Diversity & Inclusion: The New Cultural Barometer

A report into the challenges facing financial services around culture and conduct, based on the views and opinions of business leaders across the sector.

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Introduction

Why is New Street Consulting Group interested in this research?

New Street Consulting Group provides agile talent resourcing solutions and support to organisations in regulated markets with a diverse range of people challenges from talent attraction and sourcing to volume assessment and compliance.

New Street Consulting Group is passionate about customer centricity and diversity and inclusion and we believe that the UK financial services sector is facing a wake-up call on culture on conduct.

High-profile media stories have reported sexism and shocking behaviour – and put a piercing spotlight on workplace culture and issues around diversity and inclusion. The FCA, meanwhile, is sharpening its focus on non-financial misconduct and the cultural factors that enable it.

So, what is the reality of the threat to firms? Are leaders aware of, and prepared for, the challenges in front of them? Do they understand what a 'good' culture looks like? And are they doing enough to make cultural change happen? What actions should they take?

This report sets out to answer these pressing questions. Informed by a comprehensive survey of City leaders, it is a timely investigation into behaviour and culture, which highlights diversity and inclusion as the crux of the matter.

Its findings will be essential reading for leaders in financial services and regulated industries – especially those seeking to minimise misconduct risks and reap the benefits that a more diverse, inclusive culture brings.

Contents

Executive summary

Based on a survey of 100 HR, risk and compliance and Board level leaders in firms across the sector, this report investigates the interlinked issues of conduct, culture, diversity and inclusion within financial services.

Reputational damage and FCA supervision pose pressing challenges

Recent media stories have put misconduct and culture in the headlines, highlighting the threat of reputational damage to firms. Concurrently, the FCA is increasing its focus on culture as a 'supervisory priority' and extending its Senior Managers & Certification Regime (SM&CR) powers – for which firms must be prepared.

Leaders are nervous about reputational threats

There is no panic about reputational risk among leaders, but many are concerned about specific threats. Concerns highlighted include: whistleblowing (**57%** of responses) and sexual misconduct allegations (**47%** of responses). **64%** of leaders within firms with over 250 employees cited *"reputation for a lack of diversity"* as the biggest concern.

Firms are largely aware of FCA supervision but not fully prepared

- **73%** of leaders are aware that a senior manager can be held personally liable for non-financial misconduct on their watch.
- **64%** of leaders agree that the new FCA focus on diversity and inclusion is an opportunity to leverage for better business outcomes.
- **48%** of leaders feel that supervision on diversity and inclusion is just another hoop to jump through.
- **75%** of leaders are not fully prepared for the extension of supervision by the FCA on diversity and inclusion.

The FCA is using diversity and inclusion as a cultural indicator

The FCA is not directly measuring or prescribing culture. However, it has highlighted diversity and inclusion as a key indicator they will assess. The regulator believes diversity in people and thinking prevents poor decision-making, risky behaviour and consumer harm, while providing many benefits.

Firms that act now will mitigate risk and gain a competitive advantage

Firms that measure their culture, and do more to promote diversity and inclusion, will be able to demonstrate positive indicators of culture to the FCA. At the same time, they will reduce their misconduct risk and gain the commercial advantages that diverse, inclusive cultures bring.

But firms face challenges in becoming more diverse

Firms cite several challenges, including a lack of senior level role models, retention problems and lack of promotion opportunities. The number one issue is recruitment. **40%** of leaders in financial services say difficulties in hiring is a barrier to increasing diversity.

Recommendations for leaders

- Understand their personal and corporate responsibility relating to the SM&CR right now.
- Recognise the link between healthy corporate cultures and good customer outcomes.
- Identify diversity and inclusion as a key indicator and influencer of a company's culture.
- Take accountability for their working culture and act to enhance diversity and inclusion from the Board down.
- Review hiring practices and approach to improve cognitive diversity, female and BAME representation.

Misconduct, culture and diversity: taking the pulse of leaders

Research purpose, methodology and participants

The findings and analysis in this report are based on independent research conducted by BrightPool in Spring 2019. It canvassed over 100 leaders working in firms (50 to 2,500 employees) across the UK financial services sector.

The research was designed to investigate leaders' attitudes to conduct, culture, diversity and inclusion. Its purpose was to take a snapshot of the current picture in financial services, and establish feelings towards these issues, as well as the interventions by the FCA. The survey questions focused on three specific topics:

1. **Reputational damage:** How concerned are leaders about reputational damage from culture and conduct issues? What are their attitudes towards specific reputational threats?

2. **FCA supervision:** How aware are leaders of the Senior Managers and Certification Regime (SM&CR) and the FCA's supervisory focus on diversity and inclusion? What are their attitudes towards it? How well prepared are their firms for it?

