



CHANCELLOR
OF THE HIGH COURT

Banking Standards Board Lecture

***Integrity and independence in the judiciary and
the financial services industry: a comparative
study***

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England and Wales**

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Abstract: The Chancellor will explore, in the context of the digital revolution, the culture of and relationship between the UK financial services sector, the UK legal profession, and the judiciary in the Business and Property Courts of England and Wales, in a changing economic environment, and consider the importance of an independent and trusted judiciary to an internationally competitive UK financial services sector.

Introduction

1. May I first thank Dame Colette Bowe for inviting me to deliver this talk.
2. I want to examine the different approaches to integrity and its importance in the legal community on the one hand and in the financial services industry on the other hand in the context of the digital revolution. In many ways, the law and financial services have an important symbiotic relationship, which will need careful monitoring as the essence of what we all do changes in the coming months and years.
3. I feel reasonably well-qualified to speak on this subject, having undertaken litigation arising out of some of the biggest financial scandals of the day over some 32 years at the Bar. I was involved in the early 1980s in Alexander & Alexander, which was one of the earliest Lloyd's scandals and I acted for the finance

director of Guinness in the Guinness/Distillers takeover in the mid-1980s. From there, I moved on to act for the MGN Pension Fund trustee in the Maxwell affair. I later acted for the Lloyd's names in their successful claims against the Gooda Walker syndicates, and then in the Barings scandal, and in many more later such sagas. I was also before 2009 a judge in the Courts of Appeal of three offshore jurisdictions, where we saw a wide variety of cases concerning international financial frauds and scams. Since then, I have been deciding cases at various levels of the judiciary in England & Wales in more modern financial scandals.

4. There is, however, a distinction to be made at the outset between dishonesty and mismanagement, although the two sometimes overlap. The scandals I have mentioned were mostly occasioned by out and out dishonesty, but some other massive pieces of litigation may be somewhere on a sliding scale of mismanagement and dishonesty. I am thinking of the Bank Charges litigation in the late noughties, which I took all the way to the Supreme Court, and a number of more recent financial services insolvencies. Again, in the context of a digital era, the manifestations of dishonesty will change dramatically, and effective management will take a completely different form when paper-based transactions are a thing of the past.
5. The subject of honesty and integrity is, however, always a difficult one, because generally people prefer not to talk about it, assuming, when the evidence is often to the contrary, that it exists in greater measure than it actually does. The BSB's latest survey of some 35,000 employees in some 25 banking institutions shows that integrity is far from a universal feature. In answer to the statement "I see instances where unethical behaviour is rewarded", 25% of respondents either agreed or neither agreed nor disagreed. In commenting on the statement that "my colleagues act in an honest and ethical way", 9% either disagreed or neither agreed nor disagreed.
6. These results and some of the financial scandals that I have already mentioned, and many that I have not, demonstrate quite clearly that a lack of integrity in financial services surfaces in every generation. It is worth investigating, therefore, firstly some of the reasons why integrity remains important, secondly the causes of continuing lapses, and thirdly what the relationships between the legal community and the financial services industry can do to ameliorate these ongoing issues, and what we may expect in the future.

