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Culpable Culture

- regulatory risks and the challenge for Boards

What do we mean by “culture” & why are regulators interested?

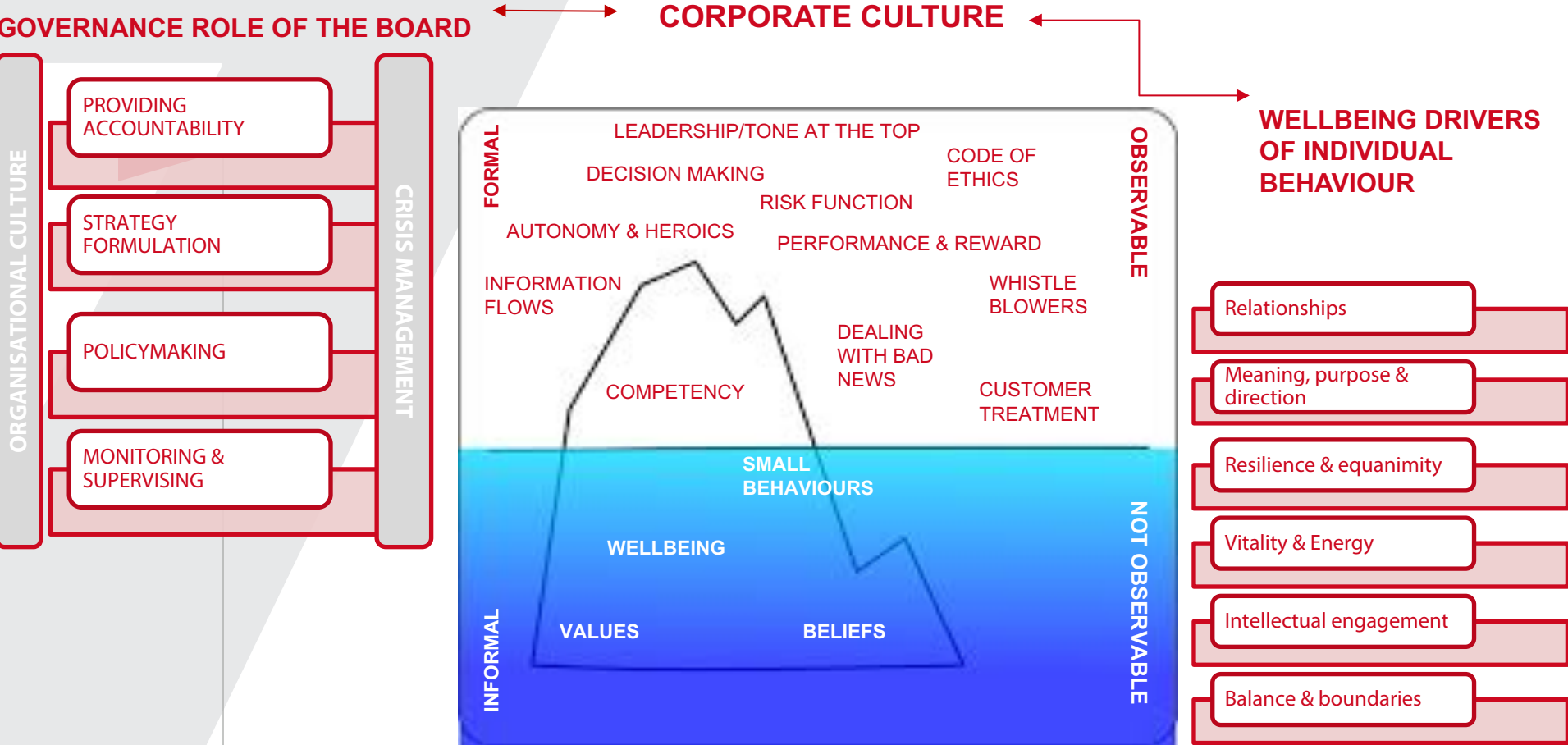
Source	Term	Definition	Key culture message
Commonwealth Criminal Code	Corporate Culture	An attitude, policy, rule, course of conduct or practice existing within the body corporate generally or in the part of the body corporate in which the relevant activities take place.	Attitudes & behaviours or behavioural artefacts
O’Reilly VA and Chatman JA –Culture as Social Control: Corporations, Culture & Commitment – Organisational Behaviour 1996 Vol 18, pp 157-200	Organisational Culture	A system of shared values (that define what is important) and norms that define appropriate attitudes and behaviours for organisational members (how to feel and behave).	Attitudes & behaviours
ASIC	Culture	A set of shared values and assumptions that reflect the mindset of the organisation and influence the way staff conduct themselves on a daily basis.	Mindset & conduct
Institute of International Finance –Reform in the Financial Services Industry: Strengthening Practices for a more Stable System, 2009	Risk Culture	Norms and traditions of behaviour of individuals and of groups within an organisation that determines the way in which they identify, understand, discuss, and act on the risks the organisation confronts and the risks it takes.	Behavioural norms
APRA	Risk Culture	The impact of organisational culture on risk management (the way the organisation takes & manages risk).	Attitudes & behaviours
ACCC	Compliance Culture	A company with a culture of compliance is one in which a dominant value from top to bottom favours activities which support compliance with laws.	Behavioural norms