3. **Culture, diversity and inclusion:** How well do leaders think their own companies are performing on culture and diversity? Is promoting diversity viewed as a business benefit or simply a box-ticking exercise? What challenges do firms face in improving diversity?

The survey findings are intended to provide a rounded insight into the factors at play. They help to clarify the challenges leaders face. They also highlight any gaps between how the sector is currently approaching culture versus what it should be doing.

Ultimately, the findings will help to identify the steps that leaders need to take in response to FCA's supervision and wider issues around culture, diversity and inclusion.

Survey methodology and participants

The sample features a 60-40 male female split and is representative of leadership positions and functions across Board, HR and risk and compliance. The survey was conducted independently and anonymously by Opinium Research on behalf of BrightPool in April 2019.

SECTION 1

Behaviour and culture in the spotlight

Reputational concerns

There's an old adage that all publicity is good publicity. In the #MeToo era, that cliché can be consigned to the waste bin. Non-financial misconduct in the City is attracting increased media attention – and the headlines don't make for pretty reading.

The story that kicked off current interest was the FT's investigation into the President Club's dinner published in early 2018.

In July 2018, the topic gained further exposure after the release of a new report from the House of Commons Women and Equalities Committee into sexual harassment in the workplace.[1]

In March 2019, Lloyds of London faced allegations of sexist bullying and poor behaviour. *"Lloyd's of London rife with sexist bullies"* said female employees.[2] Subsequently, numerous opinion pieces on the culture in financial services appeared in newspapers and industry websites.

> **"Many of the hostesses were subjected to groping, lewd comments and requests to join diners in bedrooms elsewhere in the Dorchester."**
>
> Financial Times, 2018

1 Source: https://www.ft.com/content/075d679e-0033-11e8-9650-9c0ad2d7c5b5
2 Source: https://publications.parliament.uk/pa/cm201719/cmselect/cmwomeq/725/725.pdf

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The organisation took immediate action to address issues, including imposing an alcohol ban during working hours. Despite the good intentions by the firm to tackle the problem head on, the introduction of this new policy didn't go down well with employees and contractors. It highlighted how complex the task of 'managing ' culture within an organisation is.

While news stories like these can ruin an individual's career and reputation, the danger of public censure is what should concern leaders. The financial services sector has struggled to re-establish its reputation after the credit crunch, particularly in light of scandals such as LIBOR.

Accusations of sexist behaviour, bullying and a lack of diversity reinforce stereotypes that the public have about 'City' workers. These allegations can drive wider public disillusionment in the sector as a whole and the specific services it delivers.

The damage to the sector has a knock-on effect on all firms working within it. But it is the impact of reputational damage to individual businesses that must be highlighted above all.

In 2015, the European Corporate Governance Institute published a study into regulatory sanctions and reputational damage in financial markets.[3] It found that for UK firms, the commercial impact on stock price reactions are on average nine times larger than the financial penalties imposed by the regulator.

Take a moment to let that figure sink in. Nine times larger. The figure relates to share prices, but non-listed businesses can expect to take a significant hit too. Given the level of risk involved, leaders in financial services simply can't afford to ignore cultural issues, particularly as the stories in the news are just the tip of the iceberg.

Only a small proportion of cases are reported in the media however. In 2018 alone, the FCA cited a **220%** increase in whistleblowing complaints about "*non-financial misconduct*" – covering issues such as sexual harassment, homophobia and bullying, which suggest cultural problems as well as individual misconduct.[4]

The combination of media stories and whistleblowing complaints has sparked the FCA to toughen its stance on behaviour and culture.

Reputation-linked UK stock price reactions are on average nine times larger than the financial penalties imposed by the regulator.

ECGI Report, 2015

Key takeaways

1. The workplace culture in financial services is under intense media, government and public scrutiny.
2. Negative publicity leads to reputational damage and a loss of trust.
3. Reputational damage has a far greater financial impact than regulator fines.

3 Source: https://ecgi.global/sites/default/files/working_papers/documents/finalarmourmayerpolo1.pdf
4 Source: https://www.ft.com/content/27286612-035e-11e9-9d01-cd4d49afbbe3

Reputational risk: what's worrying leaders?

Reputational risk is a real threat to financial services. So, are financial services leaders genuinely worried about this risk? What are their challenges and fears when it comes to culture and non-financial misconduct?

BrightPool's research surveyed HR, risk and compliance and Board level leaders in firms with over 250 employees. They were asked how worried they are about five specific reputational threats. See table below.

Potential reputational issue	Concerned
The company is worried about detrimental gender pay gap figures being published	**57%**
The company is worried about being known for having a lack of diversity in the workforce	**64%**
The company is worried about whistleblowing	**57%**
The company is worried about accusations of sexual misconduct	**47%**
The company is worried about highly publicised scandals like 'Me–Too'	**43%**

Fears or nerves?

