

#2 Compliance or Culture of Right Action?

By Gai Roper, Christina Kirk, Culture Navigator

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In May 2018, David Murray, then newly appointed Chair of AMP, was reported as saying:
*"... improving the cultural problems plaguing the financial sector will not be achieved by regulation alone."*¹

Haynes, in his introduction to the report on the Royal Commission on Misconduct, was unequivocal in his holding management responsible for misconduct.

*"There can be no doubt that the primary responsibility for misconduct in the financial services industry lies with the entities concerned and those who managed and controlled those entities: their boards and senior management. Nothing that is said in this Report should be understood as diminishing that responsibility. Everything that is said in this Report is to be understood in the light of that one undeniable fact: it is those who engaged in misconduct who are responsible for what they did and for the consequences that followed. Because it is the entities, their boards and senior executives who bear primary responsibility for what has happened, close attention must be given to their culture, their governance and their remuneration practices."*²

¹ 'You can't regulate for culture': next AMP chair David Murray by Clancy Yates, SMH, May 12, 2018
<https://www.smh.com.au/business/banking-and-finance/>

² Final Report, Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry, February 2019, page 4

As an organisation with decades of experience and accumulated wisdom in large scale, organisational behavioural change, we couldn't agree more.

For the financial services industry it's about making a choice

Culture is very often held as distinct from performance, growth and strategy ... the pragmatic, realistic, measurable and distributable outcome of labour and capital. Purpose, values, company pride and qualities such as ethical practice, truthworthiness, responsibility and accountability are commonly dismissed as irrelevant to 'Business'.

However culture and performance cannot be separated. All organisations have a culture. The important question is whether or not it is aligned and directed to accomplishing the performance outcome intended. The challenge for the industry now is to develop organisational culture to achieve past levels of performance AND maintain reputation and credibility and demonstrate trustworthiness ... with neither performance outcomes nor quality cancelling each other out!

There is no evidence supporting the idea that maintaining a culture of high integrity and trustworthiness runs counter to high performance. And it's not especially difficult. Mostly it requires the capacity for leadership to embrace the seeming paradox of customer centricity and organisational profit in a win-win relationship.

Right now, financial organisations have a choice:

1. Do nothing and hope the noise will eventually go away
2. Do enough in enforcing compliance to address recommendations ... take the short term option of what we would call 'Enforced or Monitored Compliance'
3. Take the medium/long term approach of embedding compliance, ethics and performance within the organisation as inseparable in shifting performance and future growth to a new level ... a 'Whole System Compliance'.

Exploring Choice #1 – Do nothing

This has already proved to be wishful thinking and is really no longer an option. Doing nothing will ensure government and other regulatory bodies decide, for the industry, how the compliance will be regulated or whether entities can continue to operate. Alternatively, repeating the same painful (and costly) inquiry again in 10 years time.

"Saying sorry and promising not to do it again has not prevented recurrence."

... The financial services industry is too important to the economy of the nation to allow what has happened in the past to continue or to happen again”³.

Exploring Choice #2 – ‘Enforced Compliance’

The motivation and attitude of ‘Enforced Compliance’ tends to be “I have to do it this way or I’ll get into trouble (or lose incentives)”.

The **benefit** of this approach is that implementation is relatively straightforward, requires minimal time and short term investment and is less disruptive to the organisation. It also avoids some of the more contentious and difficult conversations that have to be had around incentives, the way financial performance is valued over responsible service, the true cost to the business of short term outcomes and continued customer concern when failed compliance issues arise; to name just a few related issues of this approach.

The **cost** of taking this approach is that it requires significant and continued oversight in order to make it work. And that’s almost impossible! There is simply too much going on, day to day, to have oversight over everything and everyone.

Anna Bligh, head of the Australian Banking Association, points to this in a SMH article in January this year.