Companies behaving badly[^]

	Behaviour	Observable Drivers	Accountability	Worker or Customer experience
	Bullying & shaming Punishment rituals Obscene acts	Sham-contracting model? Gross under-payment	\$85m class action Customer losses Independent reviews Individual: Fear & intimidation?	Worker: fear & humiliation/ not belonging Customer: reputation
	Secret affair Credit card abuse	Conduct Code violations Concealing problems	Fair Work Claim Human Rights Commission Complaint Headline Publicity Individual: Unequal position/ squeaky wheel?	Worker: not belonging/ termination Customer: reputation
	Heroics Over confidence Sex, drugs & excess Profanity & bullying Credit card abuse	Remuneration & incentive structure Virtual autonomy Permitted risk taking/ risk management Conflicts of interest	Wrongful dismissal claims Parliamentary Committee Hearing (Senior Manager Regime) Individual: Collateral damage?	Worker: not belonging/ termination Customer: loss of trust in bank(s)

[^] Analysis based on publicly available information including media reports.

Key 'accountability' theme & some 'behavioural' indicators

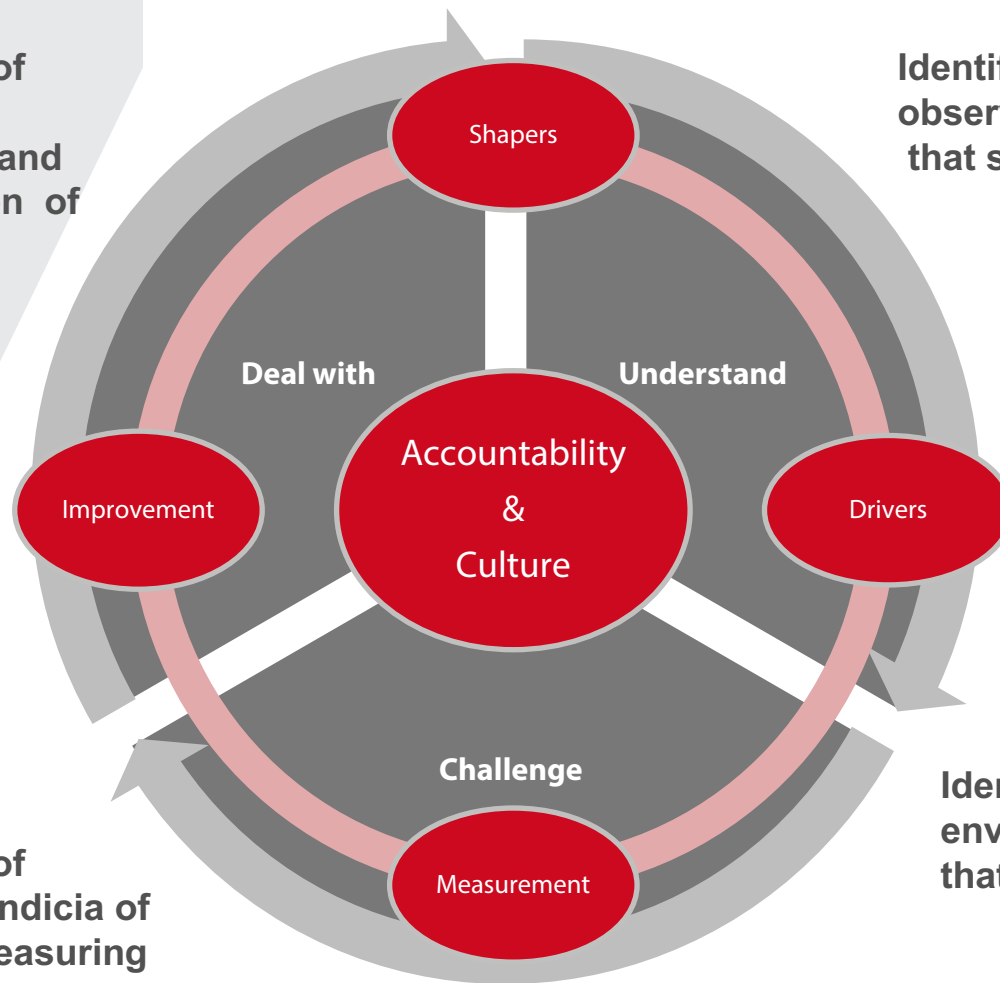


Sources – B. Tricker, Corporate Governance Principles, Policies & Practices, 2nd Ed. 2012, Oxford Press & MEWS Wellbeing Survey (Diagram – Sector Seven)

Board challenges –diagnosing and oversighting culture

Identification of improvement opportunities and implementation of improvement action plans

Identification of non-observable root causes that shape culture



Identification of measurable indicia of culture and measuring culture

Identification of environmental factors that drive culture



REFERENCE MATERIAL

Corporate criminal liability for culture

Commonwealth Criminal Code 1995[^]

- Defines “corporate culture” as an attitude, policy, rule, course of conduct or practice existing within the body corporate generally or in the part of the body corporate in which the relevant activities take place.