Clearly, there is no panic about reputational issues. Yet, it is important to recognise that each issue is at least 'slightly concerning' to at least **43%** of leaders. Perhaps, the best way to describe the way leaders feel is nervous.

It's interesting that leaders are more concerned about being known for a lack of diversity than about scandals and misconduct. This suggests that the majority of leaders have confidence in their own team's behaviour (past and present) – but they are worried about being perceived as non-diverse.

As the survey was undertaken shortly before the latest gender-pay gap figures were released, some leaders were right to be concerned about the issue. The media was quick to highlight the worsening performance of many City firms in this area.

SECTION 2

FCA supervision: awareness, attitudes & preparedness

FCA sanctions and supervisory priority

The FCA began taking a stronger interest in culture and non-financial misconduct in the wake of the last financial crisis.

As the FCA itself says, "*Culture in financial services is widely accepted as a key root cause of the major conduct failings that have occurred within the industry in recent history, causing harm to both consumers and markets.*" [5]

There are two areas of FCA interest that are of most relevance to leaders concerned with conduct, culture and diversity. The extension of the Senior Managers and Certification Regime (SM&CR) and the FCA's announcement of culture and diversity as a supervisory priority.

> **"Our message to firms is non-financial misconduct is misconduct, plain and simple."**
>
> Christopher Woolard, Director of Strategy and Competition, FCA

The Senior Managers and Certification Regime

To tackle potential misconduct, the FCA implemented the Senior Managers and Certification Regime (SM&CR). It is key to the FCA's goal of shifting financial services from a 'compliance culture' to one where employees choose 'do the right thing'.

It applied initially to the banking sector in 2016 and was extended to insurance during 2018. In 2019, it is now being rolled out across the rest of the FCA regulated financial services market.

The SM&RC ensures that senior executives are directly accountable for functions which fall under their responsibility and that they are 'fit and proper'. It also requires firms to explicitly identify the senior manager with responsibility for ensuring that individuals within a wider population of employees – certified staff – are 'fit and proper'. This person is responsible for ensuring their firm takes appropriate steps to assess whether its certified staff remain 'fit and proper' at least annually.

5 Source: Transforming Culture in Financial Services Discussion Paper https://www.fca.org.uk/publication/discussion/dp18-02.pdf

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The regime has the teeth to impose serious penalties and sanctions. Senior managers who hold 'significant influence' over a firm, dealing with its customers or managing its risk, are held personally accountable for any failings within that firm that cause risk or harm to customers. This is in addition to 'corporate' accountability that the firm has itself.

Essentially, this places an onus on individuals to take responsibility for their actions and those of their teams. Given the link between poor behaviours and culture and poor outcomes for customers, it is possible for relevant senior manager(s) to be held personally accountable for cultural and behavioural failings that ultimately cause consumer 'harm'.

The FCA re-emphasised in its Business Plan 2019/20, that it will be *"holding individuals to account under SM&CR when things go wrong."*

In the FCA's judgement, the way a senior manager approaches issues around diversity may be relevant to our assessment of their competence and character.

Interestingly, the FCA has specifically highlighted that *"D&I issues may have an impact on the fitness and propriety of senior managers."* It is sending out a message that non-financial misconduct, including harassment and discrimination, will be examined and possibly punished.

The extension of the scheme is expected to affect over 100,000 approved persons and over 40,000 future senior managers. The lesson is that all financial services businesses and leaders need to understand the Senior Managers & Certification Regime (SM&CR) and how it can affect them.

Potential sanctions

1 FCA authorisation can be removed and leaders can be asked to leave their position if the FCA deems their behaviour unsuitable in relation to diversity and inclusion.

2 If a senior manager is responsible for non-financial misconduct, they can be held personally liable for any material impact or consumer harm it may cause, including censure or financial penalties.

Key takeaways

1. The FCA has clearly stated that non-financial misconduct is misconduct.
2. Under the SM&CR, leaders may face personal penalties and sanctions if responsible for non-financial misconduct in their firm.
3. The way leaders approach diversity issues may be relevant to FCA assessment of their competence and character.

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Awareness of managers' accountability for D&I and FCA supervision

The FCA's statements and expansion of supervision have serious implications for firms and individual employees. It's important to gauge how aware leaders are of the Senior Managers & Certification Regime (SM&CR) and FCA supervision, what counts as misconduct and what the penalties could be.

Awareness of liability

The research asked leaders about the potential consequences of non-financial misconduct under FCA supervision.

73% of survey respondents were aware that if a senior manager is responsible for non-financial misconduct they could be held personally liable for any material impact or consumer harm it may cause, including censure or financial penalties.

That leaves over a quarter of leaders still unaware that serious personal penalties are enforceable.

Interestingly, the figure drops to **62%** awareness that FCA authorisation can removed and leaders can be asked to leave their position if the FCA deems their behaviour unsuitable in relation to diversity and inclusion.

