Business conduct of financial institutions

Proper business conduct by financial institutions is more important than ever. Corporate culture and risk management play a key role. FINMA takes action against specific instances of misconduct and holds individuals to account. Where necessary, it issues a warning as a preventive measure.

More than almost any other branch of the economy, the financial sector depends on trust. But that trust, so often taken for granted in the past, has been seriously eroded in recent years, and especially since the financial crisis of 2008. More recently, the repeatedly unacceptable business conduct of many financial institutions has contributed to the problem.

There have been numerous examples of misconduct, some directly involving Swiss banks. They include fraudulent speculation by a trader in London, interfering in the prices of securities, aiding and abetting tax offences abroad and manipulating key interest rate benchmarks and the foreign exchange market.

The causes of misconduct

The common element in all these cases is a corporate culture driven by misdirected incentives and excessively focused on profit generation and variable salary components, with client interests taking second place. Business conduct risks have been identified and managed inadequately or even ignored. Some arise through violations of codes of conduct; others may be unregulated but are still of importance to operational business.

Requirements for proper business conduct

A number of general measures are required to reduce the risk of misconduct. Senior management must lead by example. Companies must not put profits before the interests of their clients. Remuneration systems must not incentivise inappropriate conduct. Firms need to pinpoint where the dangers lie, and issue internal directives and regulations to limit them. Employees need to be trained in what is expected of them, and adherence to directives must be rigorously enforced. Compliance needs to be a strong and effective control function; misconduct must be strictly sanctioned internally.

Role of senior management

Senior management must set an example in all aspects of business conduct. Top executives have to make it absolutely clear that profiting from inappropriate or unethical conduct will not be tolerated, and especially not rewarded.

Remuneration systems must send a clear message

Incentive systems, including those for senior management, must be appropriate. They must recognise more than just performance indicators, net new money inflows or profits. Proper business conduct, identification and prudent management of risks, as well as professionally conducted internal controls must also be rewarded. Executive salaries must reflect the degree to which those who receive them have lived up to their responsibilities. They must send a clear message, not merely recognising good practice through higher salaries and variable compensation, but also curbing remuneration that is not earned.

Improved identification and sanctioning of misconduct

Technology is making misconduct increasingly risky. The greater transparency that comes with the digital age is making it easier than ever to expose misconduct and sanction it accordingly.

FINMA takes corrective action whenever it identifies specific instances of misconduct. Increasingly, it uses the freedom granted to it by law to hold individuals to account and does not hesitate to ban them from practising when they are found responsible for serious misconduct.

If FINMA establishes that a problem is not an isolated incident but a more widespread phenomenon, it issues a preventive warning to supervised institutions. Going forward, FINMA will place increasing emphasis on monitoring compliance with codes of conduct.

Responsibility lies with institutions

Ultimately, the key to avoiding over-regulation and repressive measures lies with financial institutions themselves. They must recognise that they are part of a larger system that only works if the fundamental social consensus to support it is preserved.