Corporate culture and corporate regulation

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CHECK AGAINST DELIVERY

Introduction

Thank you for inviting me to be a part of the seminar today. As you know, I've been talking a lot about culture recently.

One of ASIC's key priorities is promoting investor and financial consumer trust and confidence. Trust and confidence is critical to the operation of the financial system. Poor culture can undermine that trust and confidence.

So, today, I'd like to start by addressing some fairly fundamental questions – what is corporate culture, and why does it matter?

Secondly, I would like to talk about what a good corporate culture looks like and who is responsible for it.

And, finally, I want to talk about what we can do to improve poor culture.

What is culture and why does it matter?

We tend to describe culture as 'the mindset of an organisation'. The Criminal Code sets this out well, saying corporate culture is an attitude, policy, rule, course of conduct or practice.

Culture matters to firms because good culture is good for business. There are a number of ways that having a good culture can benefit the firm itself. For example:

- increasing customer loyalty, brand and reputation
- reducing or avoiding the financial impact of fines or remediation, and

- attracting and retaining staff.

But why does ASIC care about culture?

Culture matters to ASIC because poor culture can be a driver of poor conduct. Culture has been at the root of some of the worst misconduct we've seen in the financial sector. Looking at cultural problems can give us an early warning of where things might be going wrong to help us disrupt bad behaviour before it happens and catch misconduct early. Importantly, it helps with identifying not just individual instances of misconduct but broader, more pervasive, problems.

We think improved culture in the industry we regulate will have a long-lasting positive impact on the industry in a broader way than deterring or disrupting isolated misconduct. And we hope that cultural change will reduce the need for regulatory intervention.

However, we see cultural change not as a panacea, but certainly as something that will contribute to enhancing consumer outcomes.

What does 'good' corporate culture look like?

We think good culture puts customers first and leads to trust and confidence in the financial system.

When we talk to firms about their conduct risk – of which culture is an important component – we have a 'three Cs' message. These are the hallmarks of a good culture:

- effective *communication*
- encouraging *challenge*, and
- guarding against *complacency*.

Starting from the top, organisations need to set the right tone, and then ensure that it is effectively communicated. That means making expectations about conduct and values clear and consistent; and proactively reiterating them across all levels of the organisation.

By challenge, I mean that organisations need to challenge existing practices, and also to foster an environment where employees are encouraged to raise concerns and are rewarded for speaking up.

And finally, there is a danger in complacency. By this, I mean thinking that it hasn't happened yet so it won't happen, or thinking once about conduct and culture and then ticking that box as 'done'.

But we, as the regulator, won't be looking over everyone's shoulder to test their culture. We won't dictate how a business is run. We encourage firms to take action to address culture themselves.

Addressing poor culture

What we will do through our surveillance is to look at culture to help us to identify systemic conduct and behavioural issues leading to poor consumer outcomes.

We will be looking out for cultural indicators, like policies not lining up with what people say and do, or a lack of action when things go wrong, that suggest we should take a deeper dive to look for poor conduct.

This might mean a more intensive surveillance or a broadening of the scope of our surveillance.

Where we identify poor culture, we will make this clear to the firms in which we see it.

Beyond surveillance, we are looking at all the tools available to us to help address poor culture resulting in misconduct.

But going beyond where we currently are, there are possibilities in how we can seek to improve culture within firms. These are through:

- peer review
- whistleblowers, and
- individual and corporate accountability.

Peer review

A good way to shape culture is through peer pressure.

One option that uses the power of peer pressure is a co-regulatory solution, such as a financial services industry disciplinary panel. Similar to the Markets Disciplinary Panel, it could issue infringement notices to deal with civil breaches. This would be an independent peer panel, made up of respected industry experts assessing the conduct of their peers. The significance of this cannot be underestimated. Being judged by peers has major reputational consequences above and beyond any monetary impact.

Whistleblowers

We know that whistleblowers play a key role in preventing and detecting corporate wrongdoing. The importance of whistleblowing was raised in the Senate inquiry into the performance of ASIC.

Effective internal whistleblower policies are important in ensuring the right culture. Whistleblower reports to management can provide firms with important information that help identify where there are problem areas that undermine the firm's culture.

Whistleblowing to the regulator is also critical. In our submissions to the Senate inquiry, ASIC raised the need to expand the definition of 'whistleblower' and the kinds of information that will trigger the whistleblower protections.

Another big issue for whistleblowers is having the confidence to come forward in the face of potential loss of employment and income. In recognising the important role of whistleblowers, we need to make sure they will not be deterred by the potential impact of their disclosures on their personal financial circumstances.

Individual and corporate accountability

To drive cultural change, individuals in companies need to be responsible for the company's culture and actions.

I believe that those who create or encourage a culture that breeds misconduct should be held accountable for it.

In the United Kingdom, the Senior Managers Regime has recently been developed to hold individual managers accountable for poor conduct occurring in businesses for which they are responsible. The regime involves firms mapping out responsibilities for senior managers and having them pre-approved by regulators. Firms will also need to identify staff who could pose a risk of significant harm and assess their fitness and propriety.

While I do believe that holding senior managers and key staff accountable is important to culture, I don't think we want, or need, to micromanage in the way the UK regime does.

As I'm sure you are aware, the Financial System Inquiry recommended ASIC be given a power to ban certain individuals from managing financial firms, in large part as a way to 'remove individuals involved in managing a firm that may have a culture of non-compliance'. The Government has decided it will develop legislation to give ASIC this power. I am keen to see the banning power implemented in a way that helps remove people from the industry where they have been responsible for poor culture.

While further law reform in this area is a matter for the Government, another area I mentioned some months back that could be considered is civil penalties for individuals and companies where they enable a poor culture that leads to breaches of the law by employees.

In this context, is interesting to note the model in the United Kingdom in relation to bribery. The UK *Bribery Act 2010* creates a corporate offence for failure to prevent bribery, with a defence available to the company where it can establish they have adequate procedures in place to prevent the breach.

A deemed 'poor culture provision', if implemented, could hold the manager or firm accountable for an employee's unlawful conduct, unless the firm or manager could show that it had adequate procedures in place to prevent the conduct.

Conclusion

Of course, there are no simple answers. And at the end of the day, as I have emphasised, law reform is a matter for the Government.

But I am committed to the principle of individuals and companies taking responsibility for their culture.

Culture is important to us as regulators because it drives conduct.

But it should be more important to companies, because trust and confidence in financial institutions themselves – and the financial system as a whole – is critical to all of us.