Awareness of non-financial misconduct indicators

Digging deeper into awareness levels, the research determined whether leaders in financial services believed they could be held personally accountable for specific indicators of non-financial misconduct? The answers suggest there is a lack of clarity on the detail of FCA supervision.

Discriminatory hiring and recruitment processes was cited as the most prominent example of non-financial misconduct that senior management could be personally accountable for (**51%** of respondents).

Just behind, **49%** of respondents selected remuneration and incentive structures that promote executive risk-taking or poor conduct.

A perceived tendency for the Board to appoint like-minded individuals or evidence of non-merit appointments was recognised by **44%** of respondents, while evidence that star performers are not penalised for breaching policies and controls came in at **42%**. A lack of open culture for whistle-blowing was the least recognised indicator of diversity and inclusion at **37%**.

The lesson for companies is stop passing the buck around and decide exactly who is responsible. This might mean reviewing the whole diversity strategy or simply clarifying who is taking the lead and then communicating this to the whole organisation.

Key takeaways

1. Most leaders are not linking diversity initiatives to culture and better business outcomes.
2. 40% of leaders in financial services are facing issues with recruiting diverse workforces.
3. 25% of leaders in financial services are struggling to increase female representation on the Board and in senior management.
4. There is some confusion over who should be responsible for improving culture and diversity.

Culture as a supervisory priority

The FCA's Business Plan 2019/20 published in April 2019 reiterated culture as one of its continuing, 'supervisory priorities' for the year ahead. The FCA has again stressed that healthy cultures help firms to make judgements that do not result in consumer or market harm. The FCA believes weak governance or poor culture increases the likelihood of harm and detrimental customer outcomes.[6]

As the FCA explains, "*We expect firms to foster cultures which support the spirit of regulation in preventing harm to consumers and markets. These kinds of healthy cultures can also complement and support businesses' financial performance.*"

> **Given its impact and the role it needs to play in re-building trust in financial services, firms' cultures are a priority for the FCA.**

Released in Spring 2019, last year's plan positioned culture and governance as one of its four FCA supervisory priorities deemed to be of principal risk to financial services consumers. Crucially, in late 2018, the FCA strengthened its view on culture to highlight the issue of diversity, partly in response to both media stories and the increased volume of whistleblowing complaints being reported.[7]

In a speech given in December 2018, Christopher Woolard, the FCA's Director of Strategy and Competition, said "*We've come a long way since the conformity experiments of the 1950s and there's a growing consensus over the need to nurture diverse, open cultures in financial firms and beyond. It should be clear by now that the FCA's interest in diversity is not merely a matter of social justice, but a core part of how we assess culture in a firm.*" [8]

How does supervision and assessment work?

Megan Butler, the FCA's Head of Supervision, says "*Through its supervision of firms, the FCA seeks to ensure that they understand the importance of fostering a healthy culture.*"

It must be clarified that 'supervision' and 'assessment' are not the same as 'regulation'. There is no formal need or way to ensure compliance on cultural issues. In a sense, supervision is a preventative measure. The FCA will be working collaboratively with firms to promote and embed healthy cultures, focusing on its four drivers of behaviour – purpose, leadership, rewarding and managing people, and governance.

The FCA will be asking firms specific questions about diversity during their regular supervisory engagement with those firms. What the FCA is expecting is for firms to demonstrate indicators of a healthy culture, which can be linked to good outcomes to customers. Firms need to take active steps to engage positively with the FCA and show tangible ways in which leaders are fostering inclusive cultures.

The imperative is for firms to ensure they understand their own cultural issues, so that engaging with the FCA becomes a genuinely constructive and commercially beneficial exercise.

> **"It should be clear by now that the FCA's interest in diversity is not merely a matter of social justice, but a core part of how we assess culture in a firm."**
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> Christopher Woolard, Director of Strategy and Competition, FCA

6 Source: https://www.fca.org.uk/publication/business-plans/business-plan-2019-20.pdf#chapter-4
7 Source: Transforming Culture in Financial Services Discussion Paper https://www.fca.org.uk/publication/discussion/dp18-02.pdf
8 Source: https://www.fca.org.uk/news/speeches/opening-and-speaking-out-diversity-financial-services-and-challenge-to-be-met

‘Supervision’ vs ‘investigation’

Leaders should be under no illusion about just how serious the FCA is on this issue. Complaints and whistleblowing could now lead to serious consequences – delivered through investigation and the powers of the SM&RC.

In January 2019, the Watchdog stepped up its probe of Royal Bank of Canada UK’s ‘working culture’. It was reported that the FCA had begun a full-blown investigation into the working culture at Royal Bank of Canada in London. Dozens of former employees complained about their treatment.[9]

While the FCA doesn’t comment on current cases, the press reported that the FCA is *“seeking to determine whether there is a pattern of poor treatment of staff by the Canadian bank, and how it handles internal complaints about employee behaviour.”*

One former employee who met the FCA said it was clear the regulator was seriously scrutinising the bank. *“There was no way this was just a little exploratory chat”*, the person said. *“Every question was culture, culture, culture.”*

“Every question asked by the FCA was culture, culture, culture.”

