Running Halsey Keetch
Individual Accountability
The Senior Managers Regime
Measuring Culture
The Evolution of Enterprise Risk
A Life in Audit

IN CONVERSATION

vol. III - 2019

HALSEY KEETCH

EXPERTISE IN FINANCIAL SERVICES GOVERNANCE & CONTROLS SINCE 1988

A warm welcome

We are pleased to present the third edition of our annual publication, In Conversation.

As you may be aware, Halsey Keetch is a specialist executive search and market intelligence firm with a long-standing focus on the governance, regulatory and controls functions, spanning compliance, audit, risk and finance. We also run a busy Board Practice focused on recruiting INEDs for a wide range of financial institutions. After more than three decades in business, we are privileged to be connected with some of the most talented individuals in the industry, whose views and experiences add huge value and interest to our work. Contained within this publication, you will find an edited selection of the conversations that we have had with some highly experienced, well-informed and thoughtful people across our network over the last twelve months.

Without a doubt, the topics of good governance, regulatory risk management, and effective controls, are all subjects of ongoing and energetic discussion across the financial services industry and related sectors. In an era where diversity, inclusion, well-being, transparency, and doing the right thing are becoming ways of life for well-run modern businesses. Previously held truisms are making way for new theories, almost on a daily basis, and the relentless pace of technological innovation is a catalyst for such change. Reflecting some of these issues, we have endeavoured to select some of the most relevant and engaging Q&As from the past year, for your consideration. Topics include the practicalities of the Senior Managers Regime, new frontiers in enterprise risk management, and the implications of increased accountability for the financial services industry.

We wish you good reading, enjoyable and stimulating conversations of your own, and a prosperous and well-governed 2019.

The Halsey Keetch Team, Spring 2019

In Conversation with
Alex & Caroline Keetch

on running a Governance, Regulatory & Controls search firm

Alex and Caroline Keetch are the directors of Halsey Keetch, having taken over and rebranded the business following the passing of the firm's founder, and Caroline's father, Nigel Halsey, in 2015. In this conversation, they share some insights on the origins of the firm, the current state of play, and what the future might hold, with the firm's valued senior adviser and co-head of the firm's Board search practice, Mike Gostick.

Let's talk about the background to your executive search business. Where did the focus on governance, regulatory and controls functions come from?
It's a good place to start, given our focus on these functions underpins our business model. In 1988, when Nigel originally launched, it was an exciting time for the City. The topics of governance and regulation must have been in discussion, but the pursuit of new commercial opportunities was probably taking precedence. 'Big Bang' had taken place a couple of years before, and had opened up the City to new people, new influences and new opportunities, so it would have been an exciting and dynamic time for the financial industry. There were lots of new products being launched, companies merging, and international banking groups coming into London and expanding here in order to gain access to Europe. However, when Black Monday occurred, in October 1987, there followed a huge drop in stock markets and other assets around the world. Investors and financiers got their fingers quite badly burnt in the process, in the same way that the dot-com crash was very painful for those involved a decade or so later on. Among other things, Black Monday must have been a wake-up call for the financial services industry, and particularly for regulators, as far industry regulators went back then, and our company was born into this era of opportunity and turbulence. In the early 1990s, there was the Savings and Loan crisis in the US, and the Barings Bank collapse in the mid-1990s, which had implications both in London and Singapore. These were both

> “We believe a great search firm is able to blend the art of finding the right people, based on intuition, knowledge, experience and human instinct, with the science that only a detailed process and thorough research can provide.”

horrible frauds in themselves, and indicative of huge lapses in controls at supposedly well-run, self-governing firms. The functions in which we specialise commenced their gradual rise in prominence at that point, to where we are today.

And Halsey Consulting, as the firm was then known, caught the regulatory wave from there, would you say?
Well, in the very early days the firm's range was wider, in fact, but risk and regulation quickly became more of a focus as the demand for such people grew across financial services. I (Caroline) was only little back then, but I can remember helping my father move into his first office, unpacking his papers and stationery from cardboard boxes. Nigel spent the very early years of the company working on a fairly wide range of roles. He ran the graduate scheme for an investment bank on an outsourced basis for a while, he recruited accountants for the BBC, and did some commercial work in the investment industry as well. For example, he placed a young Anne Richards as a fund manager in the late 1990s. Anne has gone on to become Chief Investment Officer of Aberdeen Asset Management, and more recently CEO of Fidelity International. As mentioned, though, the notion of increased regulation was creeping up the agenda for all sorts of service providers – consultancies, technology providers, law firms etc. Risk, audit and compliance began to play a big role for us. Nigel's leaning in that direction started with the audit and controls roles. He had started out in the early 1980s as an internal recruiter for Peat Marwick, which is now KPMG, helping the firm to hire partners and directors into various practices. He had gained a solid understanding of the audit space, and also started to develop a senior network amongst the accountancy profession. The next step in the regulatory and governance direction for Halsey Consulting was the formation of specialist regulators like IMRO and the SFA, and their interest in hiring chartered accountants into their ranks, presumably in order to bring some robustness to their processes, and that rigorous audit mindset to the supervision and investigation of regulated businesses. Nigel assisted in placing people into those organisations, and some of the placements made in those days remain amongst our best and most senior contacts in the market to this day. We've been in the risk and regulatory space ever since then.

That must have has played into your hands in the last ten or twelve years, as the dramatic increase in industry regulation and improved governance standards in finance, particularly since the financial crisis, have put these roles in the spotlight, and increased their remit and strategic importance. What key issues do you perceive when it comes to hiring at senior levels in these areas today?
For the last few years, everyone has been looking for the same thing simultaneously, so hiring into these areas has been made most challenging by a good old-fashioned talent shortage. Finding strong and dynamic leaders across these disciplines is a real challenge, and one made harder by continuous supply vs demand issues. The challenge for functions like audit, risk and compliance is that they have been enlarged and upskilled on an industry-wide basis in the last decade, so there have been wars for talent, significant compensation inflation, and generally insufficient supply to cope with such demand. Managing client expectations for firms like ours in those conditions is challenging. At the same time, it has been a positive development for various reasons. For one thing, the enhanced prominence of these functions is generally a good thing, and points towards a safer and better governed financial services industry. We'll never patch every hole in the boat, but it's fair to suspect that a lot of wrongdoing and a lot of mistakes will be avoided in future, thanks to stronger, more independent compliance, risk and audit functions across the industry. Another positive is the cross-pollination you have seen from other departments. Lots of lawyers, ex-business people, former accountants and others have migrated into functions like compliance and risk, adding real depth and substance to both the talent pool and the quality of leadership in these areas.

Yes, I certainly saw quite a bit of such movement during my time in HR. My sense is still that there still aren't enough people in the governance functions to go around.
Well this is certainly true at the most senior levels. Investment in people, and the development of leadership in these areas is on the rise, but it takes time to develop leadership-level talent in what have typically been heavily technical roles. Regulation is ultra-heavy already, increasing, and continually changing. The industry keeps evolving too, so firms need a lot of expertise and hands on deck to keep up and maintain control. An obvious point to make in this regard is on the rise of regulatory technology, or Reg Tech, which is a super hot area for investment and innovation, but for the foreseeable future, there is only so far that can go. The real modern issue in governance, controls and regulation is leadership. The concept of leadership comes up in almost every client conversation we have, and it is a problem to be solved in almost every search that we run.

Can you expand on that a bit?
From what we can see from all our work at the senior hiring levels, these functions now need to be led, managed and developed by really high-quality, inspiring people with the ability to set the agenda, influence those around them positively, develop the next generation, and cement the importance of good governance and controls in the administration of the industry, for the good of society as a whole. It's no mean feat and these are high-pressured roles. For obvious reasons, therefore, the industry is dealing with a supply problem in this regard.

And in this disintermediated age, where does a search firm add value to a senior recruitment process nowadays?
The quickest answer to that question directly

relates to the previous answer. Where there is a genuine talent shortage at senior-levels in a certain function, a specialist search firm can provide a client organisation with a real edge when it comes to identifying and hiring the best people. A search firm's reason for being is to find, engage, and then secure people the best people, where a non-retained or direct recruitment exercise might fall short. A specialist firm such as ours understands the environment in which we operate. We understand, and know, the people we interact with. We know what good looks like, and we understand the challenges that organisations might face when it comes to attracting the best people. Where we are able to truly partner with our client, discuss these issues and advise accordingly, we are able to provide a true competitive advantage to that firm. Regardless, the management of expectations is always key – and some clients are more open to the reality of the talent market than others. Additionally, senior-level talent, even though often committed to their current roles, still remain ambitious and want to know what their options are, and what a sensible or exciting next career move might look like for themselves. It's easy to think that accomplished and driven people already have all of this figured out, but the fact is, they are often too preoccupied by the content of their current roles to dedicate much thinking time to their next moves. Coming into contact with the search industry allows for a pause, some time to reflect, and an opportunity to bounce ideas around. That's especially relevant in the non-linear careers world of today, and it's also relevant where someone actively wants a change, or where a potential employer wants a person with a bit of a different background for a particular role. Our network know that they can get in touch with us and have an open discussion about their options, based on our understanding of their specialist areas.

And in terms of actually doing the work, how do you create that advantage for your clients? How do you achieve those results?
We believe a great search firm is able to blend the art of finding the right people, based on intuition, knowledge, experience and human instinct, with the science that only a detailed process and through research can provide. Our attitude towards our methodology is traditional but incredibly robust. Despite the fact we live in a highly technological age, we believe in the value of human connection when it comes to our work. We invest in a lot of facetime with our clients and candidates and we encourage our clients to invest in that time with us too. This enables us to have continually open discussions around processes, and to overcome obstacles effectively with those we are working with, albeit driven by the underlying agenda of filling a given role. Transparent reporting is a key factor for us too. We provide detailed longlists, market insights and intelligence, and incredibly thorough candidate reports on every search that we handle. Our goal is for our clients to have full-view of the search process from start to finish, and to develop a real understanding of the market in which they are hiring as part of the exercise. This enables people to truly understand why they are hiring one individual over another.

And amongst search firms in the market, does HK have a clear differentiating factor that you trade off?
Most definitely. Without disparaging any of the other outstanding search firms out there, our longstanding focus on governance functions has consistently given us an edge in the processes we run. In our experience to date, it is one of the key reasons why our clients work with us - our understanding is naturally focussed and more detailed than a generalist firm, and our network amongst what is a fairly close-knit community is particularly well-developed. Risk, compliance and audit are continuing to develop as disciplines as well, and we are right on top of that in terms of subject matter expertise, best practices, what strong leaders look like and so on. The other key advantage that we have is that we are owner-managed, We strike an effective balance between winning the work by having our clients place their trust in us, personally, and doing the work, in that our presence and input through the introduction and hiring process is truly value-adding to clients. Plus we love doing what we do - we're hugely motivated by the mission of preserving and adding to our firm's legacy, and supporting the strengthening and increased resilience of the financial services industry.

