor raised the difficulty in measuring the effectiveness of compliance. He added that it was impossible to stop the 'determined man factor' - the person who breaks the rules in the full knowledge of the potential repercussions of his actions. He was concerned that this would reflect on corporate compliance in an environment of zero tolerance and that there was too great an emphasis on punishing companies rather than individuals.

### **Active collaboration**

It was broadly agreed that the key to navigating the new regulatory landscape lies in increased engagement, cooperation and collaboration with policy makers and the regulatory authorities. Rick Haythornthwaite stressed the need to 'stop asserting and start co-analysing' with the regulators to help them tease out the dynamics of the driving forces behind both risk and perceptions of risk in order to help them resolve the best level, type and place of regulation. He argued that, rather than imposing business plans on regulators, it is necessary to collaborate to demonstrate that business plans are aligned with the direction in which regulators wish to be heading. He implored businesses to 'return every time to outcomes' rather than to 'retreat to process' once alignment had been reached.

Mark Harding re-emphasised the need for collaboration and stressed that regulatory change is inevitable. He said that changes in regulation will lead to new relationships between the regulator and the regulated, not least because the regulator will maintain much closer and more intrusive contact with regulated institutions. He also highlighted the need for effective coordination between International, EU and local regulatory initiatives to avoid significant competitive distortion.

One contributor highlighted the hitherto unconstructive attitude of businesses and especially trade associations in their dealings with the FSA. He argued they opposed without any gesture towards consensus or providing an alternative.

There was some scepticism within the room that it was possible at the present time to find suitable interlocutors to allow dialogue and consultation between the banking industry and the government in order to deflect the charge that the government was being 'soft' on bankers.

## **The role of external counsel**

Mark Harding offered the benefit of his experience as a 'sophisticated' procurer of external legal support to give his thoughts on how legal firms could alter their approach to offer a better service to their clients in the current environment.

While generally very positive about the work undertaken by corporate law firms, he felt that they could do more to provide a more thoughtful 'risk radar' to help internal counsel assess and manage the legal risk inherent in their business. He also expressed a desire for creative thinking about how better processes for the management of legal risk can be put in place. Whilst acknowledging a point from the floor that corporate law firms were generally brought in to oversee transactional business, he felt that more businesses would engage with external counsel on a forward-view basis if they felt that it offered sufficient value. He highlighted the need to provide increased legal certainty, citing in particular the use of anti-terrorism legislation to freeze the assets of Icelandic banks and the potential for other vagaries within badly framed legislation to create uncertainty.

## **Potential regulatory impact of the financial crisis**

There was some disagreement as to whether there would be significant regulatory impact on other sectors of the problems of the banking and financial services industries.

Rick Haythornthwaite did not feel that there would be great overflow into other sectors, but he did think that it would affect the mood in which regulatory policy was made. Mark Harding thought it was generally too early to say the degree to which there would be impact on other sectors, although he voiced his expectation that there would be some effect in terms of corporate governance. The general opinion on the floor tended towards fearing the worst. One contributor felt that the enormity of the financial crisis made it inevitable that there would be some cross-over.

On the subject of legal regulation, Mark Harding felt that corporate clients were not significantly concerned about the way in which their external counsel was regulated. However, while relief of onerous regulatory burdens to facilitate the running of law firms is also in the interests of the client, he added a caveat that there will remain issues where clients expect appropriate regulation and high standards - specifically management of conflicts of interest, maintenance of confidentiality obligations and the approach to liability capping.