Key takeaways

1. The FCA supervisory process will now include assessment of a firm’s culture.
2. Supervision is intended to promote and embed good cultures.
3. Misconduct may lead to cultural investigation and penalties.

9 Source: https://www.ft.com/content/5b34240a-14de-11e9-a581-4ff78404524e

Attitudes of leaders in financial services towards FCA supervision

Awareness of course, is just one piece of the puzzle. A more interesting question is how do leaders really feel about the FCA's stronger focus on non-financial misconduct? Is action on culture and diversity something that leaders genuinely buy into? Or is it seen as an unwelcome box-ticking, quota-filling burden?

At first, the findings from the research seem clear:

- **64%** of leaders agree that the new FCA focus is an opportunity to leverage for better business outcomes rather than something to avoid. 13% of respondents disagree.
- **63%** of leaders agree that the FCA taking the stance that "*non-financial misconduct is misconduct*" is a step in the right direction for the financial services industry. Only 15% of respondents disagree.
- **63%** of leaders believe that supervision will be effective at creating more diverse workplaces in the financial sector. Only 9% of respondents disagree.
- **67%** of leaders believe the risk of potential penalties will be the main driver for change in organisations.

Nearly two thirds of leaders have a positive attitude towards FCA supervision on non-financial misconduct. **15%** or less are against. It is interesting to note that leaders believe the risk of penalty will be the biggest driver of change – the threat of the stick seems to be sparking a reaction.

While this is not a resounding endorsement of supervision, leaders are overwhelming more pro than anti. There seems to be a willingness to get behind cultural change and endorse its benefits.

A note of caution, however. Given the generally positive sentiment towards FCA supervision, the following finding is one that stands out:

48% of leaders feel the FCA's focus on diversity and inclusion in its supervision of firms is just another hoop to jump through.

The research findings suggest that only around **15%** of leaders feel negatively about the overall goals of the FCA on misconduct. Yet, at the same time, they are reluctant about having to act within their own organisations. In these cases, mindsets may have to change at senior level, before cultural change can happen on a firm-wide level.

Preparedness for FCA supervision

So, firms are largely aware of increased FCA interest and generally supportive of it. The big question now is whether firms are ready for this increased supervisory focus?

Given the mixed picture on awareness of FCA supervision, it is unsurprising to see how leaders feel about their firm's preparation levels.

Only 25% of leaders in financial services firms say they are fully prepared for increased supervision on diversity and inclusion.

That leaves three quarters of firms who know they should be doing more. The **59%** who are 'slightly' prepared need to start acting fast. The **15%** who are not prepared need to be even faster if they are to genuinely mitigate risk.

It would be interesting at an individual organisational-level to dig deeper into the reasons for this to help firms understand how to plan for any remediation-type actions.

SECTION 3

Culture & diversity in detail: attitudes, barriers and actions

The link between culture and diversity

The FCA is now 'assessing culture'. But it is important to understand what this means in practice. The simplest way to make sense of the issue is to quote the FCA directly.

"To measure culture, we do not attempt to assess mindsets and behaviours directly; instead we recognise that there are numerous drivers of behaviour, many of which we and firms can identify and therefore manage. As a regulator, our focus is on assessing four of these main drivers: a firm's purpose, leadership, approach to rewarding and managing people, and governance arrangements."

The crucial point here is that diversity and inclusion indicators are a measure that the FCA can use. The FCA believes that how a firm approaches diversity and inclusion tells them a lot about its culture. And, the way firms handle non-financial misconduct, including allegations of sexual misconduct will be potentially relevant to our assessment of that firm, in the same way as handling of insider dealing, market manipulation or any other misconduct.

This message was highlighted in September 2018 in a widely publicised letter from Megan Butler, Head of Supervision at the FCA, in response to Westminster's Women and Equalities Committee Report on Sexual Harassment in the Workplace.[10] She said, *"Firms that promote gender diversity significantly lower their conduct risk. And this is where the FCA's interest comes in."* She also added, *"Firms with monocultures suffer* **24%** *more governance related issues than their peers."*

> **"Firms that promote gender diversity significantly lower their conduct risk. And this is where the FCA's interest comes in."**
>
> Megan Butler, Head of Supervision, FCA

10 Source: https://www.fca.org.uk/publication/correspondence/wec-letter.pdf

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This point on monocultures is especially crucial. The Government has already acted on BAME representation on Boards through the 2017 Parker Review, which stipulates FTSE100 Boards must have at least one director from an ethnic minority background by 2021, and by 2024 for FTSE250 Boards.[11]

However, monocultures are not just about the male-female balance, or proportion of ethnic minorities. The FCA is keen to stress that diversity in all forms is important to mitigate the risks of groupthink, false consensus and poor decision-making.