How should your clients expect to work with you? What do you ask of them?
Whilst the onus is obviously on us to get the job done for our clients, the success of a search exercise depends hugely on the relationship we are able to strike with the stakeholders of the search. Of course we can map the market, meet people, sell a role and bring people to the table, but we also need to be able to work closely and openly with clients in order to manage the search successfully post the shortlisting stage. It is not easy to hire leaders in the governance and controls functions so joining all the dots within an organisation is key – it is important that everyone involved is aligned when it comes to the reason for the hire, and the profile and impact of the person required. Crucially, we must be able to talk openly and honestly with clients at every step of the way in order to navigate any obstacles that may occur. On a more process-focused point, it is important that a good degree of momentum is maintained once candidates are introduced to a client. These hires can take time, of course, but allowing a search to take months due to internal diary management or lack of communication around changing plans can damage the integrity of a shortlist, and the engagement of those on it. Ultimately, the search business is a people business, through and through. We are only successful if we treat everyone we interact with respectfully and stay in close contact with those we are working with and for. We ask for the same back in return.

How do you see the future for the search industry, and your business in particular?
Well, like any business person, we hope that the future holds plenty more work! Plenty more business for the firm, interesting assignments for our team to work on, and genuinely, more scope to make a positive contribution to the improved governance of the financial services industry. To focus on one particular area, we are finding the board-level search work we have been doing of late absolutely fascinating, so we are hopeful that there will be more opportunities to help clients to find INEDs for their boards in future. For the search industry, we think the future is generally an exciting place, although there are a few pitfalls for us and our peers to watch out for. Advances in technology that may change and redefine how we interact with clients and candidates are already here. We're all in constant communication thanks to mobile communications and mobile internet, and social networking has brought us all a lot closer, which is both very helpful and also a competition factor. There's a tendency towards more detailed assessment of senior individuals, in order to understand the likelihood of success in a given role from one person to another. A facilitator of that analysis is the field of psychometric-driven leadership assessment. Almost every large firm we speak to has an interest in psychometrics and how we use them, and progress in fields such neuroscience, behavioural theory and social anthropology will continue to drive advances in that space. We think that is exciting, especially when a general psychometric assessment is tailored to the particular requirements of a senior governance role, like a Chief Risk Officer or modern Chief Compliance Officer. Returning to our business, we'll maintain our specialist focus on our key areas, and continue to increase our footprint in London and Edinburgh. A Europe office opening as a reaction to Brexit is almost a certainty. Brexit is a an extraordinary situation, and the outcome remains unclear, but most of the firms we have spoken to are doing the best to turn the situation to their advantage, which seems like a constructive approach. We'll respond to Brexit in our way because of the implications the process has for London, which is our key market, but also because of the size of the industry on the continent. There are huge opportunities there. London remains our home though - the City is in our blood, and it has always been a fantastic place to work.

> “Investment in people, and the development of leadership in these areas is on the rise, but it takes time to develop leadership-level talent in what have typically been heavily technical roles.”

In Conversation with Nicola Megaw

on the issue of individual accountability in the fast-evolving financial services industry

Nicola Megaw is Chief Legal Officer and Company Secretary at Nucleus Financial Group. She has been with the group, a leader in the wealth management platform space at the vanguard of financial technology, since 2012. She studied law at the University of Aberdeen and trained at Shepherd and Wedderburn LLP, where she gained experience in capital markets, funds and financial services, as well as general corporate advisory work. Nicola has a passion for diversity and inclusion and actively champions Nucleus' work in this area.

Nicola, would you set the scene for us by telling us a bit about Nucleus?
We are a wrap platform, based in Edinburgh. Our goal is to create value through the strategic alignment of financial advisers and their clients. We aim to achieve this by having a compelling proposition for our platform users and customers, an attractive value proposition for shareholders, and a motivating people proposition to inspire high-quality execution. We recently listed on the AIM market and have always been FCA-regulated. Both of these factors give rise to a number of rules and regulations that create a healthy tension with our desire to innovate and disrupt traditional financial services.

How have you been helping the firm to prepare for the Senior Managers and Certification Regime?
The SMCR will apply to us from December 2019, but we are already making changes to our governance arrangements to move towards an ethos of aligned accountability. As a fintech firm, I'd imagine we are grappling with many of the same issues as our peers in this emerging industry. Our product relies on our behaviours, as much as our software, regulation, and the governance and risk management frameworks within which we as financial industry professionals must act. On the face of it, things like agile methodologies for software development may not necessarily equate with individual accountability. Nevertheless, we want to empower our teams to deliver momentum and growth. We resonate with the Spotify model of 'aligned autonomy', and are challenging ourselves to ensure our governance structures balance autonomy and alignment with accountability. We aim to build a model that supports our senior managers to derive the trust they need that operations are running as intended, and the tools to validate that trust through positive conduct and accountable behaviours as much as reporting and attestations. In our view, 'I will', not 'I must', tends to lead to more accountable and ethical behaviours.

That's a very progressive approach. Does the SMCR differ greatly from the previous regime, in your opinion?
This is a regime that will work through behaviours more than process, and if it is implemented well in each firm, I think it is for the better of the industry as a whole. I like to think of it as providing a structure that will empower and enable a company's people. This is an opportunity for business leadership to get behind what the regulator is trying to achieve.

An aspect of the regime itself is getting the industry, and regulation thereof, fit-for-purpose for the next stage of the market's lifecycle. What questions do you think it raises about the nature of corporate governance in the UK?
Looking at the positives first, there is certainly some overlap with what our UK corporate governance regimes and the regulator are trying to achieve, particularly as corporate governance in 2019 heralds the increased importance of the 'stakeholder', alongside the long-established idea of 'shareholder primacy'.

> "Ultimately, company leadership teams and boards need to display the cultures and behaviours that are going to make the SMCR a positive success."

Customers, users and the workforce – those with whom and for whom the business operates – are back in the centre of the value conversation. This aligns with two of the core conduct rules that apply everyone in each SMCR firm – the duty to act with integrity, and to pay due regard to the interests of customers and treat them fairly. Also, the governance codes are all now moving towards shorter, sharper principles – accordingly, the focus is on how you do it, not if you do it. Seeking the approach that's right and proportionate for a given organisation is the way forward. I welcome this approach in the SMCR too. Where it doesn't join up, though, is in how SMCR calls the concept of the unitary board into question.

That's an important point, can you expand on that issue?
Some see this as a regulatory reaction to an inability to prove the culpability of boards as a whole. Do corporate failures lie with boards as a whole, or does it come down to an individual in particular? It's always a tricky question to answer. At Nucleus, we are focusing hard on ensuring that we do not create homogenous bias in our decision-making, by introducing targets and voluntary regimes to measure our diversity as a collective. But how does that sit with regulations that effectively split the accountability between different board roles, as the SMCR does? At senior executive level, this may have the desired effect. We've recently seen the CEO of Barclays, Jes Staley, personally fined in the first case brought by the FCA and PRA under the Senior Managers Regime, and TSB's former CEO has stepped down following the IT meltdown in 2018. But should the equivalent be true for some, but not all, of our Board's non-executive directors? Additionally, the chairs of each committee will hold senior management functions in their own right, distinct from the non-chairs. How does this align with the basic company law principle that all directors are equal in terms of corporate responsibility? Not only could this undermine collective decision-making, but it will also inevitably lead to a new discussion on remuneration. It will also be interesting to see how the asset management industry reacts, as the FCA's study into the industry has led to recommendations that all firms have at least two independent non-executives on each board.

It's an evolving discussion, and some of the questions raised are going to make interesting topics for consideration by the City's law firms, I am sure. In the meantime, you alluded to diversity in your last answer. We know diversity is high on the agenda at Nucleus, as of course it is for many firms in the financial services industry. In your view, does the increased focus on individual accountability seem likely to promote and facilitate that growing diversity and inclusion agenda?
I think this is a really interesting angle. If diversity is the desired outcome, inclusion must be the act. At its core, achieving greater diversity by addressing under-representation across a range of factors is simply the right thing to do, both morally and ethically. However, there is also – helpfully – a business imperative that is increasingly hard to ignore. Cognitive diversity – that is, diversity of thought – is a must for a healthy decision-making environment. The manner in which we address inclusion will go a long way towards making sure that we are creating the right conditions for our people to do their best work – and this goes all the way to the top. Whilst SMCR highlights that certain individuals may be culpable for certain activities, the new regime also acknowledges one of the basic tenets of good leadership. Accountable individuals must take 'reasonable steps' to prevent breaches, and to discharge their responsibilities. In practice, this will be achieved day-to-day through strong delegation, coupled with appropriate oversight, and careful consideration of the evidence required to demonstrate challenge in decision-making. Done right, using such a 'trust and validate' approach, accountable leaders can still create the space and environment for those to whom responsibility is passed to let the team develop and grow. Where we run the risk of creating non-inclusive environments is when we do not create the conditions for healthy debate, challenge and shared decision-making.

> "The SMCR is a regime that will work through behaviours more than process, and if it is implemented well in each firm, I think it is for the better of the industry as a whole. I like to think of it as providing a structure that will empower and enable a company's people."

What's the 'next frontier' in the inclusion conversation, in your opinion?
I'd like to see kindness play a prominent part in our industry's corporate structures and values. Supporting the principles of fairness and respect, of inclusion, and of putting our customers' interest first. I think with this approach to our structures, our peer-to-peer, adult-to-adult collective decision-making and support mechanisms can flourish. This extends to a concept of relational leadership – behaviours that promote trust and human connections, and promoting the team despite individual culpability. We've all heard of the Amazon.com ethos of "disagree and commit". It makes sense, of course, but ideally, we should be striving to achieve a consensus, following healthy debate and challenge. This is as true at the executive table as it is at the board.

In the words of David Hume, "truth is reached through disagreement between friends." Do you think the SMCR will have a positive impact on the industry overall? What possible adverse effects can you envisage?
As we touched on earlier, I do fear that if we don't do aligned accountability right, we risk threatening that basic tenet of corporate governance, the unitary

> “If diversity is the desired outcome, inclusion must be the act. At its core, achieving greater diversity by addressing under-representation across a range of factors is simply the right thing to do, both morally and ethically. However, there is also, helpfully, a business imperative that is increasingly hard to ignore.”

board. Does our regulator really have the right to create opposing forces between ‘regular boards’ and ‘regulated boards?’ If we isolate our top team and their decisions, we could be inviting additional stress and mental health strains, which, needless to say, will be counterproductive. It will be interesting to see how the impact of certain public mistakes will be considered by the FCA in terms of those already subject to the regime, and what long-term impact that may have on the attractiveness of non-executive and senior positions in financial services. From a positive perspective, though, this is about culture, conduct, behaviours. We are kidding ourselves if we don’t also recognise the importance of these things in how we lead our people and our companies. The regulator is at times reluctant to help us design processes. It can sometimes be hard to get a clear message on what good looks like, particularly with conduct risk. With the potential for more fines against individuals, I’d like to see the industry react by developing behaviours and cultures that support aligned accountability – teams, collectively driven and comprised of autonomous, empowered individuals who are supportive of one another.