The necessary context

7. Before I do that, however, I would like to say a little more about the necessary modern-day context for a discussion of financial and legal integrity. It is already apparent that there is considerable scope for fraud in the brave new world of fintech, smart contracts and artificial intelligence, to say nothing of cyber-crime, hackers and cyber-blagging. Credit card and online banking scams are just the start. This context may make the frauds of yesteryear look modest, even though we may have thought back in the day that Mr Maxwell, for example, was something of a giant in that field.
8. As far as digitalisation is concerned, we are staring into a firmament about which few people of my generation have any comprehension. The way in which both legal and financial services are delivered will be unrecognisable even 5 years from now. The growth of fintech and legaltech is exponential and will also have dramatic effects on the problems thrown up by a lack of integrity. Mark Carney, the Governor of the Bank of England, suggested in a speech on 2nd March 2018 that it was time to regulate cryptocurrencies and their ecosystem. Whilst he did not believe that cryptocurrencies posed a current risk to financial stability, they could do so “if more consumers piled in”. The Prudential Regulatory Authority and the Financial Stability Board are looking closely at the problem as we speak. I discovered last week, however, that the FCA has approved at least one bond issue in a cryptocurrency, Ethereum, recorded on a public blockchain.
9. There are certainly more very positive aspects to the context. Another aspect of it is the steps that have been taken since the 2008 financial crisis to strengthen UK financial institutions. Sir John Cunliffe explained the lessons we have learnt in a lecture that he gave in September 2017 to “celebrate” or perhaps “mark” the 10th anniversary of the collapse of Northern Rock. When we recall the failures of Northern Rock, Lehmans, RBS and Lloyds and the litigation that those events have caused, one can immediately see how close the relationship is between the legal and the banking sector.
10. John Cunliffe also reminded us of the international nature of banking collapses when he said that confidence in the regime for the resolution of international banks is of crucial importance to the UK, because we are home to a number of major international banking groups, and host to a very large number of foreign banks. We thereby import considerable risks from other jurisdictions. For that reason, Sir John concluded “[i]t is ...

crucial to financial stability in the UK that we can rely on foreign banks operating in our jurisdiction having viable resolution strategies in line with international standards. Absent such assurance, we would need to ensure the entities operating here have greater resilience locally”.

11. Then, in terms of context, we should not forget the dramatic developments in legaltech that are changing the way in which legal services are delivered. I attended a conference earlier this month at which a number of young entrepreneurs spoke about their legal and financial start-ups. They gave a fascinating insight into what we will be dealing with in a few years if not months:
 - (1) The first was the development of an artificial intelligence software platform for intelligent automation of knowledge, documents and processes. The aim is to reduce lawyers’ bills. JP Morgan reduced what they spent on lawyers by 360,000 hours in a year, it is said, by using these tools. McKinsey claim that by 2030, 83% of lawyers’ work will be automated, and 79% of judicial work will be automated.
 - (2) The second was a project aimed at preventing “intentional data loss”, where staff of major companies fraudulently or at least improperly send sensitive data to personal emails. That same project has developed a system aimed at identifying malicious incoming emails.
 - (3) The third was a project on contract automation that would allow lawyers to negotiate live online rather than using the track-changes facility in Word introduced more than 20 years ago.
 - (4) The fourth was a business that stopped sensitive emails going to the wrong people, using machine learning to understand what is normal. In that way, the system can conclude if any particular email is going to the correct recipient before it is sent.
 - (5) The fifth project concerned the need for international integration of legislation on the use of artificial intelligence. One can easily imagine how impossible it would be if there were, for example, different legislation in different states in relation to driverless cars. How would you be able to travel beyond national boundaries? Likewise, the regulatory approach to blockchain simply

cannot be different in different countries, since the technology is borderless and global.

12. And in terms of dispute resolution, we are also on the verge of a technological revolution. We are introducing online courts to deal with divorces, guilty pleas, social security issues, and small claims up to £10,000. But we should not suppose that online dispute resolution will stop there. It will not be long before cases in the Business and Property Courts also have an online element, even if they are not immediately undertaken entirely online. I have said for a long time that now that we can get everything we want on our smart devices either instantaneously or at worst within 24 hours, neither the public nor business people will any longer accept the speed at which we presently deliver justice. There will be an urgent imperative requiring the justice system to make full and proper use of technological advances to create a far speedier and less ponderous justice system if we are to retain the confidence of the millennial generation.
13. Of course, one of the most important parts of the current context to this talk is the departure of the UK from the European Union. That will create challenges in terms of the regulation of the financial services industry and of competition. But it will not, I think, inhibit the growth or globalisation of fintech. There are opportunities here for English law and UK jurisdiction to offer the legal foundation for both digital ledger technology and smart contracts, using the inherent flexibility of the common law, based as it is, not on a statutory code, but on a set of principles that can be applied to any developing commercial situation. I will return to that issue in a moment.
14. To summarise then, the background to a consideration of integrity in the law and financial services encompasses the terrain in which we will all be operating, namely global digitalisation and the rapidly changing regulatory position as we leave the EU. The areas of danger will continue to include fraud, cyber or otherwise, banking collapses, economic instability and insolvency risks more generally.