“A dramatic increase in regulation, which won’t necessarily mean stronger customer protections, can cause inefficiency and duplication ultimately impacting customers through overly complex credit applications and shareholders through reduced returns.”⁴

This is usually where this type of intervention fails because it is not sustainable. New rules that run contrary to, or just overlay usual practice create confusion, frustration or stasis. In facing contradictory, complicated or inconsistent demands people tend to default to previous behaviours and decision-making ... thus old culture remains the default.

It also focusses on pushing compliance down through the organisation with little requirement for leadership to take responsibility for the whole system and how leadership decisions may be creating ongoing ethical and compliance dilemmas. This is an issue that ASIC is particularly interested in addressing, proposing an FSI Disciplinary Panel, a peer review panel, to bring executives to account for oversight.⁵

³ Final Report, Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry, February 2019, page 4

⁴ <https://www.smh.com.au/business/banking-and-finance/tough-for-the...inty-grips-bank-investors-ahead-of-grim-year-20190118-p50s57.html>, Clancy Yeates, SMH, Jan 21, 2019

⁵ Australian Financial Review, ‘ASIC uses ‘peer pressure’ to tackle bad corporate culture’, Misa Han, June 17, 2015

However, because it's not a whole system approach, "it ignores the root causes of conduct, which often lie with the systems, processes and culture cultivated by an entity".⁶

When the oversight is inadequate, behaviours revert to non-compliance through work-arounds, norms, subtle collusion or coercion, which leaves the organisation exposed to potential legal issues and public scandals.

History shows us that this 'forced compliance approach' is open for gaming, has holes and gaps that can be exploited and that attention drifts away from the compliance focus when new challenges or opportunities arise.

Further, amendments in legislation gradually allow gaps and loopholes or water down consequences for non-compliant behaviour. And we're back to square one!

The UK the Banking Standards Board, established in 2013 to address lender misconduct, reported recently to UK Treasury that:

*"Little progress has been made on fixing the UK's poor banking culture, five years on from a major industry inquiry meant to address lender misconduct, the chair of the sector's standards board has admitted."*⁷

Exploring Choice #3 – 'Whole System Compliance'

The difference with 'Whole System Compliance' is, where 'Enforced Compliance' is externally driven by organisational shapers such as KPIs, incentives and formal compliance practices, "Whole System Compliance" is internally driven by people's values and behaviours, supported and reinforced by all the operational elements through which the business achieves outcomes.

*"I believe that the starting point for culture is the systems of the organisations, and the very good design of those systems so that there's clarity of people's role, clarity of their accountability, and that the systems themselves have a process of internal control that allows the executive and the board to see exceptions from expected behaviour."*⁸

The oversight structures of 'Enforced Compliance' are still required and need to be included within 'Whole System Compliance' because people are people and, despite the best of intentions, we sometimes behave in ways that meet our personal and collective emotional and psychological needs rather than our ideals. Concepts about how things should be may well be just that ... ideas that bear little relationship with the way people actually behave.

⁶ Interim Report, Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry, September 2018, page 87

⁷ "Overhaul of UK's poor banking culture is slow, admits standards chair", Kalyeena Makortoff, Guardian, Nov 14 2018; <https://www.theguardian.com/business/2018/nov/13/overhaul-of-uk-poor-banking-culture-is-slow-admits-standards-chair>

⁸ 'You can't regulate for culture': next AMP chair David Murray by Clancy Yeates, SMH, May 12, 2018 <https://www.smh.com.au/business/banking-and-finance/>

Essentially, it takes both the intangible shapers of culture – values, behaviours – and the tangible shapers of the business – structure, systems, processes – to ensure deep and effective change.

Accepting and actively working with that reality facilitates a more easily integrated change effort. The monitoring that occurs within 'Enforced Compliance' also provides evidence that compliance is actually occurring within the system.

The organisation's performance expectation is held within its values and beliefs ... Is the intention to maximise profit, deliver shareholder reward, provide opportunities for individual gain OR is it to do all the above in a way that also protects customers and builds organisational and industry reputation? To settle for the former is tacitly acknowledging a lack of imagination!