Yes, it’s interesting to see the regulator already flexing its muscles and showing the industry that it is serious. A final question is this: how do we get this to be about encouraging and embedding positive behaviours, rather than simply dodging fines?

The SMCR shouldn’t be, or be seen as, a system designed to catch people in the act of poor behaviour, thereby promulgating a fear culture – fear of not being good enough, or fear of a negative regulatory reference. That said, it needs to have an impact and people need to take it seriously. The regulator can achieve this to an extent by making it clear that the consequences of violations are serious. Companies can recover from fines, but can individuals recover their careers after a negative regulatory reference? Ultimately, company leadership teams and boards need to display the cultures and behaviours that are going to make this a positive success. That means promoting good governance, finding an equilibrium between taking risks and maintaining controls, and creating a positive, forward-looking culture of kindness, resilience and collective endeavour.

An inspiring note on which to end this fascinating conversation. Thank you for your time and your thoughts, Nicola.

In Conversation with Gary Storer

on the topic of the Senior Managers and Certification Regime

Gary Storer is Founder and Managing Director of Enterprise Learning, a leading and award-winning regulatory consultancy focused on the people element of compliance and regulatory risk management within financial services. He founded Enterprise Learning in 2002 after a career in people change and organisation transformation, mostly in regulated financial services organisations, including senior roles at Legal & General, Gartmore Investment Management and NatWest, as well as an early tenure as Managing Consultant in KPMG's Financial Services Practice.

Gary, can you explain what the Senior Managers and Certification Regime is, and what it means for senior professionals at financial institutions?
Over the last ten years or so, since the financial crisis, there has been a growing desire to hold senior leaders to account for the conduct or misconduct of their organisations, whether these are charities, audit firms, or the media. Obviously, one of the focal points has been financial services. In my view, the SMCR is the most important new regulatory regime since 2002, when the FSA was first set up, because it's all about personal accountability. Eventually, by the end of 2020, every single person in financial services will have a personal obligation to contribute to the good conduct of the organisation that employs them. It's a sea change in regulation.

The difference being that it was previously more about the organisation having accountability for conduct issues than employees?
The Approved Persons Regime gave accountability to some senior managers and some specialists, but the burden of proof that a regulator had to meet, in order to prove that somebody had been negligent, was very high. The crisis showed us that there was an issue with that, in that very few people actually ended up being fined or banned from the industry, despite the litany of conduct issues exposed.

What are the key conduct rules that underpin the new regime?
There's a personal obligation to adhere to five key rules for Senior Managers, and also those who fall under the Certification side of the regime. The only people who are excluded are those in functions such as corporate services, facilities and so on. Everybody in the industry will have a personal obligation to comply with the five conduct rules, just as a lawyer or a doctor might adhere to a code of conduct in their industries. Then, for people in Senior Manager roles, there are four additional conduct rules that are relevant to managing the organisation.

It sounds like it has been kept fairly simple and formulaic on the surface, but interpreting these, then demonstrating and documenting compliance, could be quite complex, especially for large firms. Is that correct?
Comparing it to the old Approved Person regime, the most important thing that impacts on senior people is what's called the new 'Duty of Responsibility'. Whilst under the old regime, regulators would try to hold people accountable but would only be able to do so in cases of demonstrable negligence or criminality, under the new regime, what the regulator needs to prove is that the individuals have not taken 'reasonable steps' to do their jobs properly. It lowers the bar when it comes to proving accountability.

It's already in place across banking and large insurers, and it will soon be rolled out across the whole of financial services. What kind of things can those organisations learn from the experience that the banks have gained in recent years?
A great deal, is the short answer, although there are probably two really key lessons from the banks' experience and that of big insurers under the Senior Insurance Managers Regime. The first is just the operational burden: the banks had to set up a lot of operations to deal with annual certification of thousands of people. No longer will the regulator do the screening of individuals who are, in the old language, Approved Persons. It's down to the firms. Secondly, banks have also told me that they underestimated the cultural and behavioural challenge in helping people to really understand and accept their new obligations. People in financial businesses are taking on a new level of accountability for their actions, and have to assimilate that into their daily work.

There generally aren't enough hours in the day as it stands, let alone factoring in another large chunk of activity, the validity of which some people might initially be inclined to question in the first place. I can see where the challenge would arise.
The trick is to implement the SMCR so that

it doesn't become an operational challenge. What you don't want to do is tie Senior Managers up in bureaucracy, but you do need them to think, if this decision is being looked at by regulators in future, is it clear why we've made it? And were we taking into account the various risks that we are running, and risks to the customer, and has this been demonstrated?

What kind of penalties are being talked about? Are there clear guidelines on that?
There are a lot of examples of what the regulator would see as a breach of the rules. In terms of penalties, it's probably too early to say yet, because there aren't that many examples of people being held to account, but the regulator can now both fine and ban individuals from the industry.

What has the banking industry's response been like to the Senior Managers Regime?
I think they are taking it seriously. It has been a bit of a wake-up call because the relationship between Senior Managers and the control functions has changed. A lot of new governance frameworks have been set up and Senior Managers have had to change the way the way they think. Interestingly, one of the things I have heard is that it has also changed the way that they work with each other at board-level. Individual directors now need to work quite hard not to be too divisive in board meetings, whilst protecting their own obligations and accountabilities. It would be easy to allow a culture to develop whereby everyone protected their own areas of accountability and didn't really collaborate. I've seen examples of this, and I've talked to Senior Managers who have noticed that was happening and have taken action on this.

It sounds as though it will fall to HR and compliance to work with Senior Managers to help them understand their responsibilities. What should HR and compliance teams at asset managers and other firms be thinking about at this stage?
I certainly see HR teams getting more involved in regulation and risk management than they previously had, driven by the new regime. HR and recruitment teams are now very clear about the accountabilities and obligations of the people they are hiring, for example, and are working with compliance and Senior Managers to ensure that onboarding processes for new joiners are thorough. Each Senior Manager is required to sign a statement covering their personal obligations, and the regulator expects a due diligence and a handover process to ensure that those people know what they're taking on. Often, that's coordinated by HR and compliance. Additionally, under the new regime, if there's ever a breach, that has to be reported through regulatory referencing, which is another operational challenge for the HR function.

To what extent is this on the board agenda as a strategic or operational issue?
A Senior Manager, not HR or compliance, needs to hold accountability for how the regime is running, and that can be the CEO, or it can be one of the board directors. That's one of the SMF accountabilities. Generally, accountability, as in how Senior Managers make decisions, and whether they are taking reasonable steps to protect customers as well as the organisation, is definitely something I am seeing discussed at the senior level. When a new initiative is proposed, or a strategic decision is made, people are asking more questions than they have done previously. Interestingly, it's forcing the discussions that perhaps haven't been held in the past.

How is it all being administered? Is technology playing a role?
There are systems out there now which take over from the point that an applicant applies for a role, that will do a lot of the referencing and screening prior to the recruitment process getting underway. HR teams are still struggling a little bit to weld the requirements of SMCR into some of the generic performance management systems that they use, and that has been a challenge, given the specificity of some of the requirements. I think the smart way of maintaining and monitoring compliance that we've seen in some organisations is to try and build those controls into normal day-to-day processes.

The next question must be how to turn compliance with the Senior Managers Regime into a competitive advantage.
Many firms have realised that by having an adequate risk framework in place, at the very least you can avoid the consequences of misconduct, such as fines from the regulator, or management distracted from their work by having to fix things that have gone wrong. There is real evidence that if firms have not just adequate, but robust, thorough and thoughtful risk management frameworks in place, they will be allowed to take more risk by regulators, and can move into different areas of business or even different parts of the world. Conversely, weak risk frameworks in this 'post-crash era' make regulators more reticent to extend permissions.

> "There is real evidence that if firms have not just adequate, but robust, thorough and thoughtful risk management frameworks in place, they will be allowed to take more risk by regulators, and can move into different areas of business or even different parts of the world."

You can see that being impactful at smaller businesses. Large groups that are already globally active are going to take this in their stride, but smaller groups that are looking to grow could make forward-thinking compliance with the regime a strategic advantage. A facilitator of growth, instead of the opposite.
On the other hand, some firms have become a bit too risk-averse. I spend quite a lot of my time as a consultant and coach helping Senior Managers understand that a 'reasonable steps' defence is about reasonable steps – it's not about jumping over a very high burden of proof.

Or having to spend an excessive amount of money on covering every single base.
Absolutely – in fact, where things are working well and risk management is being integrated into the day-to-day business, the cost of risk and controls actually falls. Eventually we might see a premium from the regime if it becomes truly embedded.

From a search and selection perspective, the impact we've seen is that when hiring for banks, a lot of supporting documentation is provided on the precise areas that a certain Senior Manager is going to be responsible for looking after, the entities that they'll have responsibility for covering and the reasons why, adding several pages to the job description in some cases. You can tell when an organisation has been taking this seriously because that documentation is thorough and it's a step forward from what we've seen in the past.
And conversely, I'm hearing from HR contacts that when candidates are applying, they are asking challenging questions about the role that they are taking on, the obligations and responsibilities involved, and how the organisation works. Even in sectors where the SMCR isn't yet in force, applicants for what will be Senior Manager roles are looking hard at what they're taking on, and at how ready the hiring organisation is to support them in their duties.

One thing we're not clear on yet is the remuneration impact of SMCR, as in what additional compensation it might take to get people into Senior Manager roles in future. When cases come to light and the FCA starts penalising people, I suspect we will see higher expectations.
Yes, I'm sure that will happen. I've been party to one situation where the head of HR for an insurance firm felt very strongly that taking on accountability for risk management was part of the existing day job, and the obligation to do that hadn't changed from pre-SMCR to post-SMCR. That said, where Senior Managers become more careful about what they're going to take on and which organisations they'll work with, one of the ways that might be mitigated could be through more interesting compensation structures.

Compensation is always an interesting topic in financial services, particularly given some of the Senior Managers most impacted by the new regime, and possibly with most at stake, will be those in senior commercial functions. They will be heavily incentivised salespeople and business leaders whose activities will be closely monitored. You might be forgiven for thinking those people would be inclined to be cooperative with the regime, to protect their positions.
That's where the biggest challenges are: senior management teams will now pay more attention than previously to where a business's profits are coming from. I'm seeing NEDs in particular being quite challenging about revenue numbers that are coming in if they are far in excess of expectation. Additionally, the individuals in sales and other commercial roles themselves will also need to look at how they are generating their income, and whether their methods will now pass the litmus test of external scrutiny. Chasing profit will eventually be noticed by the regulators and by Senior Managers, and challenged. It's about embedding this mindset into commercial processes – structuring, marketing, sales, trading – and the fact that those functions have been separate in the past will make that difficult.