Why is integrity important?

15. I can start then with the reasons why integrity in the legal system and in financial services is important.

16. It is obvious that potential court users will only wish to use a particular legal system to resolve their business disputes if they have confidence in its integrity. That is the same whether or not the process is web-based. Moreover, overseas investors will only wish to invest in a market where a reliable, efficient and independent dispute resolution process is available. The integrity of any legal system starts, of course, with the need for an independent and incorruptible judiciary, and proceeds through the need for an independent legal profession, which is willing to act for anyone without fear or favour, and ends with the constitutional safeguards that protect the courts from political interference and allow them to operate independently to resolve disputes fairly, including those that involve the state itself. These are major elements, of course, of the rule of law.
17. As regards the financial services industry, there are similar but not identical reasons for the need for integrity. Overseas investors will not, of course, choose to use UK financial services unless they have confidence in their integrity. They have a choice; just as overseas business people have a choice about whether they wish to use UK dispute resolution services. The need for integrity does, however, have other features. There is, for example, always an insolvency risk for investors. The integrity of management will generally reduce that risk, but is very difficult for an outsider to evaluate. The quality of regulation will also reduce the risks of fraud and insolvency, but generally regulators, like auditors, assume integrity rather than a lack of it, so there remains the need for a culture of integrity if the financial services industry is to maintain a secure reputation.
18. So, with that introduction to the need for integrity in each of the legal system and the financial services industry, we should ask how successful we have been in the past and what can be done to improve what we are doing in the future.

Have we successfully defended the integrity of our institutions?

19. How well, then, has the legal system done in maintaining its integrity over the years? First, we should not assume, as many do, that legal systems across Europe are equally reliable.

20. Some 11,712 judges participated in a recent survey undertaken by the European Network of Councils for the Judiciary. Those judges came from some 25 European countries. In 18 of those 25 European countries, more than 10% of judges thought that some of their colleagues either were taking bribes or were not sure whether they were. Those countries where over 50% of judges thought their colleagues either were taking bribes or where they were not sure were Bulgaria, Latvia, Romania, Croatia, Czech Republic, Italy, and Lithuania. That is by itself a shocking list, but when you know that even France, Germany, Belgium and Austria and Spain are included in those countries where more than 10% of judges thought their colleagues either were taking bribes or where they were not sure, the level of concern is increased. Only Sweden, the UK, Ireland, Finland and Denmark produced entirely negative results in this part of the survey.
21. So, let us assume that we do, in the UK, have courts that can be relied upon to decide business cases fairly. How does that legal system interact with the financial community? There are many situations in which the financial services industry in general and the banks in particular encounter the courts and other forms of dispute resolution. These range from the humble mortgage action to the recent RBS class action. Somewhere in the middle are the occasions on which the Business & Property Courts are asked to approve Part VII banking business transfer schemes and insurance business transfer schemes and, more recently, the major banks' ring-fencing transfer schemes. I recently approved the first such ring-fencing transfer scheme promulgated by Barclays. The ones promoted by Lloyds, Santander, HSBC and RBS will follow shortly. But, in addition, we are expecting a surge in the more normal Part VII insurance and banking business transfer schemes as the day on which we will leave the European Union approaches.
22. Nonetheless, the occasions on which the banking and financial services industry actually come into direct contact with the courts are relatively few and far between. But banks have ever growing legal departments and are more and more influenced by their general counsel, as used to be the case only in the US.
23. I think it is not so controversial to say that the banks and financial services have not done quite as well in terms of integrity in recent years as some may like to think. There has been a massive increase in carousel frauds, some involving banks. These frauds are providing a huge workload for HMRC in their attempts to recover the value added tax avoided. The LIBOR scandal had far-reaching effects. The banks that falsely

inflated or deflated their rates did so in order to improve their apparent creditworthiness or simply in order to make a quick trading profit. Since LIBOR is said to underpin some US\$350 trillion worth of derivatives, this had a huge systemic effect on the market and on the other financial products that relied on LIBOR as a reference rate, such as ordinary domestic mortgages, consumer credit transactions, and even student loans.