Embedding compliance is a whole system approach, something recognised by ASIC as of primary concern. It starts with what is valued by the individuals and the collective. If the organisation does not place a high priority value on operating in an ethical and compliant manner then no amount of oversight will be sufficient to drive compliance. The result will be an 'espoused' set of values and an 'operating or actual' set of values ... and the latter is what the customer will experience.

The **cost** of taking this approach is that it requires more disciplined, focussed time and investment in aligning specific values and business shapers to deliver the required compliance and performance.

The **benefit** of a whole-system approach is that it requires people to examine both the big picture and the detail, the strategy and the execution, the short and long term results, the process and the outcome. It is a development of cognitive capacity that results in a mental habit of deeper, more strategic level of thinking and decision-making that becomes part of the day to day ... not something that happens at an annual offsite.

*"...It's then down to the behaviour of leaders at the board and through the organisation to reinforce those systems. I still believe you can't regulate for culture, but if we're not careful we'll deal with issues that won't drive culture by themselves, rather than dealing with the systems in the organisation."*⁹

In conclusion, whilst whole system compliance may at first sight seem time consuming and potentially overkill, the cost of taking this approach is likely to be far less than the repercussions of a task half done. Customers and society in general will be the final judge.

⁹ 'You can't regulate for culture': next AMP chair David Murray by Clancy Yeates, SMH, May 12, 2018 <https://www.smh.com.au/business/banking-and-finance/>

"Hayne put the onus on firms themselves to clean up cultural problems and determine whether any changes have worked."¹⁰

Can it be done without major cost and disruption?

Decades of practice in shifting organisational culture has proved to us that it can be done both faster and cheaper than feared because this approach coordinates many levers of change at the same time; it harnesses the intelligence and enthusiasm for change within the organisation; and develops the knowledge and skill of those involved.

All it needs is the will to do the job right and to see it through to the end!

Essential to success is the commitment and stamina of those responsible which starts at Board and Executive level. They will set the compass and monitor the progress. A Whole System Approach will not work if this level of organisational responsibility and insight is not fully engaged.

What does this really mean? If Boards, CEOs and Executives start the change with their own attitudes, mindsets, values and commitment to right action, transformation becomes exponentially easier as people fall into line with new expectations and respond to recognition of right action. As David Murray says,

"...It's then down to the behaviour of leaders at the board and through the organisation to reinforce those systems. I still believe you can't regulate for culture, but if we're not careful we'll deal with issues that won't drive culture by themselves, rather than dealing with the systems in the organisation."¹¹

As consultants in this field our experience has shown that real culture change starts with a decision to change, a commitment to taking responsibility and the courage and tenacity to include all and everything in the process.

Who is Culture Navigator?

Dr Christina Kirk

Christina Kirk is a practising culture change and change transformation consultant who has been operating in the field for 25 years, primarily in large, global corporations. Her career includes being a Strategic Change partner in IBM, a Director in PwC Consulting and a

¹⁰ Australia Banks Pay Price for Scandals as Pay, Culture Lambasted, Peter Vercoe, Bloomberg, Feb 4, 2019 <https://www.bloomberg.com/news/articles/2019-02-04/australia-banks-hit-with-tougher-regulation-after-scandals>

¹¹ 'You can't regulate for culture': next AMP chair David Murray by Clancy Yeates, SMH, May 12, 2018 <https://www.smh.com.au/business/banking-and-finance/>

General Manager in Fonterra. She holds a PhD in the delivery of culture change and is co-founder of Culture Navigator.

Gai Roper

Gai Roper is a specialist in working with values and behavioural change at leadership levels that enables culture transformation in large organisations. She holds a MAppSci in Social Ecology, has over 30 years' experience in people and whole-system organisational change and culture transformation, has successfully led organisation-wide leadership development for Australian and global firms and is co-founder of Culture Navigator.