- Corporate culpability applies where an employee commits an offence at law^{^^} in circumstances where it is proved that the body corporate “*expressly, tacitly, or impliedly **authorised or permitted** the commission of the offence*” and may be established by, among other things proving that-
 - the Board “*expressly, tacitly, or impliedly authorised or permitted the commission of the offence*” or
 - that a **corporate culture** existed “*that directed, encouraged, tolerated or led to non-compliance with [the provision]*” or
 - that the Board “*failed to create and maintain a **corporate culture** that required compliance with [the provision]*”

[^] Part 2.5-Corporate Criminal Responsibility, Division 12

^{^^} The offence must have a fault element other than negligence (intention, knowledge or recklessness)

ASIC's 7 key indicators of culture & guidance for boards

7x key culture indicators

1

Tone from the top

2

Cascading to the rest of the organisation

3

Translating into business practices

4

Accountability

5

Effective communication & challenge

6

Recruitment, training and rewards

7

Governance and controls

Guidance for Boards

1. Has the culture of the organisation been independently **assessed**? What were the results of that assessment?
2. Do the firms stated values match the actual **experiences** of customers, employees and suppliers?
3. Is culture a regular feature on the Board/Audit & Risk Committee **agenda**?
4. Does the Board hear from key employees such as business line managers, to help obtain **insights** into the corporate culture, sub-cultures and team specific issues?
5. Is there Board **engagement** with external stakeholders such as customers, suppliers and regulators?
6. Is there **monitoring** that captures data or key indicia, gathered through employee feedback and surveys, customer complaints, progress on employee training or culture issues and using data analytics to gain insights?
7. Is the information in internal and external **audits** being fully utilised?