24. I do not think that we should assume that the prophylactic measures that Sir John Cunliffe celebrated in his recent lecture have put an end to risk-taking or a lack of integrity. Financial success will always involve taking risks, and some of those who take risks will always sail close to the wind. The results of the BSB's survey that I alluded to just now confirm what I have said. Even if the results have improved a little from 2016 to 2017, there is still a way to go.
25. It is noteworthy that there are many more fintech and legal tech start-ups in the UK than in any other country in the EU. Some of these start-ups will, as I have already mentioned, reduce the risk of fraud, for example by preventing data loss. But other aspects of digitalisation will provide opportunities for those wishing to game the system. For the older ones amongst us, cyber insecurity in the burgeoning digital environment is probably the most frightening risk of all.

What are the prospects for future integrity?

26. I would not want to be pessimistic, but I think the very speed of some of the advances I have spoken about gives rise to a greater risk of fraud in our financial and legal systems than ever before. Some think, or perhaps hope, that greater and more effective regulation will reduce those risks, but I am not completely sure. Heavier regulatory burdens can slow down technological advance. That is perhaps why we have more tech start-ups than in other parts of Europe (though Paris and Berlin are working hard to catch up); because the UK has always been on the side of a lighter touch approach to financial regulation than our EU colleagues. Interestingly, the US approach to fintech, mimicked elsewhere in Europe, has been to view its development through an entirely regulatory prism, whilst here we have taken more of a business-friendly wait and see approach – quite rightly I think.
27. In my view, we need to develop much smarter regulation than we have had in the past. The regulation needs somehow to be

part of the code that underlies the smart financial transactions themselves. Insider frauds and cyber-crime are the integrity lapses that we will be seeking to protect ourselves against. But cyber-crime moves fast and is continually evolving. In a meeting I had recently, I was told that the police will become an irrelevance if they do not move faster to ensure that they understand the digital environment in which cyber-crime can flourish. In some forces, officers have only recently been issued with functioning smart phones. Effective policing for the digital financial age will need to look quite different – and very soon.

28. There will, I think, also be an inevitably rather enhanced risk of fraud if we move headlong towards the use of permission-less digital ledger technology – towards the use of public blockchains for financial transactions. That is, of course, the use of digital ledgers to record transactions where any node or computer can join the network if it fulfils the coded requirements. So far, crypto-currencies have used permission-less DLT and that has already led to the DAO (distributed autonomous organisation) theft of \$60 million worth of the crypto-currency Ethereum. An answer may be the greater use of *permissioned* digital ledger networks, with which some of the banks are now experimenting. But even such systems are unlikely to be invincible. I should add a note of optimism: the blockchain bond issue that I have spoken about already seemed to go off without incident, and may be the first of many.
29. So far as the judicial system is concerned, there are the same risks of cyber-insecurity as we move towards online dispute resolution. But my concern here is as much about the quality of justice as digitalisation progresses. If we are to retain the pre-eminence of English law and our UK jurisdictions, we shall have to maintain and even enhance the quality of our justice systems, the integrity of our judges and, as I have said, the speed at which we deliver outcomes. We cannot stand still in the face of massively increasing competition internationally. There are, as you will all be aware, new “common law” courts operating in English to resolve financial disputes in Paris, Amsterdam, Brussels, Frankfurt, Kazakhstan, Abu Dhabi, Qatar and Dubai to name but a few. Many of those courts are already or will very likely be wholly or partly staffed by judges and lawyers originating from the UK. Against that background, the problems we face in recruiting enough of the very best business lawyers onto the High Court bench has come at a very bad time. I am not suggesting that we risk an imminent threat to judicial integrity, but the financial services industry which depends on the quality of our justice system cannot afford any reduction in judicial quality. Our legal system has historically only been as

resistant as it has to any depreciation in judicial integrity, because of the very high standards we have operated in our recruitment process.