More than this, the FCA wants financial services businesses to see the benefits of diversity for themselves.

Diversity as a commercial imperative - thinking beyond quotas

As the FCA is keen to stress, the debate has moved well beyond diversity as a 'nice to have' – it is now increasingly recognised as a commercial imperative for firms. Cultivating a diverse and vocal workforce is not just a question of mitigating the risk of groupthink – it is also potentially a competitive advantage to organisations.

It's clear that there is a commercial imperative in creating a more diverse, inclusive culture – the power of diversity to help organisations make better decisions, to think in the long-term, to prosper.

Christopher Woolard, Director of Strategy & Competition at the FCA, highlights diversity as a competitive advantage for businesses. He says, "*We need varied life experiences – race, age, social background, sexual orientation, education...the list goes on. True diversity comes when you're open to – and make space for – them all.*" [12]

Leaders need to adopt the mindset that delivering on diversity is a positive thing, not just a way of ticking boxes and mitigating risk. Diversity and inclusion will play a key role in re-building trust in financial services – while supporting individual businesses' financial performance.

Key takeaways

1. The FCA will take into consideration the four key drivers of behaviour that deliver good customer outcomes:
   - Purpose;
   - Leadership;
   - Reward and people management; and
   - Governance.
2. The FCA makes a strong link between diversity and culture
3. Diversity is a commercial imperative that brings benefits beyond mitigating risk.

11 Source: https://www.gov.uk/government/publications/ethnic-diversity-of-uk-boards-the-parker-review:
12 Source: https://www.fca.org.uk/news/speeches/opening-and-speaking-out-diversity-financial-services-and-challenge-to-be-met

Company performance on culture

So, how are firms performing on culture and diversity? We asked leaders to assess how diverse their firms were and whether they see a link between culture and diversity.

Does the financial services sector have a cultural problem? Leaders don't seem to think so.

Survey respondents were asked how they thought their firms were performing culturally, encompassing customs and the working environment. They were also asked about conduct and behaviour – how well employees behave to each other.

- **90%** of leaders believe they are performing well culturally. Only 8% judge their firms to be performing badly.
- **83%** of leaders believe they are performing well on conduct. Only 17% judge their firms to be performing badly.
- **82%** of leaders believe they are performing well on behaviour. Only 17% judge their firms to be performing poorly.

At first glance this finding should be good news. However, this is contrary to current scrutiny of financial services firms by the media, and surge of whistle-blowing incidents reported to the regulator. It would be fascinating to see if the wider workforce shares this confidence in the health of their company cultures.

What are leaders basing their judgement on? Of course, most leaders like to believe they preside over a healthy culture. And in many cases, they probably are. But, is this view based on gut feeling and their own perceptions? Or are leaders using specific indicators and assessments to measure culture?

Firms need to be mindful that FCA representatives with an external perspective may assess culture differently to leaders on the inside.

The importance of diversity in the workplace

Clearly, leaders value diversity in all its forms. However, it is interesting to note where there are gaps between the perceived importance of diversity – and actual level of diversity.

When considering the importance of the diversity among their staff, **84%** think it's important to have cognitive diversity, **79%** think it's important to have diversity in educational attainment and **77%** think it's important to have a diverse age range. Diversity in sexual orientation (**58%**) is considered the least important.

However, when asked how diverse their company is in these following areas there are some conflicting results. For example, while nearly three quarters (**73%**) say diversity of abilities is important, only **47%** say their company is diverse in this area. Similarly, while **79%** say diversity in educational attainment is important only **67%** say their company is diverse in this area.

Cognitive diversity

Financial services has been criticised for encouraging monocultures and groupthink – this is a specific complaint of the FCA.

In his December speech, Christopher Woolard, Director of Strategy & Competition at the FCA said, "*The real nuggets – the perspectives that make you stop and think – come from people who cause you to think differently. To look at something from a new angle or see something in a new light. So, we need to get different voices around the table.*"

But as he warns, "*Deciding to incorporate, say, more women in your team, is not a silver bullet. Because if those women had similar upbringings, went to similar schools and had similar career paths, then it stands to reason that their thinking will be similar too.*"

There is a real danger that firms believe they are cognitively diverse, but in fact their employees are far more similar than they realise or would like to admit. If firms are truly serious about cognitive diversity, they need to attract and retain people who have different ways of processing information and who bring fresh perspectives.

Motivations for investing in diversity

It is valuable to consider leader motivations for improving diversity. Survey respondents were shown a list of reasons for implementing diversity initiatives. They were asked to highlight which of these were reasons for their own diversity initiatives.

