Checks Needed For Naughty List To Improve Wall Street's Rep

By **Evan Weinberger**

Law360, New York (December 23, 2015, 11:09 PM ET) -- Wall Street banks may back a push to create a central registry of employees who misbehave in a bid to improve internal culture at the country's biggest banks, but worries about the accuracy of any potential list and other due process concerns have given some observers pause.

Federal Reserve Bank of New York President William F. Dudley has been advocating for the creation of such a central registry that can be used by banks when recruiting new talent as a way to make sure that serial rulebreakers are kept out of the biggest banks. And a readout of a meeting on bank culture with Wall Street bigwigs in November appear to show that the banks are getting behind the idea.

While creating such a central registry could go a long way toward preventing bad actors from engaging in future frauds and improving the internal workings of banks, there are risks that people could be wrongly included on the list and shut out from jobs, or that individuals could be made scapegoats for larger, institutional failures at the big banks.

In order to prevent that from happening, any formal registry of wrongdoers set up by the banks must have strict rules for when a person is added and how they can appeal their placement on the list, said Ellen Zimiles, a managing director at Navigant Consulting.

"It should be very clear why someone is named," she said.

The idea of a central registry for misbehavior among financial sector workers is not new. TheFinancial Industry Regulatory Authority already maintains one, and with the reputation of Wall Street in tatters following the financial crisis and the series of other mega-fines for anti-money laundering violations and benchmark rigging, the banking industry appears to support expanding it from the broker-dealer world to other sectors.

Participants in the November conference at the New York Fed said that they were concerned that they were unable to flag violations during the process of recruiting new hires from their competitors. Putting together an industry-maintained central registry similar to FINRA's could help prevent those serial violators from getting hired in the first place.

"Several participants noted a problem of blind recruitment and argued for a searchable database as a solution," a readout of the gathering posted on the New York Fed's website said.

The database could be used to chart violations by individuals that were not named in official enforcement actions, either because the violations were of internal bank policies or because the bank self-reported violations to regulators who then dealt with them outside of the enforcement action process, Zimiles said.

Even when there are enforcement actions, responsible individuals are not always named — a frequent complaint among critics of the regulators.

"You don't always know who is involved," Zimiles said.

Despite the seeming benefits of a central registry of bankers who break the rules, it will only work properly if appropriate safeguards are built in.

"Creating a central registry raises the potential for abuse when organizations seek to scapegoat individuals for what may be, in reality, organizational failures," said Anne Eberhardt, a senior director at consulting firm Gavin/Solmonese. "Such a registry would almost certainly raise concerns with respect to violations of individuals' privacy, particularly if there is no formal process requiring the establishment of culpability."

Participants in the New York Fed gathering raised similar concerns, according to the readout.

The registry would need to have a “safe harbor” provision to ensure accurate reporting, and employees would need the ability to challenge their placement on the list, participants said, according to the New York Fed’s document.

The appeals process and other employee protections would need to be in place to prevent the registry from being turned into a “system of rough justice,” the readout said.

The industry would also have to create a clear set of guidelines for when a violation would require placing an individual’s name into the registry, as well as other safeguards like approval from multiple supervisors, Zimiles said.

Those protections could “address those concerns because it would be very clear why someone is named,” she said.

Still, despite her concerns, Zimiles said that having a registry of bad actors could increase the amount of individual accountability for Wall Street’s misdeeds, something that has been lacking.

But some say it does not go far enough.

The Dodd-Frank Act mandated new compensation rules, and more than five years after the law’s passage, they have still not been completed. Without compensation reforms, including clawbacks for violations, a central registry will not be enough to truly reform Wall Street’s internal culture, said David Reiss, a Brooklyn Law School professor.

“Together, perhaps the registry and clawbacks could have a positive effect on firm behavior if they are implemented thoughtfully and are designed to work together,” he said.

And even with the addition of compensation reforms to the central registry forming a “belt and suspenders” approach to reform bank culture, the fiercest of Wall Street critics say that changes will not come unless bankers are brought before courts for alleged violations and sent to jail if found guilty.

“And, of course, along with the belt and suspenders, there should be prison bars as well,” Bart Naylor of Public Citizen said.

That’s something that critics say was missing after the financial crisis.

The registry, however, could be a start to bringing about much-needed accountability, they said.

--Editing by John Quinn and Philip Shea.