It's quite good to hear that the regime empowers NEDs and other Senior Managers to ask the difficult questions of an organisation's most profitable staff members; questions that might not be welcome, but could save us over time from another financial crisis. Setting aside the positives, do you think there are any 'blind spots' with the SMCR that might cause problems?
The regulator's view tends to be that the way an organisation's culture can and will change and improve is 'top-down'. Their view is that Senior Managers' behaviour shapes the culture of an organisation. I believe that 'culture' is a lot more complex than that, and I'm not sure that the Senior Managers Regime fully recognises the way that organisations work. You might have a large organisation with a number of different cultures from one division to another, so Senior Managers will have to work quite hard to make sure that they understand where all the risks are, especially in dynamic environments. External specialist firms – auditors, consultants and so on – may get close to the more esoteric areas and provide useful advice, but I'm not sure the new regime will be able to cover everything. The other danger is that senior managers themselves come to rely on a bureaucratic incarnation of management reporting, which provides false comfort through box-ticking. To combat this, Senior Managers will need to go the extra mile when it comes to understanding where the risks are in the organisation, this networking and questioning on one's own account will be at least as important as adhering to the formal governance structures put in place. Compliance departments will facilitate this as well, as long as they can position themselves to do so. In the course of your search activity, are you seeing a change in the required skills and characteristics of risk and compliance specialists?

Yes, the profile of the chief compliance officer, and the chief risk officer, is moving in the direction of that of the general counsel, so a sort of consigliere, or trusted adviser, to the business. Controls are such a key component of the current business conversation that it's become essential that they do, and where firms don't feel they have the right level of advisory capability in those roles, they are taking action. It's an issue in some cases, because the advisory skill set doesn't come naturally to everyone. The controls functions generally are working on this through leadership assessment and development, but I get the sense that there is still a way to go. There are time constraints on training versus business as usual, there are budgetary issues that constrain remuneration, and there's generally an issue relating to the size of the existing talent pool.
You're right to raise the issue of leadership development. It has been neglected somewhat in controls functions, and the SMCR is now driving an increased focus on formal leadership development. I'm doing some work with Ashridge Business School to launch a new programme there, focused on leadership in regulated environments, which is getting quite a bit of attention. We are also seeing a lot more focus on coaching and individual support to help leaders deal with the challenges and dilemmas that they face day to day.

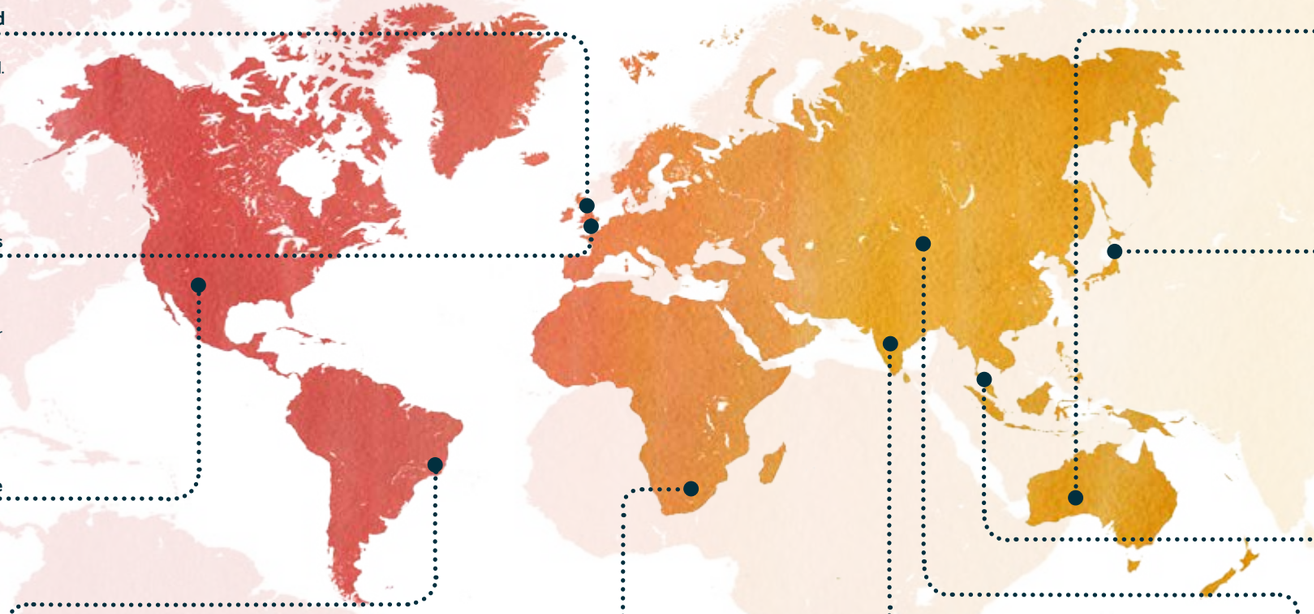
What about the Certification regime? The good thing about that seems to be that it catches people early, in terms of their careers, and should embed an accountability for behaviour at this level that previous generations might have lacked as they developed in the industry.
I think that's absolutely right. I suspect that if the SMCR beds in and companies get it right, then just as in hospitals or law firms where you find people are very conscious of their personal responsibilities, we'll find that in financial services, and that will percolate through successive generations of leadership. That's the long-term goal of the regime, and it's a noble one.

Let's not forget to discuss activities outside the UK. In a global marketplace, the success of the SMCR will rely on not only the UK having a regime based on personal accountability, but also other parts of the world as well. Are other countries following in the UK's footsteps?
Yes, a personal accountability regime is on the way in Australia, and the US has always had a much stronger focus on individual accountability. I think the approach that's been taken in the US is quite extreme, so you see financiers frequently doing the 'perp walk' in New York, which we've only rarely, if ever, seen over here. It will be interesting to see whether the SMCR goes down that route and makes things more punitive – the next couple of years will be telling. We're also seeing similar accountability regimes in the Middle East, for example, as those countries try to persuade banks and insurers to base themselves over there. The focus on conduct, misconduct, and the accountability of individuals for what their organisations do, is a phenomenon that we are seeing across the world in lots of different sectors, and especially in financial services, which is a truly global industry.

It's a positive development, on the whole. Thank you very much Gary, this has been interesting.

OUR World Map of Governance News

In financial services, commerce and industry, and politics, the topics of governance, regulation, and occasionally scandal, are constantly in the headlines, and consequently drive conversations amongst the organisations affected and their global peers. Evidently, anything can and does happen, meaning that effective regulatory, reputational, operational and political risk management remains critical to the functioning of businesses around the world.



UK (Birmingham): Collapse of Patisserie Valerie Due to Massive Fraud

Patisserie Holdings plc, the owner of Patisserie Valerie, collapsed into administration recently following the discovery of an alleged accounting fraud. Aspects of the fraud, described as "scandalous" and "devastating" by fund managers holding stakes in the company, include "thousands of false entries" in company ledgers, and "secret overdrafts" totalling more than £9 million. 71 of Patisserie Valerie's 155 UK locations will close down as a consequence, although the story may yet have a happy ending, as the firm's administrators are confident of finding a buyer and saving circa 2,000 jobs

UK (London): The Trials of Senior British Executives, and Their Prosecutors

Current and former leaders of Barclays Bank faced difficulties in 2018. The Serious Fraud Office-led trial of four senior executives, linked to the bank's crisis-era capital raising from investors in the Middle East, began in late 2018. In the meantime, Barclays' new CEO, Jes Staley, was fined by UK regulators for his reaction to a letter from a whistleblower in 2016. Meanwhile, the pressure is on the SFO itself to achieve a significant victory, following the embarrassing collapse of its cases against former Tesco executives for their role in a 2014 accounting scandal, and against City brokers accused of LIBOR rigging in collaboration with convicted trader Tom Hayes.

USA: #MeToo Movement, Originating in the US and Spreading Worldwide

The #MeToo movement took flight in 2018 and became a worldwide protest against sexual harassment and sexual assault in all walks of life. The ubiquity of the term 'Me Too' in 2018 gave a sense of the magnitude of the problem. Women and men coming forward with tales of harassment, in some cases dating back decades, led to the exposure and occasionally prosecution of many powerful men across a multitude of environments. An example of the impact of the movement in the UK was the closing down of The Presidents Club, a charity which organised a long-running, men-only event for business leaders. An undercover Financial Times investigation in 2018 discovered and exposed widespread sexual misconduct at the event.

BRAZIL: The Rise and Risk of Strongman Politics

In 2018, Barack Obama characterised 'strongman politics' as "the politics of fear and resentment" and made clear that they are globally on the rise. Following in the footsteps of China's Xi Jinping, the Philippines' Rodrigo Duterte, Hungary's Viktor Orban, Recep Tayyip Erdogan of Turkey, and others, the most recent 'strongman' elected into high political office was Jair Bolsonaro in Brazil. A former Army captain and prominent far-right wing politician, he won by pledging to fight crime and corruption. However, critics are worried by his praise of Brazil's repressive former military dictatorship, and for his offensive comments on race, women and homosexuality. The contrast in 2018 between the rise to political prominence of such people, and the rise of the #MeToo movement and similarly progressive initiatives in business and society, was striking.

SOUTH AFRICA: Conduct of Accountancy and Consulting Firms

It was a challenging year for the world's major audit and consultancy firms. The 'sign-off' of KPMG's pre-crisis audit of HBOS caused sufficient public outcry in the UK to warrant a review of the entire audit industry by the Competition and Markets Authority, and a review of the effectiveness of the Financial Reporting Council. In South Africa, work by consultancies on behalf of the Gupta family, accused of 'state capture' through corrupt links with the regime of former South African premier, Jacob Zuma, led to a boycott of, and lasting reputational damage to, the firms involved.

INDIA: The Nation's Biggest Ever Bank Fraud

A US$2 billion fraud at Punjab National Bank, India's second largest state-owned financial institution triggered a massive investigation and regulatory changes across the nation's banking sector. The investigation showed that the fraud avoided detection because of widespread risk control and monitoring lapses across various areas of the bank. It is another wake-up call for the global financial services industry, which has been struggling to combat financial crime in recent years. The fraud has attained international attention due to the involvement of 'celebrity jeweller' Nirav Modi, who is in the process of seeking asylum in the UK, citing "political persecution".

AUSTRALIA: Widespread Investigation-Misconduct in Financial Services

Australia's government launched the epochal Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry in December 2017, and has since revealed a failed industry culture blighted by ineffective and overpaid executives, regulatory issues, and an underfunded industry regulator that has consistently failed to hold firms to account. More pain may be yet to come. "It has not even scratched the surface in terms of bank scandals," said one industry observer. "The industry thinks it is just about off the hook, but we are only at the beginning."