These findings will give us a better sense of leader enthusiasm for the benefits of diversity. How many leaders see it as a box to tick? Do leaders consider the importance of diversity in the same way the FCA does?

Reasons for implementing diversity initiatives	
Create a more open and accepting environment	**48%**
Ensure that we remain relevant to everyone in society	**46%**
It leads to better business outcomes	**40%**
Ensure we are an Employer of Choice	**37%**
Aid decision making with a wider range of views and perspectives	**34%**
Greater opportunity to align our business to our customer base	**33%**
Avoid penalties for lack of diversity	**32%**
We don't want to become obsolete	**22%**

There is a key insight to take from these results. The FCA believes diversity leads to healthier cultures and better business outcomes. Yet, less than half of leaders are promoting diversity to create a more open, accepting environment.

Only **37%** are harnessing diversity initiatives to become an employer of choice.

Only 34 % of leaders in financial services are boosting diversity to aid decision-making with a wider range of views and perspectives.

This statistic conflicts with the level of importance leaders claim to put on cognitive diversity). It also suggests that only a minority of business leaders are making the link between culture and diversity.

Only **40%** are introducing diversity initiatives to achieve better business outcomes – while the FCA is clear that diversity is key to achieving better outcomes.

There is a disconnect here that should act as a warning sign for leaders. They genuinely think their organisations are diverse – but too few leaders are linking diversity to culture, and then culture to business outcomes.

Challenges and barriers in increasing diversity

Despite the fact leaders think they are doing well on diversity, the sector does have well-publicised diversity issues, especially with women and BAME candidates reaching senior roles and the Board. So what challenges are companies facing with boosting diversity at every level? And what is holding firms back from becoming more diverse?

Diversity challenges cited by firms	
Attracting diverse new talent to the company	**24%**
Lack of diversity at senior levels	**23%**
Staff turnover	**22%**
Lack of diverse role models across the organisation	**21%**
Lack of internal promotion of high performing diverse talent	**16%**

Barriers to diversity cited by firms	
Difficulty in hiring	**40%**
Lack of diversity at a senior level holding back wider workforce diversity	**24%**
Leadership team are not prioritising making these changes	**22%**
Difficulty retaining diverse employees	**15%**
The company is very set in its ways	**15%**
Speaking out on diversity is not encouraged	**14%**
Resistance inside the business	**13%**

There are two key themes to note here. Issues over recruitment and retention are the primary barrier. Indifferent leadership and organisational resistance combine as the secondary factor in play.

It is a long-term process for firms to drive the cultural change needed to overcome resistance to diversity initiatives, especially when senior leaders are unenthused. However, recruitment is easier to act on, including increasing diversity at senior level where that will have a knock-on effect in the wider organisation.

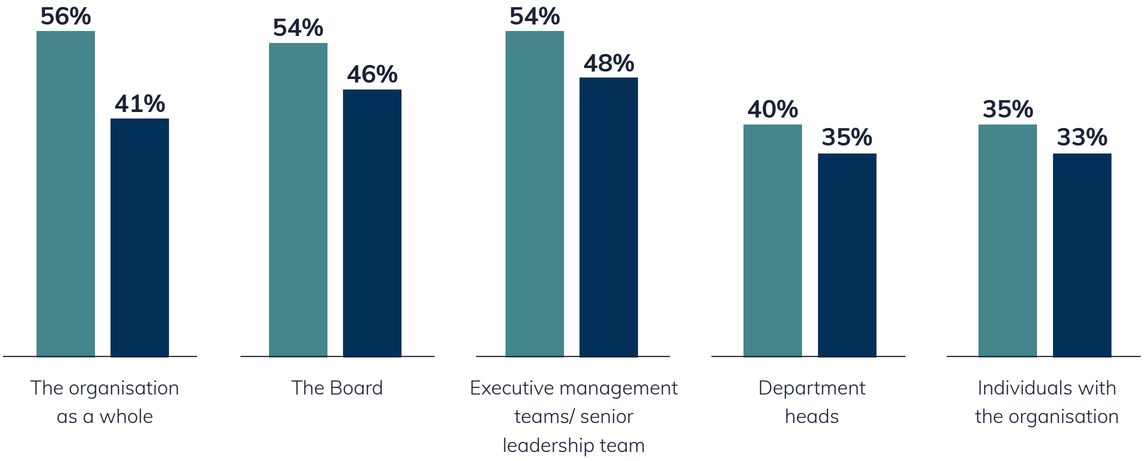
For example, a review of recruitment processes, may find unconscious bias and discriminatory hiring processes. It is often possible to look outside obvious candidate pools. New approaches are available to deliver candidates with cognitive diversity and moral integrity. Succession planning can boost retention and improve the pipeline at senior level.

