



Inspiring Trust: Evolutions in Financial Conduct Regulation

CULTURE, GOVERNANCE AND ACCOUNTABILITY

Date: 13 March 2024

Presenter: Lezanne Botha



AGENDA



- 1. The evolution of market conduct regulation**
- 2. Why the focus on culture?**
- 3. Cultural drivers**
- 4. The link – culture, governance, accountability**
- 5. Collaboration - What are we doing?**



The evolution of market conduct regulation



Issues relating to conduct and culture of increasing importance due to –

- *rapidly changing financial markets driven by innovation*
- *shifts in consumer expectations*
- *and broader societal challenges.*

What was?

- Silo focus
- Reactive
- Box-ticking
- Ritualistic
- Adversarial
- Non-strategic
- Backwardlooking
- Rules based

What is?

- Pre-emptive
- proactive
- Forwardlooking
- Intensive
- Intrusive
- Collaborative
- Risk-based
- Outcomes focused
- Comprehensive
- Operational and business model focused
- Align with international standards

The Evolution

- Move from **talking** about TCF outcomes to **proactive management** of market conduct / conduct of business risks



Why the focus on



- **Effective culture is pivotal to strengthening and maintaining public trust and confidence in the financial sector.**
- **Vital to understand key components of corporate culture - these can significantly influence the achievement of various outcomes for financial institutions, customers and other stakeholders.**



Why the focus on culture?

Financial institutions must embed a culture that consistently promotes sound prudential and conduct outcomes

Regulators must assess effectiveness of financial institution's culture in actually delivering on these outcomes

- Is your culture:
- sustainable
- healthy
- purposeful
- safe?

CULTURE

describes the collective principles, philosophies, goals and standards as well basic assumptions that influence decisions, actions and behaviour of members of the organisation

Each culture is *unique*

- No 'right' or 'good' culture

Are you "effective" or "ineffective" in delivering on outcomes



Managing culture not a one-off event.

It needs ongoing reinforcement to yield permanent and meaningful outcomes

Does the culture of your financial institution effectively promote positive outcomes related to –

- its overall safety and soundness,**
- the interests of its financial customers and other stakeholders,**
- and**
- the fair treatment of customers?**

Cultural Drivers



Many of the incidences of misconduct that emerged during and since the [global financial] crisis reflected, at their core, significant deficiencies in organisational culture, demonstrated through poor governance, remuneration and risk management frameworks, often driven by an unhealthy “tone at the top”.

- *Andrew Bailey (Chief Executive Officer, PRA), Culture in financial services – a regulator’s perspective, May 2016*

Institutions faced with conduct issues or scandals do not necessarily have a bad culture overall - elements of their culture are misaligned with the outcomes sought by these institutions and these drive undesirable or inappropriate behaviour. The delivery mechanism may work, for example, but the values or behaviours fail at one or more critical points, such as middle management.

- - *G30 Steering Committee and Working Group on Banking Conduct and Culture, A Permanent Mindset Change, November 2018*



Financial Conduct Authority has described culture as the habitual behaviours and mind-sets that characterise an organisation, its key drivers being the organisation’s leadership, purpose, governance and approach to managing and rewarding people.

- *FCA UK Transforming Culture in Financial Services Discussion Paper DP 18/2, March 2018*



What are the various drivers of culture, conduct and decision-making?



What is the "unspoken" culture when looking at the organisation holistically?



LEADERSHIP, TONE AND DRIVE

- Values, objectives, strategies, purpose
- Leadership accountability

RISK AWARENESS AND INTEGRATION

- Regulatory knowledge and clarity
- Awareness of social impact
- Transparent internal communication
- Diversity, Equity and Inclusion

INCENTIVES AND PENALTIES

- Appropriate remuneration and performance structures
- Effective consequence management for misconduct

The link - culture, governance & accountability

Effective culture can help, prevent excessive risk-taking leading to more prudent and fair outcomes generally.

Ineffective culture can serve as stimulant for risky behaviour that leads to adverse outcomes - for the financial institution, financial customers, but more broadly for the financial system as a whole

Financial institution led by a Board that demonstrates ethical and transparent decision-making (culture) can help reinforce the implementation of strong governance, risk management and internal control systems (prudential) resulting in lowered instances of unfair business practices and better outcomes for customers (conduct).

Board whose decisions are driven solely by interests of short-term-profit-oriented shareholders (culture) may set aggressive profitability targets (prudential) that could incentivise unfair product design, sales and claims handling practices (conduct), which could lead to large scale consumer complaints, litigation, reputational damage and significant longer-term losses (prudential and conduct).