ENABLES

Good corporate culture.

Seven culture questions boards should ask

1. 'Do you know the organisation's values?'
2. 'Does the leadership team walk the talk on those values?'
3. 'Have you been bullied or sexually harassed at work?'
4. 'Would you be confident about raising an issue of poor staff treatment after observing an act of bullying or sexual harassment?'
5. Are you led by managers whom you respect?'
6. 'Do leaders demonstrate respect for you and your work colleagues?'
7. 'Would you recommend employment in this firm to a close colleague or friend? (that is, a Cultural Net Promoter Score)'

An academic framework for measuring culture

Corporate Culture = the set of processes in an organisation that affect the total motivation of its people.

Proven correlation = high performing culture and customer satisfaction.

Theory = why people work is the key driver of how well they work. Answering 3 questions can help transform culture from mystery to science:

1. How does culture drive performance?
2. What is culture worth?
3. What processes in an organisation affect culture?

3 key indicators[^] for positive performance (direct motivators)

1. **Play** (work because you enjoy it/motivated by the work itself)
2. **Purpose** (the direct outcome of the work fits your identity/ motivated by valuing the work's impact)
3. **Potential** (the outcome of the work benefits your identity/ enhances your potential)

3 key indicators of poor performance (indirect motivators)

1. **Emotional pressure** (decision to work addresses external factor that threatens your identity/ motive is separate from the work)
2. **Economic pressure** (working to gain a reward/avoid a punishment & motive is separate from the work & your identity)
3. **Inertia** (motive so removed from the work/your identity that you cannot identify why you are working)

A regulator framework for measuring culture

- Based on the experience of the central bank of the Netherlands (De Nederlandsche Bank - DNB) since 2010.
- Although a model for regulators this approach is readily adaptable by Boards for internal measurement of culture.
- Treats behaviour and culture as **non-financial risks** to be covered by supervision.
- Takes the context for culture measurement as **risk management**.
- Analyses culture against the backdrop of a **key strategic decision taken** by the company.
- Measures behavioural and cultural risks relating to **4 topics or areas**:
 - Decision-making
 - Leadership
 - Communication
 - Group dynamics
- **Measurement** identifies the risks (qualitative & quantitative mechanisms such as surveys and interviews), assesses the risks (determines which behaviours are on a group or organisational level rather than an individual level by extracting recurring behaviours), and targets risk mitigation (to reduce or solve the risk).
- Resulting **Board action** is focused directly on the culture 'hot spots' using challenging dialogue (so in the case of an ANZ for example the Board would speak directly to the trading room).

Challenges & actions for boards

The business of the company is to be managed by or under the direction of its directors (replaceable rule section 198A(1) Corporations Act)

CHALLENGES

- Not diagnosing and fixing **root causes** (for example through wellbeing programs, or through ethics training –teach people to answer how ought I to act).
- Not **understanding** where the hotspots are (the worst cultures are often well away from Head Office for instance ANZ dealers in Sydney and New York who were autonomous and had sales incentives that encouraged ‘whatever it takes’).
- Treatment of whistle-blowers.
- Absence of courage or authority to tackle the most sacred ‘barbarians’.
- Flicking the job of corporate culture to the CHRO and the job of risk culture to the CRO –culture is a joint and several role with the Board and CEO, and/or ‘hierarchy-hugging’ CHRO’s and CRO’s.

ACTIONS

- Maintain a longer-term focus (as opposed to short-term).
- Approve appropriate remuneration and incentive structures.
- Approve and monitor a Risk Appetite Statement that sets appropriate boundaries for risk taking.
- Foster a Board/CEO relationship of ‘no surprises’.
- Ensure the Board has a sound understanding of the company including information about the challenges that managers have in operating the business.
- Access a wider group of managers/management information.
- Take a regular measure of the culture gap and deal with the findings.