JAPAN / GERMANY: A Bad Year for Automobile Industry CEOs

Carlos Ghosn, formerly CEO of both Renault and Nissan, was arrested in Japan in 2018 for various alleged financial offences, and now faces judgement under Japan's notoriously draconian legal system. Meanwhile, former Audi CEO Rupert Stadler was held in custody, and then fired from his position, for his alleged role in the emissions scandal that has plagued the Volkswagen Group. Elon Musk also had an erratic year at the helm of Tesla. His behaviour led to investigations by the DoJ and the SEC and he consequently relinquished the Chairmanship of the firm (although he remains CEO). He has since commenced 2019 with a late-night email to Tesla staff to announce a 7 % cut to the workforce. Nevertheless, quoting Musk's email, Tesla's mission – "accelerating the advent of sustainable transport and energy" – remains inspiring, and "important for all life on Earth."

MALAYSIA: 1MDB & the 'Billion Dollar Whale"

1MDB, or the 1Malaysia Development Berhad, became embroiled in scandal, exposed in 2018, involving the fraudulent investment activities of a Malaysian banker / "tabloid party boy", allegedly in collaboration with APAC-based partners at Goldman Sachs. The scandal has led to the downfall of the former Prime Minister of Malaysia, Najib Razak, and a demand that Goldman Sachs itself repay US$7.5 billion to the Malaysian people. The bank faces its first-ever criminal charges as a result of the scandal, whilst Leo DiCaprio testified before a US Grand Jury in relation to film financing elements of the fraud.

CHINA: Beijing's Social Ratings Programme

25 years on from the fictional events depicted in George Orwell's '1984', aspects of Orwell's prophetic vision appear to be manifesting themselves in reality. "Doublethink" is on the march, in that 'alternative facts' are now commonplace in political discourse, whilst 'wilful blindness' has undoubtedly played a role in numerous frauds, bubbles, financial crises and corporate collapses. Now the active monitoring of public behaviour is upon us, as the Chinese government rolls out a 'Social Credit' programme, starting in Beijing, with the aim of monitoring, rewarding and punishing 22 million citizens based on their actions and reputations. To quote the ominous subtitle of '1984': "Big Brother is watching you."

In Conversation with Alex Rickard

on Organisational Culture - who is in charge?

Alex Rickard is a highly experienced HR Director, executive coach, and consultant on leading-edge and culture-related issues. She has spent her career in global HR leadership roles in many industries including a long tenure as HR Director for Towry Wealth Management, helping to grow an organisation originally valued at £38 million to one that sold at £600 million, and is now part of Tilney Group.

Alex, a good starting point might be to put 'culture' into context. Why is the question of culture currently so topical?

It has become more widely apparent that it is a critical underlying factor of the success, longevity or failure of businesses and organisations, and the consumer and society arguably have the most to lose in the event of a business failure due to a faulty culture. There is now a substantial body of evidence that shows healthy organisational cultures are positively correlated with high levels of customer satisfaction and better financial performance. However, with this widening appreciation of culture, there is an increased danger of businesses simply ticking the 'culture' box, rather than approaching the issue strategically. A healthy culture can both protect and generate value.

By culture, do we mean employee engagement?

No. From my perspective, culture is the behaviour that an organisation displays as a collective. Its unique leadership, structures, processes and communication methods, defined by a set of values and habits, signal to employees how they should behave. It is closely related to, but should not be confused with, 'employee engagement', which is the term to describe the feelings that individuals at the company have towards their work and their firm.

Given some of the arguably culture-related implosions in British business in recent years, has there been a regulatory response in the UK?

Yes, and the response originates at the policy level – the very highest levels of government. Theresa May laid out her plans in 2016 to tackle bad corporate behaviour. Stating that corporations had a responsibility to pay their fair share in taxes, she also reintroduced the proposal that company boards should have employee representatives, in order to close the gap between company leadership and the people actually doing the work. Whilst the latter has not yet been agreed, gender pay reporting, introduced last year, has provided at times shocking insights into employers' attitudes towards rewarding employees. Eyes are also on the Government itself, due to the issues brought to light around aspects of an unhealthy culture in Westminster – bullying, sexual harassment and the like – and how they are going to tackle it, so it's not like the Government itself has the strongest moral position at this point. Nevertheless, the policy position around better corporate behaviour is naturally reflected in the communications from the UK regulators to the financial

services industry. Keith Jackson, Director of General Insurance and Conduct at the Financial Conduct Authority, reiterated that "culture and governance remains a priority" as recently as April 2018. Additionally, Sam Woods, CEO of the Prudential Regulation Authority, said: "If people want to rise to the top of firms – with all the rewards that brings – whilst ducking proper accountability, then they are in the wrong sector." The PRA's new Senior Managers Regime is arguably all about improving culture in the financial services industry, by increasing the degree of individual accountability – as in, responsibility for one's actions.

The FCA and PRA are not alone in focusing on culture – the Financial Reporting Council have been very active in the culture field in recent years, haven't they?
That's right – the FRC ran a major study of culture in 2016, and as a result have revised the UK Corporate Governance Code, which they set and to which they oversee adherence. The revised code was put in place in late 2018 and is explicit that culture is a responsibility that sits squarely with the Board. The code is applicable to all companies with a premium listing on the public markets, whether they are incorporated in the UK or elsewhere. The code does not set out a rigid set of rules, instead it offers flexibility through the application of principles, and through 'comply or explain' provisions, and supporting guidance. It makes very clear that it is the responsibility of boards to use this flexibility wisely, and of investors and their advisors to assess differing company approaches thoughtfully. There's still clearly a way to go on this, though, before boards can say they are truly engaged in the culture conversation. In a survey carried out by the FRC in 2016, involving 24 FTSE-listed companies, 33 percent said they discuss culture and ethics every six months and as a full board agenda item, and 28 percent said it was only once a year. This is frighteningly infrequent given a faulty culture can present such risks, and on the flip-side, such opportunities if a firm's culture is in the right place.

What are the key changes implied by the new code? Who will be most affected by this?
The Board and Remuneration Committee are most affected by the changes, as they are in charge of adhering to regulations and overseeing the activities of the CEO, but they now also need to figure out how they will measure or assess their culture, and that can entail some new thinking on their part. Is their firm's culture what they think it is? How do they know? It's not good enough to give a woolly description anymore – there needs to be some hard evidence, and because it is seen as a sprawling grey area, it can feel almost impossible to measure. Without a definition, or an index, for want of a better word, and agreed metrics, a starting point might seem impossible to find. For me, this is one of the major challenges for businesses in relation to culture, and the temptation is to shelve it, because it is challenging and hard to quantify. Also, who knows what you might find if you start accurately measuring your firm's culture! The elephant in the room is also the challenges that the FRC is facing at the moment, in relation to its own policing of the audit industry in recent years. This, and the issues in Westminster, lead to questions around the conduct of the regulators themselves, and the example that they are setting for the rest of us.

It's a burning issue, undoubtedly, and a field in which thought and practice are still evolving when it comes to optimising corporate governance. Are there things that companies and boards can proactively do to meet their new obligations, at least from a process perspective?
I am often asked, how can we define our culture? How do we measure our culture? How do we report on it? Well, it's very doable, but there aren't any quick fixes. One of the services I provide to my clients is that of cultural evaluation, defining the existing state of a firm's culture requires a strategic investigation, and the reviewer needs access to all corners of the business. This can be a bit uncomfortable for businesses, but the old adage applies – "the first step to solving a problem is acknowledging that you have one." The methodology I have built looks at both internal and external data, and the good thing is that there is always a lot of data to work with, if companies are keeping decent records. Internal measures of staff engagement, such as employee engagement surveys, employee staff council minutes, exit interview notes, grievances, employee policies and procedures, performance appraisal results, promotions and related reward discussions,

> "From my perspective, culture is the behaviour that an organisation displays as a collective. Its unique leadership, structures, processes and communication methods, defined by a set of values and habits, signal to employees how they should behave."

management-to-staff ratios, attendance and dropout rates of training courses, and cultural diagnostics such as employee turnover, length of service, recruitment process, and whistle-blowing policy, are all useful data points. External measures include customer feedback surveys, customer complaints, behaviour in regard to supplier payments, and the quality of regulatory relationships. All of this 'hard data' will allow the reviewer to form a critical perspective of your culture.

That data-heavy approach is interesting. Business is generally quite taken with data at the moment, so if you can apply a data-centric approach to the seemingly intangible notion of culture, you will glean some real insights.
That's right – all businesses have this data but they do not join the dots. In addition to hard data, I gather soft data by conducting one-to-one confidential discussions with employees across the organisation, ensuring each pay grade and function gets their opportunity to have their say, including the Board. A review like this is by no means a 'tick-box' exercise: it requires expert data gathering, excellent listening skills, building trust and ensuring confidentiality, whilst conveying gravitas but approachability. The real magic is in the detailed analysis of the hard and soft data in the context of the organisation's leadership. The output of this discovery phase is a strategic analysis of a firm's culture, articulated in a practical and measurable way, with recommendations and actions, next steps, a roadmap with timescales, responsibilities, risks and resources required.

How has the sort of data you're talking about been used in the past?
That's a good question. Boards and Executive Committees do have reports on some of these metrics, but as I have said before the data is not joined up. The information is looked at in isolation, whereas if it's combined and reviewed in concert, a strategic picture of your firm's culture emerges. Much of this data comes from HR, but culture is not the responsibility of the HR function. Culture defines the behaviour of the whole organisation, and defining culture is the responsibility of the board and executive committee. Without a cultural benchmark, a company cannot begin to report authentically. Without a strategic, joined-up approach to assessing culture, the company is almost inevitably missing valuable data that will impact customer experience and value creation.

What sort of response to do you get from boards with whom you have the opportunity to discuss these issues, and your approach?
Views on the importance of culture remain a mixed bag, partly due to the perceived intangibility of the issue. It's a difficult thing to think about, partly because the methodology for doing so effectively is complex, and partly because the results of a review might raise more questions than they answer. How the company approaches this responsibility tells a story in itself. Risk committees and boards focus on measures such as reputational, financial, operational, and regulatory risk, and also 'people risk', although this is often restricted to succession planning and turnover. As a consequence, flawed leadership behaviours of a CEO, and / or the Chairman, can go largely unchecked, or if noticed, unchallenged, or compromised upon. An example of where this has led to huge issues is in the recently published final report from the Royal Commission on the Australian banking and retail financial services industry, which calls for all sorts of drastic changes, including compensation crackdowns and an overhaul of financial regulators. It has been a fairly shocking and embarrassing exercise, and its findings are nothing short of damning of the industry and its endemic propensity to misconduct.

Talking of flawed leadership behaviours, one might look at some of today's world leaders, and justifiably say the highest profile perpetrator of that kind is a figurehead of a flawed organisational culture. Politics is certainly a mess on both sides of the Atlantic, and there are 'strongman leaders' popping up all over the world. Cultural issues really are everywhere you look, aren't they?
If a company's board, or organisations in general for that matter, political or commercial or otherwise, do not pay attention to the potential 'dark side' of leadership behaviour and associated decision-making, the outcome can demonstrably prove catastrophic for the firm's employees, customers, health and safety standards, shareholders and other stakeholders, and society itself. In the book, 'Wilful Blindness' by Margaret Heffernan, the judge in the Enron case said that the CEO and Chairman "deliberately blinded themselves to the existence of a fact", which led to the firm's collapse and resulting chaos – and may I also point out, lengthy prison sentences for the executives involved. The challenge for boards is that performance is a lagging indicator, whilst behaviour is a leading one.

