



ASIC

Australian Securities & Investments Commission

The importance of corporate culture in improving governance and compliance

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CHECK AGAINST DELIVERY

Introduction

Good morning everyone.

Thank you for inviting me to speak at your offsite about the importance of corporate culture in improving governance and compliance.

Good governance is one of the core elements of a positive organisational culture, and as I will talk about today, ASIC sees organisational culture as a significant driver of conduct within firms.

Today I'd like to you talk about three things:

- first, what is culture and why it matters
- second, the key drivers of culture, and
- third, the role of governance in ensuring that these are implemented in practice.

What is culture and why does it matter?

So, what is culture? Culture is a set of shared values and assumptions within an organisation. It reflects the underlying 'mindset of an organisation', the 'unwritten rules'

for how things really work. It works silently in the background to direct how an organisation and its staff think, make decisions and actually behave.

Because culture lies at the heart of how an organisation and its staff think and behave, in a financial services firm it is an important driver of outcomes for investors and financial consumers.

Culture matters to ASIC because poor culture can be a driver of poor conduct – and we regulate conduct. Bad conduct can flourish, proliferate and may even be rewarded in a poor culture. A good culture, on the other hand, can help uncover and inhibit bad conduct and reward and encourage good conduct.

In terms of what ASIC will do, where we identify poor culture we will make this clear to the regulated firms in which we see it. In particular, we think it is important to share this information with directors of regulated entities, given their role in guiding and monitoring the management of the company.

However, it is not only regulators who should care about culture. Companies should also be interested in culture because many studies have found that good culture is good for business and generating long-term shareholder value.

There are a number of ways that having a good culture can benefit your organisation – for example:

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

Poor culture, on the other hand, can lead to misconduct and result in significant financial costs – including the cost of remediation, compensation and fines – as well as not necessarily attracting and retaining staff.

Drivers of a positive culture

I'd like to move on now to talk about the drivers of a positive culture. By monitoring drivers that measure and shape culture, you can obtain insights into how your culture is aligned with your organisational values. As I talk through these drivers, you will see that good governance is important across the implementation of these drivers.

I want to emphasise we are not advocating a 'one size fits all' approach on firm culture. There is no 'correct' culture that will be right for every organisation. We understand that every organisation is unique and will therefore need to tailor what I'm going to speak about to the nature, scope, size, and complexity of its business as well as to its own organisational values.

Tone from the top

The first driver is tone from the top. The board and senior management are responsible for creating a culture where everyone has ownership and responsibility for ‘doing the right thing’ and ensuring ‘good outcomes for customers’.

The board should set the values and principles of a firm’s culture. These should be reflected in the business’s strategy, business model and risk appetite. The leadership team should then lead by example by demonstrating the conduct that supports the firm’s values. In other words, they should not only talk the talk, they should also walk the walk. For example, directors and senior executives can consider taking the Banking and Finance Oath and offering ethics training for staff or e-learning modules on their code of conduct.

Putting the right governance structures in place around board engagement with culture can ensure that the tone from the top is implemented in an effective way. For example, boards may wish to consider the following questions to help gain insights into their firm’s culture:

- Is culture a regular feature on the board and audit committee agenda?
- Is there a board dashboard report that gives updates on key cultural indicators of values alignment?
- How do they gather insights about sub-cultures, for example through pulse survey reports of staff views on values alignment?
- Is there periodic engagement with all stakeholders to get a broad perspective on how well values are aligned with customers, suppliers, regulators, and the community?

Accountability

The second driver is accountability. The accountability of staff is extremely important. All staff should understand the firm’s core values and, most importantly, that they will be rewarded or held to account for their conduct in relation to such values.

As such, the leadership team need to make sure the values are understood throughout the organisation. This is important because, quite often, the message gets lost in the middle and does not make its way to the front line.

Evidence shows that organisational culture exists primarily at the individual business unit level. We know that employees are more likely to be influenced by the conduct of their direct managers and/or the top performer in their unit than they are by the board and other senior leaders. It is important that the middle and front line managers model the firm’s values. This is because new staff and junior staff members often interpret rules based on what they have learned as acceptable conduct from their managers and colleagues.

If new staff see that the top performers are successful despite, or even because of, poor conduct, then messages from the board about the importance of the firm’s values and good conduct will not be effective in changing behaviour or aligning conduct with those values.

Leaders need to ensure that firm values are understood throughout the organisation, and are ‘lived’ by employees as part of their day-to-day roles. Measures that touch on accountability might include treatment of whistleblowers, breach or over-limit reports and customer complaints.

Effective communication and challenge

The next driver relates to effective communication and challenge. The firm should promote a culture of open communication and effective challenge to:

- encourage a diversity of views in decision making processes
- allow current practices to be tested
- encourage a positive, critical attitude among employees, and
- promote an environment of open and constructive engagement, so people don’t succumb to groupthink.

Recruitment, training and rewards

The last driver I want to talk about relates to recruitment, training and rewards.

First, this means management should include behaviours and attitudes that align to the firm’s values as part of staff selection. For example, firms might use psychometric testing to ensure potential staff have values aligned to the organisation.

Second, there should also be training to maintain staff knowledge about the firm’s values and the attitudes and behaviours expected of staff – for example e-learning modules might be used.

Third, on rewards, remuneration and incentive structures should be aligned to the values of the firm.

Rewards play a big role in driving conduct for two reasons:

- first, they affect an organisation’s culture because they impact on priorities and staff, and
- second, they act as a motivator and reinforcer of conduct.

So, it is crucial that firms recognise performance in a way that not only promotes good conduct but penalises poor conduct as well.

Rewards can be integrated into the performance management system ensuring that bonuses and promotions are linked to good conduct that is aligned with organisational values.

Governance and controls

So now I want to come back and talk specifically about governance. Practical implementation of these four drivers of positive culture relies on effective governance structures.

The firm's values should be incorporated into all of its business practices and governance structures. For example:

- how business decisions are made, including how new products are approved
- how the firm responds to customer complaints and claims
- how problems and mistakes are identified internally, as well as elevated and fixed
- how staff behave, and
- the consequences for breaches of internal policies, procedures and internal limits.

Translating the firm's core values into business practices and governance structures is important because it ensures there isn't a gap between the firm's desired values and actual conduct.

Under the board's stewardship, the management team should promote, monitor, and assess the impact of the firm's culture on conduct and make changes where necessary.

It is important that staff have direct access to the board and leadership team. It is also important that there is a process in place for periodic reporting to the board on culture and conduct issues.

We see governance structures within an organisation as key drivers of corporate culture, and a positive culture and strong, effective governance structures are mutually supportive.

A good culture will support the governance structures that are in place and ensure that they are working to protect the interests of all stakeholders.

Conversely, a poor culture will result in governance structures being given lip service – but not being a true part of how the business is actually run day to day.

Effective governance structures supported by a good culture can help organisations move beyond minimum standards and 'tick a box' compliance practices to best practice standards and compliance practices that protect stakeholders and are commercially valuable.

Conclusion

I want to conclude by saying that – from my perspective and yours– culture matters.

At the end of the day, you need to have a culture that your customers can believe in. If your culture genuinely reflects 'doing the right thing', this will be rewarded with longevity, customer loyalty and a sustainable business.

Firms with a values-led culture, supported by effective governance processes that can be implemented by front-line staff at the business unit level, are well on the way to having a culture that customers – and the public – can believe in.