The link - culture, governance & accountability

Expectation from the Board – promoting and overseeing effective governance and culture

Setting the “Tone from the top”:

- **Oversee the implementation of desired organisational culture at all levels**
- **Streamline board and governance structures to ensure integrated and holistic prioritization and oversight of high impact risks**
- **Empower boards to engage more robust decision making through better quality tracking data and management information - measure delivery of key outcomes**
- **Assess diversity and inclusion of representation, knowledge and skills across board and senior management**
- **Set business objectives and strategies for achieving objectives**
- **Effective oversight of Senior Management**
- **Promote a culture of openness and debate within the Board, with proper involvement of Senior Management and Key Persons in Control Functions**

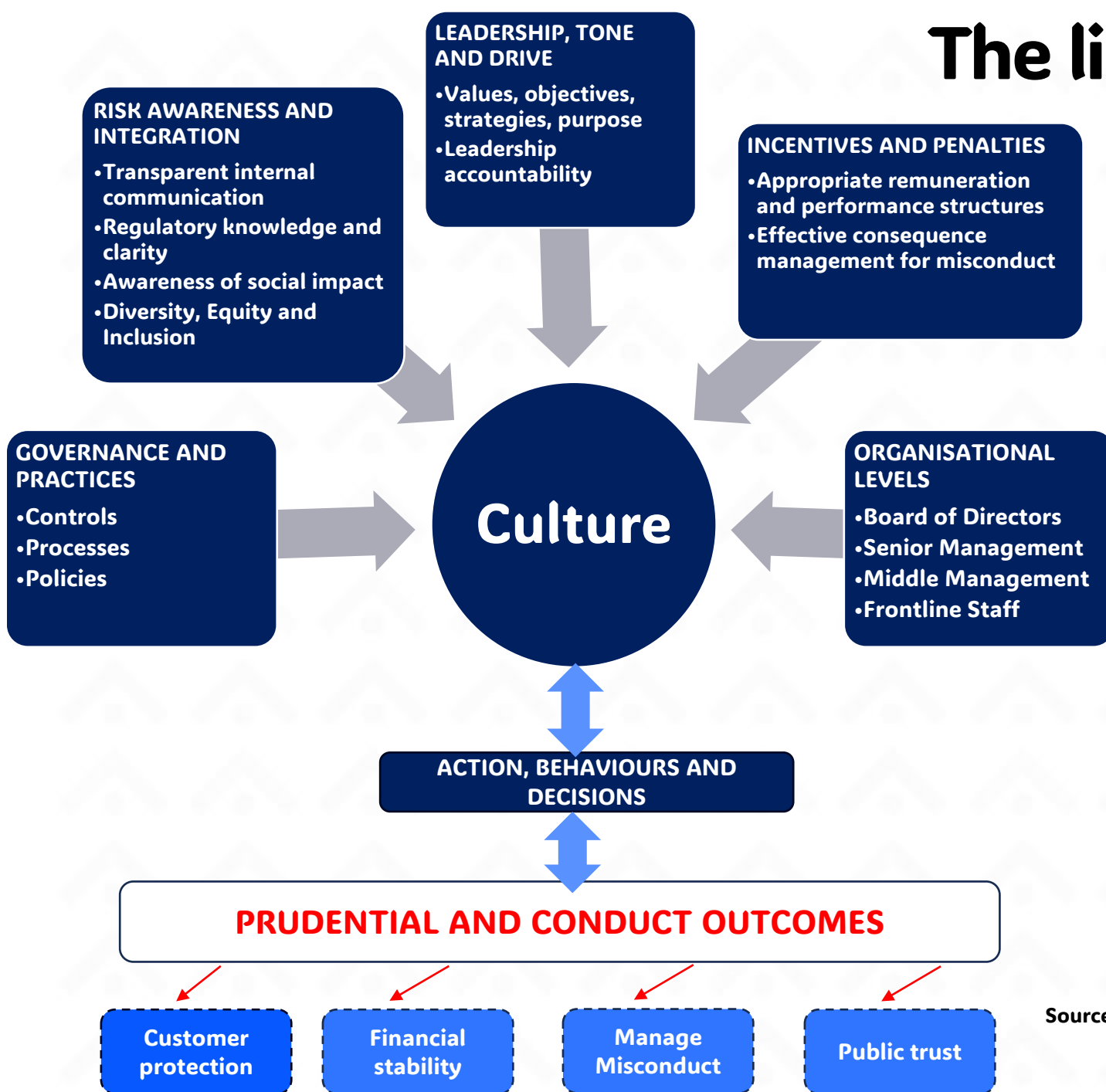
**“Mood in the middle”
Senior Management responsibility:**