That's a crucial point – performance is a lagging indicator, whilst behaviour is a leading indicator. I may have to steal that from you! OK – so how you define a good culture?
There are three key themes or principles that I look for. The first is 'purpose'. A good culture is one that is defined by keeping everyone's eyes on the firm's purpose: why does this business exist? The second is 'values': a defined set of values, which explicitly state what behaviours are acceptable and what are not, in pursuit of the company's purpose. Thirdly, people operations: the company's values should be weaved into all recruitment and selection activities, employee induction, learning and development, internal communications, appraisals and reward discussions, promotions and career development, customer service, and finally the means by which the business makes people-related decisions.

The notion of 'values' keeps cropping up in this conversation. How can a firm define its values in a thoughtful way, and then live by them?
Core values and brand values are one and the same. They are already evident in any established business, so it's important to identify them, both the good and the bad, then unfreeze the bad and publicly throw those away, whilst holding onto the good, and amplifying and living by those that remain. For example, you might consider measuring your CEO's performance through the two lenses of your organisation's values versus its straight financial performance – EBITDA, share price etc. – thereby pitting the lagging indicator versus the leading one, and seeing what the outcome is. Such an exercise will undoubtedly lead to some interesting findings. Also make sure to listen to your customers and suppliers, and seek their opinions – they will always be brutally honest about whether you are living your values.

What should CEOs be doing about culture, in your opinion?
The CEO's role is absolutely critical. The CEO of a company is in a position of great power and responsibility, and their organisation provides a platform through which they can fashion a business in their own image. Firstly, CEOs should articulate their purpose and personal values, and keep these at the forefront of their decision making. The CEO must remain grounded and true to their personal values through success, crisis and complexity, because they will undoubtedly encounter all of those things during their tenure as business leaders. Secondly, CEOs should access, evaluate and 'profile' their firm's culture, using independent expertise and diagnostic tools. Through such an exercise, you can establish a benchmark, just like you would an annual audit, and create some metrics to return to over time. After all, why would you rely on what the senior management think is an organisation's culture? Their views will be anecdotal, and may be influenced by individual biases, which are unpredictable. Finally, CEOs should be placing the culture topic firmly on the Board's agenda, and keeping it there. How it is defined, how it is measured, and how high standards are maintained, are the Board and Executive team's responsibility. Setting the standard on the cultural front will be seen as leading by example, and more importantly, in a modern context, being willing to be held to account on these issues.

And your own work at the moment is focusing on advising boards on culture at this time – is that right?
Yes – boards need a mechanism to detect when things are going awry, and an independent expert resource to call upon for an objective view of culture in real time, and that is the service that I provide. This makes good governance sense and indicates to a company's stakeholders that the Board is authentic about setting the culture, rather than being led by it, or worse, caught out by cultural issues. Furthermore, such a resource would be fully up to speed if there is a necessity to conduct a 'deep dive' review, if a cultural dilemma or reputational issue suddenly emerges – as they occasionally do.

As ever, an interesting discussion on a pressing topic. Thanks for your time and your views, Alex.

In Conversation with Tanveer Bhatti

on the topic of Enterprise-Wide Risk Management in the 21st Century

Tanveer Bhatti is a model risk and enterprise risk specialist who has spent a substantial career in global banking with the likes of Citi, JPMorgan Chase and HSBC. A gifted and passionate mathematician, he contemplated pursuing a PhD in the subject before opting instead to begin a career in accountancy, moving subsequently into investment banking. From finance and valuations, he progressed into the emerging fields of model risk and quantitative analysis, leading to his becoming Global Head of Model Risk for one of the world's largest universal banking groups.

Tanveer, a controversial question to start with, but given what happened a decade ago, was the financial crisis really down to a failure of risk management?

My response to the question may be controversial, but it was down to a confluence of many things, key amongst which were over-lending to subprime customers against inadequate underwriting standards, and lapses in corporate risk governance, with greater emphasis 'on partnering with the business' than being a 'policeman'. To expand, there were deficiencies in risk models that everyone had thought were working fine because expensive model validation staff had said so. Not pulling any punches, these analysts did not really understand the business and were therefore ineffective in challenging it. There was also a widely exposed, credibility-shredding failure on the part of the credit rating agencies, who themselves were over-rated as purveyors of an accurate view of the world. On top of that, it was a phase in the evolution of the global financial industry during which greedy bankers were only too keen to exploit all available regulatory, tax and accounting loopholes for their own commercial benefit. Loose, and sometimes vague, mark-to-market accounting standards permitted recognition of revenue on opaque transactions, which was what ultimately did for Lehman Brothers. Finally, there was the inability of regulators to attract top talent that might have adequately challenged the banks, and generally a fairly lax approach from regulators in general, as manifested in their fundamentally inadequate rules around prudential capital. So I don't think it was solely a failure of risk management, rather, it was the inability of the whole industry at the time to orchestrate an effective enterprise-wide risk management process. In my opinion, if designed and implemented properly, enterprise-wide risk management could have identified and mitigated the impact of the crisis. I'd also mention the reliance, especially in case of some credit derivatives, on models that were far too simple to suit the purpose. It is from the crisis that the field of model risk management has evolved.

Next, a bit of an essay question: ten years on from, and as informed by, the crisis and regulators' subsequent response, how would you define the role and positioning of risk managers in today's financial services industry?

Peter Bernstein, who wrote 'Against the Gods' (a book exploring the role of risk in our society), was right about the persistent tension between those who assert that the best risk-based decisions are based on quantification and numbers, determined by the patterns of the past, and those who base their decisions on more subjective degrees of belief about the uncertain future. With the crisis as a backdrop, the expectations placed on risk managers in terms of their duties and their versatility has risen dramatically. The crisis separated the risk management community into two buckets. There is the bucket labelled 'must do better' and the other is 'can bring enormous value'. As regards those who fall into the first bucket, I think a clear lesson is that a successful replay of past approaches cannot be relied upon in the future. Their over-reliance on quantitative outputs from models that assume tomorrow will be more or less like today, or to put it another way, driving by looking at the rear-view mirror, hindered their ability to foresee capital-annihilating extreme tail events and the evaporation of liquidity, both of which we saw in quick succession during the financial crisis.

Tail event risks and liquidity risks are not measured by the formerly ubiquitous risk measure – value-at-risk. VaR was catapulted into centre-stage by the Basel Committee on Banking Supervision that allowed it to be used for capital calculations, and by the Securities and Exchange Commission, that required a quantitative disclosure of market risk in banks' annual reports. Because of the crisis, value-at-risk as a concept has taken a beating in recent years. Alan Greenspan said, in the aftermath of the crisis, that he too had failed to foresee, "the whole intellectual edifice collapsed in the summer of last year because the data input into risk-management models generally covered only the past two decades, a period of euphoria. Had instead the models been fitted more appropriately to historic periods of stress, capital requirements would have been much higher, and the financial world would be in far better

shape today, in my judgement. The "intellectual edifice" was constructed largely by those I describe as being in the 'must do better' camp.

And what about the risk managers that can 'add enormous value'?
Successful risk managers bring enormous value in seeking to creatively prognosticate a future they have never experienced. They apply greater focus and concern to what can happen 1 percent of the time. They also recognise that their job is to know when they don't have a sufficiently transparent view of the risks applicable to a certain scenario to make an effective judgement. They have the experience to appreciate that models can add value, but they also know and accept that risks exist that the models are incapable of identifying. As a consequence of the crisis, such risk managers are now members of senior committees inside large firms. They are invited to senior executive management team meetings, and their opinions are sought frequently by the most senior leaders within these businesses. And you need both types of risk expertise, i.e. the quantitative and the intuitive, to cover all bases, or as many bases as possible. In this context, one can speak of two kinds of risks: (i) uncertainty in events that occur or can be considered to occur in mass-phenomena, versus (ii) uncertainty in one-off events. The former is described by the 'Kolmogorov theory of probability', the other by theories that deal with the probability of the result of a single event (for instance, Popper's propensity theory, and the Dempster-Shafer theory of belief functions). Kolmogorov's probability theory is widely taught and fairly well understood, in contrast to theories developed for non-repeatable events, which are naturally harder to define and comprehend. High-level risk managers should couch their valuable insights about risk in the language of non-Kolmogorov style theories, difficult though it may be.

It's very interesting to hear you talk about things in the context of these theories. I guess risk remains as much a mathematical concept as it is a philosophical one. Is risk itself as a concept much further forward, in terms of its definition?
I certainly think so. In banking, for example, it is now accepted that the risk concept has moved beyond the traditional quantitative taxonomy of market, credit and model risk, into the realms of a holistic notion called 'enterprise-wide risk'. To substantiate this, consider that the financial crisis was as much about faulty models as it was about ethics. Was it right to lend to folks whose credit history suggested they would not pay you back? At the height of the housing bubble, Citigroup CEO Chuck Prince said, "as long as the music is playing, you've got to get up and dance."

Which is famous for being one of the most hubristic phrases of the whole sorry affair...!
And yet it was a reflection of how the world was viewed at the time by the bankers leading the charge – a phrase almost entirely devoid of any recognition of the range of risks – economic, financial, ethical – that were, with hindsight, clearly on display. Perhaps an effective enterprise-wide risk management function would have stepped up and stopped him taking to the dance floor because of the increasingly discordant tune that was emerging!

As a concept, risk can be thought of in three categories: the first covers self-inflicted wounds generated internally, such as employee bad behaviour, badly-designed systems, lack of controls. Secondly, there are risks from doing your type of business and your choice of strategy in particular, such as the market and credit risks encountered by an investment bank. Finally, there are things caused by actors and factors on the outside of your business, such as macroeconomic and political risks. While the first can be managed using rules and monitoring processes, the other two, as underscored by the events of the crisis, require a very different approach involving open and frank discussions. It is the job of the enterprise risk function to bring all of the above together so as to provide the Board of Directors with the 'Big Picture'. Therefore it's an **emerging** function, but one with an increasingly important role.