30. Moreover, I think that our judicial system could be a little more cautious about its dealings with banks and financial services institutions. The courts have historically been over-trusting of some of the great institutions and insolvency practitioners, for example. Judges must, for example, scrutinise the Part VII schemes that I have spoken about with unstinting care. Public confidence in the financial and banking system depends on the quality of the scrutiny that judges give to cases involving these institutions. This will become even more important as we move into an entirely digital financial world.
31. When I spoke at the start of this talk about the symbiotic relationship between our two worlds, I meant what I said. The confidence of the international business community in our financial services depends on the quality of the legal system that underpins it. Likewise, if the international business community lost faith in the integrity of our financial services industry, we would see the volume of UK court-based dispute resolution, UK arbitration and UK alternative dispute resolution decline dramatically.

And what of the opportunities?

32. If we get some of what I have been talking about right, I think there are considerable opportunities for the UK in the brave new digital world. I have already said something about English law providing the legal foundation for the suggested 3 trillion financial services smart contracts that are likely to be entered into each year. We are well placed to provide that legal basis, because of the advantages of the common law, and because fortuitously we use English, which is probably more likely than, say Chinese, to provide any linguistic foundation for these smart contracts.
33. But as I started by saying, the integrity of our legal and financial systems is essential to all these opportunities. If we allow the quality of our judges or the integrity of our lawyers, banks and financial services providers to slip, we would be likely to damage our ability to capitalise economically on the digital era. The City of London still has a buzz about it, even as we are leaving the European Union. Young fintech and legal tech enthusiasts are not phased by change as are so many of the older generation.

But confidence can be lost as well as won, and the quickest way to see all this enthusiasm drain away will be if we fail to maintain and enhance our standards of integrity and our reputation for fair dealing.

34. Moreover, any future lapse in cyber-security in our financial or legal systems could be far more serious than any of the frauds I mentioned at the beginning of this talk. And the loss of confidence that such a lapse would cause could also be more serious than even, for example, the efforts of Mr Maxwell, despite the adverse effects he had on so many Mirror Group pensioners.
35. For these reasons, I think that the judiciary and the legal and regulatory community need to work more closely with those providing financial services to ensure that there is adequate vigilance in the context of a rapidly changing financial environment. That is one reason why I am so supportive of the formation of a concept group comprising government, financial services institutions, lawyers, the judiciary, regulators and legal and software and computer science academics. That group could look at developing the opportunities for the UK and the global legal and financial sectors, in addition to taking a detailed look at the increasingly complex security issues.
36. I would not dare to predict where the next great financial scandal is likely to arise. But I am sure they will not stop coming. The more we work together, the more I think we can be ready for them; the more we can limit their adverse ramifications when they come, and the more we can ensure that any loss of confidence that they cause in our financial systems and in our judicial system is as limited as possible.
37. What emerges from what I have said is, I think, the realisation that legal and financial services already transcend national boundaries. This trend is likely to increase dramatically with the growth of fintech, legal tech and artificial intelligence generally. Indeed, as I have said, judges themselves are already being recruited internationally.
38. The work of the Banking Standards Board and its excellent annual report for 2017-2018 focuses on trustworthiness and who is deserving of that trust. The BSB has obviously become an important force in the push towards greater safeguards and greater integrity in the financial system. It has done much good work, but it too must, I think, alongside other stakeholders, direct its attention as much to the creation of a culture of integrity in the digital space as to the enhancement of a culture

of transparency and honesty in financial management and operations.

39. Thank you very much for your attention.

Sir Geoffrey Vos, Chancellor of the High Court

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