- **Promoting sound risk management, compliance and fair treatment of customers**
- **Implementation of governance arrangements**

“Echo from below”:

- **Decision-making and behaviours at the middle and lower levels - critical to evaluating how deeply embedded the cultural tone is**
- **Positive tone at the top, including promoting a sound culture of openness and debate at all levels - help set norms for responsible and ethical behaviour down through middle management and front-line employees**

The link- culture, governance accountability



Source: Adapted from IAIS Issues paper on Insurer Culture (November 2021)

Collaboration - What are we doing from a supervisory perspective?



FUNDAMENTAL CHANGE IN SUPERVISORY APPROACH

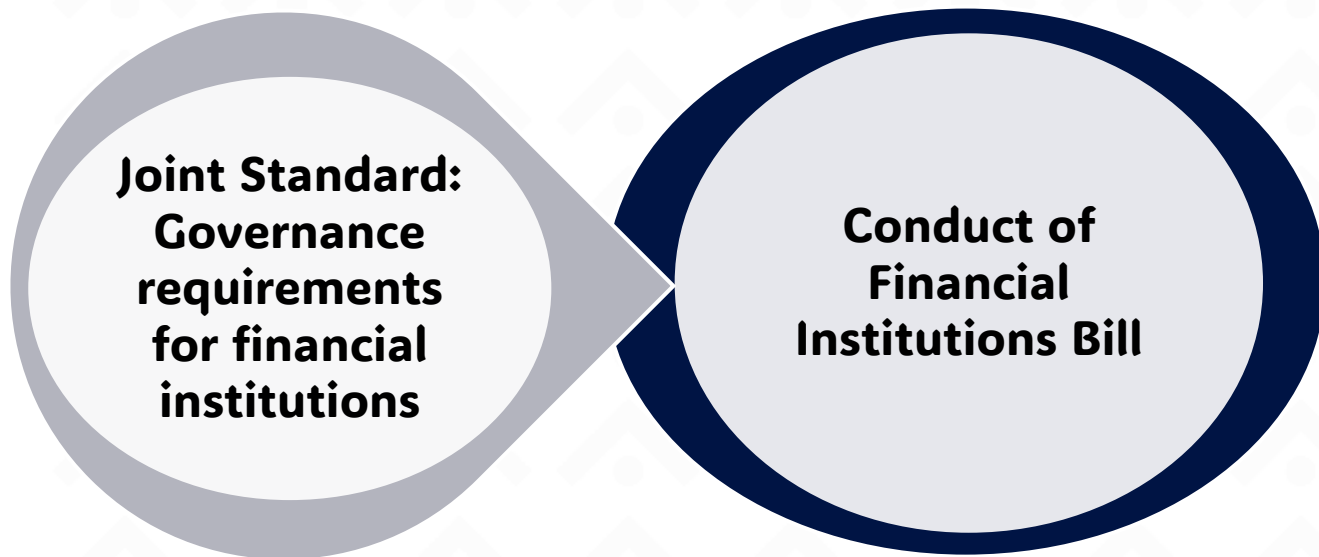
- Financial institutions must be able to demonstrate a solid leadership and cultural commitment to embedding principles relating to both sound prudential management and the fair treatment of customers across all aspects of their business
- Goal is to demonstrate whether the organisation is achieving the outcomes rather than prescribing how.

PROMOTE AN OUTCOME DRIVEN CULTURE -

- Ask yourself - is the failure to deliver an outcome rooted in cultural, operational or procedural factors?
- Rules may be introduced where there are significant inconsistencies in delivering outcomes, clear interpretational differences or irreconcilable expectations



Collaboration - What are we doing from a regulatory perspective?



• Cross cutting, principle based, focused on good governance outcomes, aligns with King Code

- Culture, leadership, and ethics
- Governance framework requirements
- Governance of the 'four lines of defense'
- Conflict of interest management;
- Principles relating to the use of technology, information, artificial intelligence, and machine learning by financial institutions;
- Remuneration and incentives

- Enhanced focus on Business Principles, Culture and Governance
- Accountability of governing body, oversight over governance arrangements
- Governance arrangements promote accountability of key persons and address roles, responsibilities and duties of the governing body



THANK YOU