Where are the frontiers in theoretical thinking around risk in finance right now?
Let's first agree on the terminology. The term 'risk' refers, often rather vaguely, to situations in which it is possible but not certain that some undesirable event will occur. For example, a risk is an unwanted event which may or may not occur. So heart attacks are one of the major risks that affect obese persons. Or, a risk is the cause of an unwanted event which may or may not occur: "A poor diet is the most important health risk in the UK." Risk also has a quantitative sense, where risk is defined as the probability of an unwanted event which may or may not occur. For example, the risk that an obese person's life is shortened by a heart attack is about 50 percent. We also have risk as the statistical expectation value of an unwanted event which may or may not occur. Some purist risk managers regard this as the only correct usage of the term. Finally, risk relates to a decision made under conditions of known probabilities – a 'decision under risk' compared with 'decision under uncertainty'. When there is a risk, there must be something unknown, or something that has an unknown outcome. And so, knowledge about risk is knowledge about lack of knowledge. A decision is made 'under risk' if the probabilities are known and if they are unknown, under uncertainty'. In practice, rarely are probabilities known with certainty. Theoretical risk management discussions of 'risk' – known probabilities – involve tossing coins or rolling dice, where the odds are assumed to be known with certainty. In 'real-life' risk management – and this point is made even more important since the crisis – even if we make a decision based upon what we believe to be a known probability estimate, we are not certain that this estimate is perfectly correct, and so there is uncertainty. For that reason, almost all decisions are made 'under uncertainty'. For practical purposes, risk managers must understand their simplifying assumption of treating risks that they confront in their day-to-day roles as a case of known probabilities, and they must acknowledge that this is an idealisation in risk management theory.

You're saying that beyond a certain point, no one can ever manage all the risks implied by a given scenario.
It is possible that when the differential between uncertainty and known probabilities is multiplied by a large exposure – like a huge and opaque portfolio of mortgage-backed securities – the result may be significant and so violate the simplifying assumption. A major risk management problem highlighted by the crisis is how to deal with the severe limitations of our knowledge of the behaviour of complex systems, such as unfolding contagion, the world economy, and climate change. These systems have many components, each of which may interact with the other in non-linear ways, making them highly unpredictable. Understanding how to make reasonably reliable statements, based on consideration of as many variable as possible, is one area at the frontier of risk management. Another frontier in risk management is the development, implementation and use of artificial intelligence in business decisions and processes.

> "The crisis separated the risk management community into two buckets. There is the bucket labelled 'must do better' and the other is 'can bring enormous value.'"

Now this is a really exciting area, for obvious reasons, although my understanding is that AI's applications are limited at present, despite all of the talk around the potential of the field.
Let's come back to AI, because it's really a crucial aspect of the current risk discussion. Expanding on the frontiers in risk theory, risk management today is setting a new paradigm for applied statistics. The tool kit of theoretical and applied statistics deployed in real-life situations that are not constrained to laboratories, industrial production environments, and the social sciences, is risk management in its current guise. There

> “The advances in technology that are enabling enhanced risk management techniques have at the same time opened up new channels for criminals and cyber terrorists, who form an expanding set of players capable of exploiting the scalability of artificial intelligence to perform ever-larger attacks.”

are many risk management institutions popping up today – take for instance the Institute of Risk Management at Cambridge University – which point towards the formation of a whole new discipline. A new way of thinking about one of the most crucial aspects of human existence, and existence in general. Another thorny problem in risk management is dealing with dependence. The models available today – the Levy process, for instance – are good first-order approximations for more complex dependence structures for which we don't yet have the intellectual tools to describe.

It's an exciting field, albeit a confounding one, and highly technical as well. Wrapping one's mind around the concepts themselves, let alone the mathematics, puts this in a highly academic realm. Clearly though, it's a point of urgency for society to more clearly understand and apply risk management to daily life, forward-planning etc. You mentioned climate change and complex systems earlier, and these are clear and present issues for modern civilisation. What about enterprise risk as a possible cure-all, ultimately? Is it the panacea that it sounds like it could be, or just a cool job title?

I don't think it's a cool title. Some find it really confusing when you already have a Chief Risk Officer. What exactly is a 'Head of Enterprise Risk'?? In all seriousness, I mentioned earlier how a proper implementation of enterprise-wide risk management could have reduced the effect of the financial crisis. Enterprise risk management expands the scope of risk management to every business risk of the firm. You need to think of all these risks and the impact they may have on each other, so you can build a total risk profile. Expansion in the scope of the function even includes things like competitor risk, strategy risk, and reputation risk, as the point of enterprise risk management is not only to identify threats to achieving the firm's objectives, but also opportunities. It is not a panacea and I don't think panaceas can exist by the very nature of an evolving risk environment. There is no 'cure-all', and hoping for one is counter-productive, in business and elsewhere.

Let's face it – there is no 'cure-all' for climate change, given the complexity of the system involved.

Exactly. What you must do is try to reduce the residual risk to a level that is within your risk appetite, and keep it there. One final point I'd like to mention is that to operate an effective enterprise risk management process, you can't just be a 'rules' person, and treat it as a compliance activity. Of course, rules-based compliance and controls have an important role, but you would be deluded in thinking that these are sufficient for an effective enterprise risk process. I know of an example of a Chief Risk Officer at a large firm who had details of someone who displayed a pattern of inappropriate behaviour escalated to him, with all the consequences for reputation risk to the firm. This CRO's course of action was to pass the matter to someone else. He couldn't handle the situation personally, because it wasn't covered in his rules-based approach to risk management. This is not the way forward.

We mentioned artificial intelligence earlier. What advances in risk management is technology enabling, and how are financial institutions making use of this?

Operating efficiency, cost containment and business transformation are some of the key areas where large firms are embracing artificial intelligence in a general sense. Although in focusing on the impact of new technologies on financial institutions, let's not forget that the financial industry has an inglorious past, where innovation has occasionally outpaced the ability of senior managers and boards to keep up from a risk management standpoint, with catastrophic consequences. The advances in technology that are enabling enhanced risk management techniques have at the same time opened up new channels for criminals and cyber terrorists, who form an expanding set of players capable of exploiting the scalability of artificial intelligence to perform ever-larger attacks. Another area that concerns risk managers in relation to artificial intelligence is the potential violation of legal and societal norms. For example, whilst the use of intelligent machines for credit risk scoring has generated benefits, this comes with hidden biases. This is because the train data used is usually based on past decisions of humans. It is possible that algorithms may identify and therefore sustain ethnic, gender and other biases. These biases cannot be pinpointed to a particular line in the code because they are incorporated within the hundreds of thousands of interacting factors used by the learning algorithm. That's a new risk management challenge, rather than an advantage. You might come across similar issues in the recruitment process, where digital hiring systems are making decisions based on previous human-made, and therefore bias-prone decisions. In addition, artificial intelligence systems are notoriously difficult to audit compared to traditional systems, because the underlying conditions that generated the outcome at the time may have changed by the time the audit takes place. This severely limits the auditor's ability to provide meaningful opinions on issues that might arise. Finally, bear in mind, neural networks do not work with literal truths. They use statistical truths. Therefore, risk managers find it difficult to state with certainty that the system will work in all cases. In some real-life / real market applications, this may not be good enough.

It sounds as though the risk manager will not find their role being entirely replaced by robots anytime too soon! What advice might you have for people starting their careers in risk management at this point?

So as to understand what is really involved, I'd recommend a bit of networking and discussion with people in the profession, like me! And prior to this, think about the relevance of your studies. When I was about to enter university, it was possible to have some reasonable belief that the contents of my degree would remain relevant to my career in business after I graduated. This may still be true for some areas of risk management, although given aspects of our discussion, I would suggest budding risk managers consider carefully the influence of robotics, machine learning and artificial intelligence on their area of planned expertise. The pace of progress in our world is curving upwards, give or take some pronounced political risk, and naive 'straight-line' prognoses around the future of work may be way off when reality crystallises.

I agree – it's important to try and manage 'career risk' as far as possible from the very outset, although the world is as dynamic a place now as it has ever been. Tanveer, a fascinating discussion – thank you for your time.

In Conversation with Ann Stock

on her successful career in Internal Audit and Operational Risk Management

Ann Stock is a senior and well-known leader in the Internal Audit field who has spent extensive periods with some of the world's most prominent investment businesses. She is currently a Principal in The Vanguard Group's Internal Audit function with responsibility for Global Professional Practices, having previously covered the firm's international businesses and global corporate functions. Ann joined Vanguard in 2012 from State Street Global Advisors, having previously spent twelve years at Fidelity International, overseeing audit, operational risk and compliance. Ann spent her early career in audit with Legal and General plc, having trained as an accountant with KPMG. Here she shares some of the insights and lessons she has learnt from her career in risk, controls and corporate governance.

"...some audit functions are too focused on ticking the methodology adherence box, thus strangling the natural inquisitiveness of great auditors who might otherwise use their judgement to go the extra step and unearth the critical issues, or make really insightful connections."

Ann, throughout your career in audit, what are the biggest changes you have seen in the discipline?
There have been some significant changes. When I joined the internal audit department at Legal and General in 1987 as a newly qualified accountant, it was a means to an end. It was a way to escape the accountancy profession, as many newly qualified accountants seek to do, to get a foot in the door in industry, and then move on internally to a 'proper' job. Back then, that was the way to do things. Audit was also a department where management could park their less effective staff. Consequently, the perception of audit was not great, and the perceived value that the function could add to a business was negligible. It was seen as a necessary evil, rather than as an integral aspect of a company's infrastructure. Audit is now very much a profession in its own right, and the discipline attracts and retains top talent, both at entry-level and later in executive careers. Boards and management teams now see audit as a strategic partner to the business, and not just for checking of process controls and other housekeeping measures. Moreover, a well-run modern audit function will live up to that reputation.

What have you found most unexpected and surprising about your career to date?
I am continually surprised at the fact that my roles have been so varied and challenging, and that my work is never boring. The fulfilling life of an auditor is one of the best kept secrets of the financial services industry! I was definitely one of those people in audit that was going to get a 'proper job' eventually, which I did after ten years. This was a mainstream accounting role in the finance department, which I hated. I took the first possible opportunity I could to get back into audit! It's definitely a career out of which you can get as much as you are willing to put in. You can be paid for learning and for using your brain power to solve problems. It is also a wonderful function for developing talent, which is a surprise, given it has had a reputation for being a bit dry and uninspiring. As a manager, you can create stretch opportunities for people in your team, allowing them to develop at just the right pace, and you can hone the negotiation and influencing skills of young talent in a safe and supportive environment. The final aspect I have found surprising is that I never expected the amount of overseas travel and international opportunities with which I have been fortunate to have been presented, although it makes perfect sense, because if you're responsible for auditing a given global business, then there's no substitute for going to the places where the business is being done, no matter how far-flung. I can honestly say that as a consequence of my audit career, I have good friends in most financial services centres globally.

You work for a progressive organisation when it comes to leadership culture; Vanguard is known for its commitment to developing its people. What is your

view on current talent management and leadership standards within the audit function?
I'm of the view that audit functions probably vary across sectors and locations in their commitment to talent management, but I think all businesses now recognise the need for top performers in audit leadership roles. In some organisations, audit is a function for 'high flyers' to rotate through, before reaching the top in a business line. A form of Utopia would be to turn this around – to have top talent rotate through business functions to reach a senior role in audit. We are not quite there yet, but I do see a shift with audit being increasingly able to attract talent from the business and offer really good leadership development opportunities. The extent to which audit functions are committed to the investment in talent does vary though, and is often a reflection of both the tone from the top, and the calibre of the head of the function. That person's ability to influence proceedings is a key factor in the audit function's overall talent agenda.

