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Maybe Lawyers Should Become the Public's Guardians

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The fragility of the U.K. banking sector has become a staple of economic and political discourse, with commentators regularly predicting its imminent demise, dragging us all down into a pit of unemployment, business insolvency, house price collapse and productivity levels even lower than their – already dire – current levels.

The risks are certainly overblown: U.K. banks and building societies maintained strong capital and liquidity positions during COVID, and have been posting healthy profits in the post-pandemic era. The major banks passed the Bank of England's resilience test (using a severe stress scenario) with largely flying colours and the collapse of Credit Suisse and of a trio of mid-size U.S. banks in 2023 barely caused a ripple in the U.K. banking pond.

That should not encourage complacency, however. The sector is vulnerable to a host of challenges outside its control, from global economic problems (such as slowing economic growth, reduced money supply, higher interest rates and risks from supply chain disruptions) to disruptive forces such as climate change, open data, digitisation of currency and decarbonisation, not to mention the ever-present risk posed by geo-political tensions.

Might it also be vulnerable to threats from within, from those who are charged with or heavily invested in protecting the banking system: the politicians, the regulators and the bankers themselves? And if so, who poses the greatest risk?

It seems odd to pose that question in relation to regulators, whose *raison d'etre* is, arguably, the maintenance of financial stability (though some would say its principal function seems to be the facilitator of moving risk from consumers to banks). However, their control of the prudential framework within which banks are compelled to operate – particularly in relation to capital requirements, liquidity and risk management practices – confers upon them considerable capacity to do harm, if that control is not exercised intelligently and appropriately.

The difficulty of that task should not be underestimated, involving as it does balancing the need to protect consumers; to ensure and monitor the resilience of financial institutions; and to mitigate systemic risks against the risk of stifling the banking sector.

The latter point carrying the risk of rendering the U.K. uncompetitive in relation to comparable – and often rival – jurisdictions, and encouraging banks to diversify into the unregulated sphere or less heavily regulated markets overseas (with potential negative impacts on both the banks themselves and the wider economy). Moreover, the outcomes of regulatory demands are not always binary: a heavy hand on the tiller, whilst potentially warranted on the ground of consumer protection, can increase expenses and operational stresses on banks, particularly smaller ones, affecting banks' profitability, impeding competition and leading to heavier costs on consumers, particularly borrowers.

There is no guarantee that regulators will successfully balance these competing considerations, or that they will act with the nimbleness and decisiveness that effective regulation in a dynamic market requires.

That said, regulators are perhaps better described as a challenge rather than as an existential threat, and there is scope for mitigating their actions through active engagement and cooperation between banks and the regulatory authorities.

The same can be said of politicians: whilst it is difficult to categorise them as a "threat", their actions (or, as often, their inaction) can have a significant impact on the financial sector. Political decisions can have deleterious consequences for the wider economy (one thinks of the Kwarteng "non-budget" of September 2022), whilst policy choices on trade, international cooperation, taxation and government debt shape the financial environment within which banks have to operate.

Banks are – or should be – sufficiently agile to cope with most of these, but even the most prudent bankers cannot anticipate what policies a government, subject as it is to media and popular pressures and living under the Damoclean sword of four-to-five-yearly electoral scrutiny, might suddenly alight upon as giving them a short-term breathing space at the expense of bankers (never a popular cohort, in the press at least).

What, then, of those who have to steer the financial sector through this ever-changing political, regulatory and economic landscape, whilst still making a profit: the bankers themselves?

Their decisions on, amongst other matters, lending practices, risk exposure, and investment strategies have profound implications for the health and viability not only of individual banks but of the financial sector as a whole. They are constantly scrutinised and judged on how they respond to the increased oversight of regulators, political and societal pressures in relation to (amongst other matters) ESG, decarbonisation and responsible lending, and the challenges posed by the increasing digitisation of banking services and the resultant need for robust cybersecurity systems.

That is a weighty burden for bankers to bear, all the more so in an age of activist shareholders and increased global competition, in which the need to drive profits becomes ever more critical. However, whilst a serious mis-step could have grave consequences for an individual financial institution, it is difficult to see how – in the tighter regulatory and prudential framework put in place after the great financial crash of 2007-2008 – it could bring the entire system tumbling down as so nearly happened 16 years ago.

Therefore, if looking for the greatest threat to the banking sector, it would be wrong to single out the bankers, the regulators or the politicians individually. It is in their combination that the danger lies: for instance, politically-sanctioned regulatory overreach could stifle innovation by the banks, with knock-on consequences for the economy as a whole. And ultimately, it is events – and how regulators, politicians and bankers respond to them – that ultimately make or break economies and the financial systems that underpin them.

What then about the lawyers? Well, perhaps they should be the public's guardians to ensure that regulators don't overreach themselves; that bankers are held to account; and that the courts retain supervision of the politicians through public and administrative law. Maybe lawyers should take on the role which finally answers that question: *quis custodiet ipsos custodes?*

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"Incredible work ethic, powerful submissions and killer cross-examinations - the ultimate advocate who also provides great strategic input." (Legal 500, 2024)

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