

## **Firm culture in financial services.**

Having worked with many different organisations, I have some experience about the different cultures that are operative in IFA firms and networks and larger institutions. The differences can be quite illuminating.

In preparation for this article, I did a little bit of research to back up my own experiences and perhaps explain why certain cultures prevail.

Culture in financial services is widely accepted as a key root cause of the major conduct failings that have occurred within the industry in recent history. Given its impact, firms' culture is a priority for the FCA. The FCA expects firms to foster cultures which support the spirit of regulation in preventing harm to consumers and markets. These kinds of healthy cultures can also complement and support businesses' financial performance.

The FCA DP18/2 is a collection of 28 essays discussing what a good culture might look like, the role of regulation and regulators, how firms might go beyond incentives, and how to change behaviour for the better.

DP18/2 offers actionable insights for financial services leaders and practitioners to consider how they effect change in their organisations. These include:

- using behavioural science to guide incentives and cultural change
- looking beyond the role of leadership in effecting change
- applying strategic focus to the continuous process for adapting culture
- fostering environments of trust to encourage openness and learning
- applying a systems perspective in assessing both internal culture and external influencers

Common corporate culture models can be summarised as follows.

- Hierarchical - an organisational model based on clearly defined corporate levels and structures.
- Adhocracies - emphasise the ability to adapt quickly to changing conditions.
- Clan cultures - a family-like environment that value consensus and commonality of values and goals.
- Market cultures - corporate environments that emphasize competition.

The FCA recognises that each firm's culture is different, and appropriately so. The FCA does not believe there should be a 'one size fits all' culture and does not prescribe what any firm's culture should be (it never does!). However, it has set out minimum standards of behaviour, in the form of 5 Conduct Rules, which sit at the heart of the Senior Managers and Certification Regime (SM&CR, known as the Accountability Regime). The Accountability Regime currently applies to Banks but there are plans to extend it all regulated firms by the end of 2019.

### **Conduct Rules**

- Rule 1: You must act with integrity.
- Rule 2: You must act with due skill, care and diligence.
- Rule 3: Acting with due skill, etc as a manager.
- Rule 4: You must be open and cooperative with the FCA, the PRA and other regulators.
- Rule 5: You must pay due regard to the interests of customers and treat them fairly.

Personally, I find it sad that these rules need to be set out in regulation; as people should surely be behaving naturally in line with these rules. I guess that has been the problem within financial services over the years that some people do not behave well.

For markets to work and firms to be successful, it is critical that they are seen as trustworthy. Social expectations have changed, and public interest has raised questions of trust in firms, and in the industry as a whole. To increase confidence, firms need to demonstrate they are working in the interests of consumers and the market

So, how can regulation promote healthy culture? Two fundamental concepts underpin FCA thinking about culture and regulation. The first is that regulation has to hold the individual as well as the firm to account. This is why the FCA considers it so important to define the 5 Conduct Rules and have them apply to all financial services individuals in the firm.

The second concept is that leaders can manage culture even if they cannot measure it very well. This is deeply embedded in the Accountability Regime too. The regime aims to hold firms' leadership to account for their own behaviour and for taking reasonable steps to manage the behaviour of those in their areas of responsibility. It also aims to ensure that leaders have clearly articulated what they are accountable for and that key responsibilities neither slip through the cracks nor end up too diffused. It provides a robust framework for a culture of accountability, bringing much needed clarity to the accountability of all individuals and a focus on behaviour that goes beyond simply complying with the rules.

I saw a statement that culture in an organisation is "how people behave when the boss is not looking". The Accountability Regime seeks to enforce this by making individuals accountable for their own actions and also the actions of those people who report to them. The accountability focuses the mind. Although, it is a negative thought that if they were not accountable, they would behave differently.

Organisations do need to be led from the front by their owners or senior staff. Richard Branson once said, "Train people well enough so they can leave, treat them well enough so they don't want to." I did some work with a firm last year that did not run training for their staff because their staff did not stay at the firm very long. They had a high turnover of staff and blamed it on people being offered jobs elsewhere that paid more. Two things there – treat them better and/or pay them more. More people leave jobs because of bad management.

Richard Branson also said, "I have always believed that the way you treat your employees is the way they will treat your customers, and that people flourish when they are praised." Again, this promotes a positive culture that will lead to good customer experiences and lead to good customer outcomes.

The Accountability Regime is the widest ranging attempt by the FCA to lead financial services towards becoming trusted by consumers.

The Retail Distribution Review (RDR) was put into place on 31<sup>st</sup> December 2012. The ultimate goal of RDR was to ensure more transparency in the investment industry; improve services through higher qualifications; and ensure investors understood the true cost of advice and trust they were receiving unbiased information. This had the effect of raising the bar of expertise and qualification of advisers. This should have led to better customer outcomes.

The Insurance Distribution Directive was directed at General Insurers to bring their standards closer to financial advisers by bringing in new training requirements and greater clarity of documentation. Again, to promote good outcomes for customers.

The Markets in Financial Instruments Directive (MiFID) II is a legislative framework instituted by the European Union to regulate financial markets in the bloc and improve protections for investors with the aim of restoring confidence in the industry after the financial crisis exposed weaknesses in the system. This brought the standard of advice throughout Europe in line with the standards in the UK. This also has been directed at providers to review their products to ensure appropriateness and suitability for their target market and ensure clarity of paperwork to improve customer outcomes.

So, having looked at advisers and products, the Accountability Regime is dealing with the structure, duties and responsibilities within firms. It is already in place within the banks and is being rolled out to all firms later this year.

It will be interesting to see how the Accountability Regime will improve customer outcomes. But it probably will have some effect by making people personally responsible and accountable and open to sanction. Time will tell.

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