Over the course of your career, what has your experience been of the role and effectiveness of audit committees?
I have seen audit committees that are passive and those that are proactive. The very existence of an audit committee, especially with non-executive directors sitting on it or chairing it, raises the status and gravitas of the audit function. Where audit committees have been most effective is in asking the follow-up questions – asking what is not in the audit report, and what the underlying message of the audit report might be. Although the audit function is independent, audit reports will be subject to 'word-smithing' and 'internal socialisation', and the Chief Audit Executive (AKA Head of Internal Audit) is sometimes just hoping for that clarification question to be asked by an audit committee member. Also, audit committees whose members engage and communicate with the audit team outside formal board meetings will be better informed as to the real day-to-day concerns of the business, and effective in questioning the issues raised at committee meetings. The audit committee also needs to be proportionate in its response to issues, avoiding unintended consequences of heavy handedness and allocating blame. Taking the more combative, destructive approach can in fact increase potential risks, because those issues might be avoided in the next report for fear of another outburst. Finally, oversight and challenge of efficiency and effectiveness of the audit process, and visible, vocal support for the Chief Audit Executive in getting their work done effectively, regardless of the interests of non-independent stakeholders, is critical.

On that last topic, do you agree with audit functions reporting directly to the CEO, or are those days behind us?
I believe that the Chief Audit Executive should report to the Chair of the Audit Committee without question – ideally an independent Chair – and I believe that relationship should involve much more regular contact than simply the quarterly board meetings mandated by regulation. In most places that I have worked, that has been the case, and is very much the norm nowadays. However, the Chief Audit Executive also needs to be part of the organisation's leadership community and therefore they should have a seat at the CEO's table. I certainly think that the days of reporting to the Chief Financial Officer are over, or at least they should be, because the finance function can be a significant source of risk and conflicts with audit, in my opinion. Again, to reiterate – it's important that the Chief Audit Executive's opinions are heard by the CEO, and vice versa, so there should be a dialogue between the two, which could in some cases be characterised by a reporting line.

Have you witnessed the audit function having a directly positive impact on the culture of an organisation?
I have, but it is often a very slow burn, and requires consistent and continuous messaging. Not necessarily through audit reports saying positive or negative things about culture, but through discussion and engagement. Audit is in a great position to identify themes and root causes of issues all the way across a given business, and can see links between functions that might otherwise be missed, and through this, audit can provide a range of insights that might help an organisation to define its culture, and related issues. Substantiating

> "Boards and management teams now see audit as a strategic partner to the business, and not just for checking of process controls and other housekeeping measures."

that, with the right consultative approach, I have seen audit directly bring about improvements to the risk and governance culture within organisations. Having this degree of influence requires that the audit function gains trust and respect through its work, which can be difficult, but once there, audit's influence can be pretty powerful.

Do you sense that most industries are sufficiently engaged with the audit agenda, and sufficiently cognisant of the benefits of a strong function?
It's an interesting question – you often need to strike a balance between the Risk and the Audit agendas, depending on the maturity of these functions. In highly regulated industries – financial services and pharmaceuticals for example – there is strong engagement with audit. I would say there is a geographical difference as well, where financial services regulators have pushed the audit agenda more aggressively (UK, Ireland, Australia, for example) the engagement is much higher.

What do you think audit functions are still getting wrong, and how might they be improved?
I think blindly following the annual risk-based audit plan on a recurring cycle, without raising sufficient questions along the way, is not the most effective way to achieve comfort on key and emerging risks. Audit functions need to be forward-looking, and prepared to be nimble in response to market and internal events. Liaison with, and leverage of, other oversight functions, compliance and risk for example, is a challenging issue, which can always be improved upon, so as to arrive at the most efficient use of resources, and the richest insights on governance for use by business and audit committees. Some of these considerations are simply logistical, but some are political, depending on the firm you're working for. Finally, some audit functions are too focused on ticking the methodology adherence box, thus strangling the natural inquisitiveness of great auditors who might otherwise use their judgement to go the extra step and unearth the critical issues, or make really insightful connections.

What lessons and thoughts would you wish to pass on to the next generation of leaders in audit, based on your experience?
Leaders should look for bright and inquisitive talent with sound judgement. Encourage creativity and challenge amongst your teams, and practice it yourself – the audit function is no longer about testing process controls. Data analytics and 'robotics' will deal with the bulk of that, although bear in mind, you should understand how those tools work too. Nurture those more creative skill sets though, as they will never be replaced by robots! Treat methodology as a 'guard rail', but focus on building trust and relationships across the business, at all levels, and continue to find ways of changing the outdated perception that audit is boring. Audit is exciting, engaging and important!

Well you have certainly done a great job of doing so over the years, Ann. Your success and the quality of the relationships you have developed is undoubtedly inspiring to your team. We wish you all the best for the next phase of your career.

> “We’ll never patch every hole in the boat, but it’s fair to suspect that a lot of wrongdoing and a lot of mistakes will be avoided in future, thanks to stronger, more independent compliance, risk and audit functions across the industry.”

Alex Keetch
Director, Halsey Keetch

Our company

In business for three decades in the City of London, Halsey Keetch provides world-class executive search, non-executive search and advisory services to companies within the financial services industry.

We specialise and have an outstanding track record in the fields of compliance, financial crime, risk, audit and finance.

Halsey Keetch is co-led by Caroline and Alex Keetch, with the support of a knowledgeable team of researchers, administrators, regulatory, HR and executive search professionals.

Our mission has always been to strengthen the governance of the financial services industry through our services, against the backdrop of an intense and challenging regulatory environment.

We are known for our ability to take a holistic view of the connections between different lines of defence.

We successfully manage UK and international assignments for clients of all dimensions, from global leaders to specialist boutiques.

Our culture and heritage is built on values of inspiration, guidance and integrity, and we pride ourselves on being straightforward, thorough and a pleasure to work with.

CONTACT US

We would be delighted to be in contact, either to provide a talent market view, or for a discussion of specific requirements

halseykeetch.com / +44 (0)20 7206 2757 / info@halseykeetch.com

HALSEY KEETCH

Our services

EXECUTIVE SEARCH

Expertise, focus and experience enable us to search for and attract the very best talent in the marketplace for your mission-critical appointments.
Our robust search methodology can equally apply to important and challenging hires from group executive to mid-senior levels.

BOARD-LEVEL SEARCH

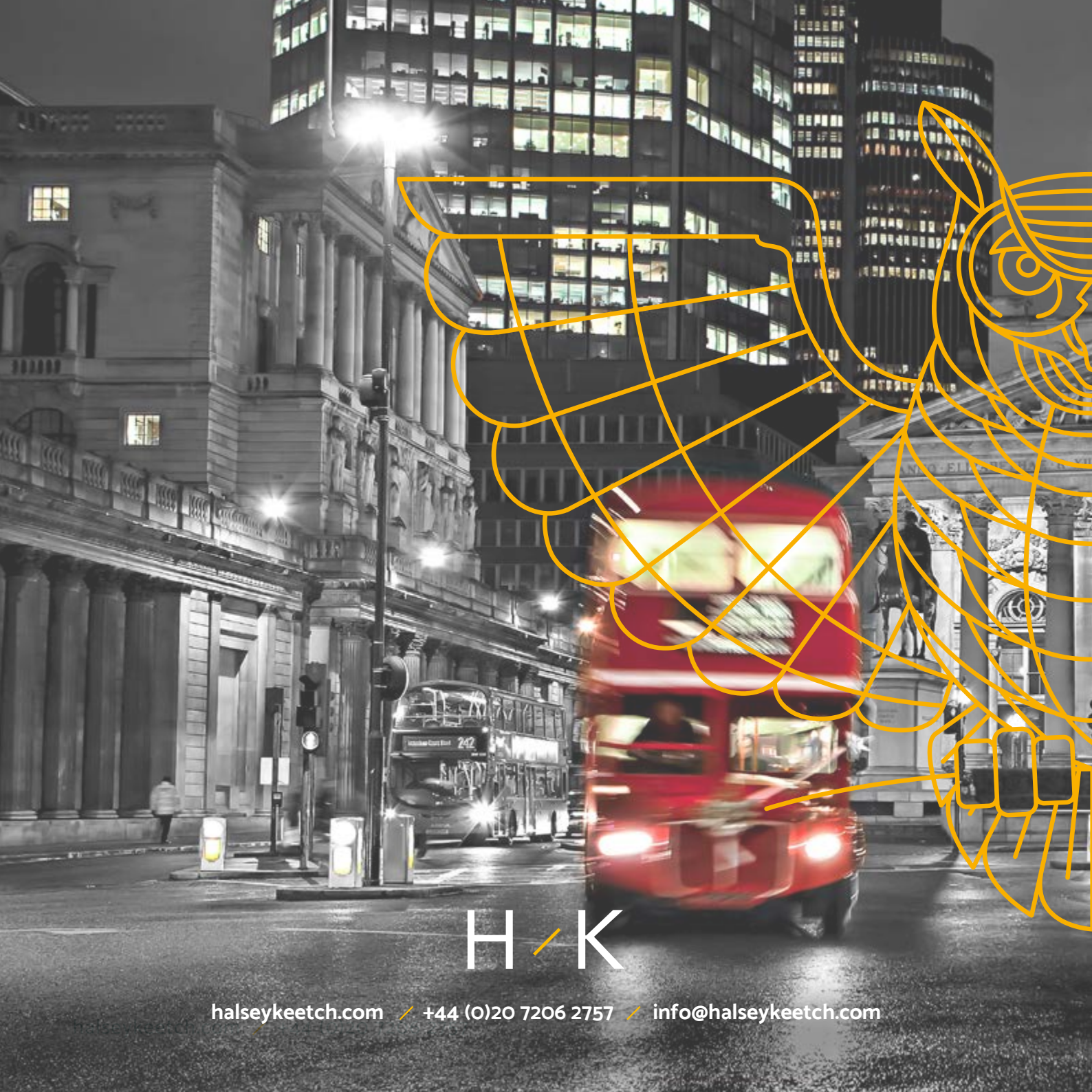
We can help you to identify and appoint the Chairs and Non-Executive Directors needed to keep governance and regulation high on the agenda. Our substantial NED network gives us first-hand knowledge of the market and access to the best solution for your legal entity boards.

MARKET INTELLIGENCE

Our tailored research will provide answers to your questions on executive personnel and organisational optimisation, to ensure you are well-informed when making important decisions. Topics covered include salary and structural benchmarking, talent mapping, and various topical insights.

LEADERSHIP & COACHING

To help you in identifying, assessing, managing and developing leadership-quality talent in your governance functions, we work using a bespoke leadership framework focused specifically on the controls disciplines, with criteria spanning business, leadership, technical and people skills.


H K
halseykeetch.com / +44 (0)20 7206 2757 / info@halseykeetch.com