Responsibility for diversity

For firms to act on diversity, then someone needs to take the lead. But who? Leaders in financial services were asked which group or groups of people should be responsible for promoting diversity. They were also asked who should be accountable for diversity.

This is an important distinction; even more so as senior leaders can be held accountable by the FCA if poor diversity practice happens on their watch. The FCA has warned that leaders could be personally censured or fined.

Which of the following do you think should be responsible for promoting/held accountable for improving diversity, respect and inclusion in the workplace?



What stands out here is a picture of confusion. No-one is quite sure who should be responsible and who should be accountable. It is interesting that only just over half of leaders think the Board and senior team should be responsible and just under half think they should be held accountable.

A third of leaders believe the responsibility likes with individuals – absolving themselves of accountability. The one in five leaders who would like the Government to be accountable may be guilty of wishful thinking.

Of course, there is no escaping the fact that the FCA will hold senior leaders accountable – so leaders need to decide who should have the responsibility and then act on it.

SECTION 4

What does ‘good’ culture look like?

Culture, diversity and inclusion are the central themes to this report. Therefore, before drawing any final conclusions from the research findings, it is valuable to address the culture question.

If firms are to be assessed on culture – then what does a good culture look like? What should leaders be aiming for?

The best way to consider the questions is to look in detail at the FCA’s announcements and language. First, what do they consider culture to be? They define it as, “*The habitual behaviours and mindsets that characterise an organisation.*”

But, as the FCA itself admits, “*We are still left with the question of how to measure it. We also need to ask, given the industry’s diversity, can there be a ‘right’ culture in financial services?*” [13]

The FCA answers its own question with a very clear answer:

“*We recognise that each firm’s culture is different, and appropriately so. We do not believe there should be a ‘one size fits all’ culture and we do not prescribe what any firm’s culture should be.*”

So, there is no single cultural ideal to aim for. The FCA’s position on culture is continually evolving. Indeed, it is reaching out to firms to provoke debate.

“*We want to promote a discussion and consensus on the essential features of a healthy culture and how firms, regulators, employees and customers can help deliver that culture.*”

This still leaves the problem of measurement. The FCA explains its approach like this, “*We do not attempt to assess mindsets and behaviours directly; instead we recognise that there are numerous drivers of behaviour, many of which we and firms can identify and therefore manage.*”

The FCA has identified four key drivers they assess to ensure poor outcomes do not result for customers:

- Purpose;
- leadership;
- approach to rewarding and managing people; and
- governance arrangements.

The FCA does not believe there should be a ‘one size fits all’ culture.

13 Source: Transforming Culture in Financial Services Discussion Paper https://www.fca.org.uk/publication/discussion/dp18-02.pdf

In the FCA's view, the four 'drivers' are manageable aspects of culture. Firms need to demonstrate good practice in all four of these areas. Firms will be expected to take active steps to shape their culture and ensure it is healthy.

So, where does diversity and inclusion fit into this? It should be clear that the FCA's interest in diversity is not merely a matter of social justice, but a core part of how it will culture in a firm.[14]

The FCA believes firms that foster an inclusive and diverse culture can change the behaviour of individuals within that firm for the better. It believes that diversity mitigates against groupthink to prevent poor decision making. More than this, it believes that diversity ensures better decisions and business outputs.

In other words, the FCA is saying that there isn't a single 'good' culture. There can be many 'good' cultures. But, culture can only be assessed positively if it is diverse and inclusive.

Referring to the four main drivers, we can see how diversity and inclusion impacts on each:

- Purpose: A company's purpose is more meaningful, authentic and impactful when it is aligned with diversity and culture.
- Leadership: A diverse leadership group makes better decisions for better business outcomes. Leaders who respect and promote diversity are 'setting the right tone'.
- Rewarding and managing people: Diverse cultures take a fairer and less risk-encouraging approach to reward. When managers treat all employees with respect and seek to harness diversity, better outcomes ensue. When people feel they can bring their whole self to work results improve.
- Governance: Open, inclusive cultures with moral integrity reinforce good governance and controls – and have fewer problems with issues like whistleblowing.

"Those organisations who focus on minimising the disconnect between a customer-led purpose and financial leadership will win the culture race."

Interim COO, Interim Partners

14 Source: https://www.fca.org.uk/news/speeches/opening-and-speaking-out-diversity-financial-services-and-challenge-to-be-met

The FCA may look more favourably on firm's cultures if leaders have taken positive action on diversity and inclusion. For example, in the context of gender diversity, this could include asking firms to demonstrate answers to questions like:

- Is the firm recruiting an even split of female and male graduates?
- Are those female graduates rising through the ranks in equal numbers? And if not, does the firm understand why?
- Does equal pay and the pay gap get attention in the firm?
- Can the firm do more to promote environments that appeal to women and give them confidence?

If leaders can measure how diversity and inclusion has shaped culture and affected business outcomes, all the better.

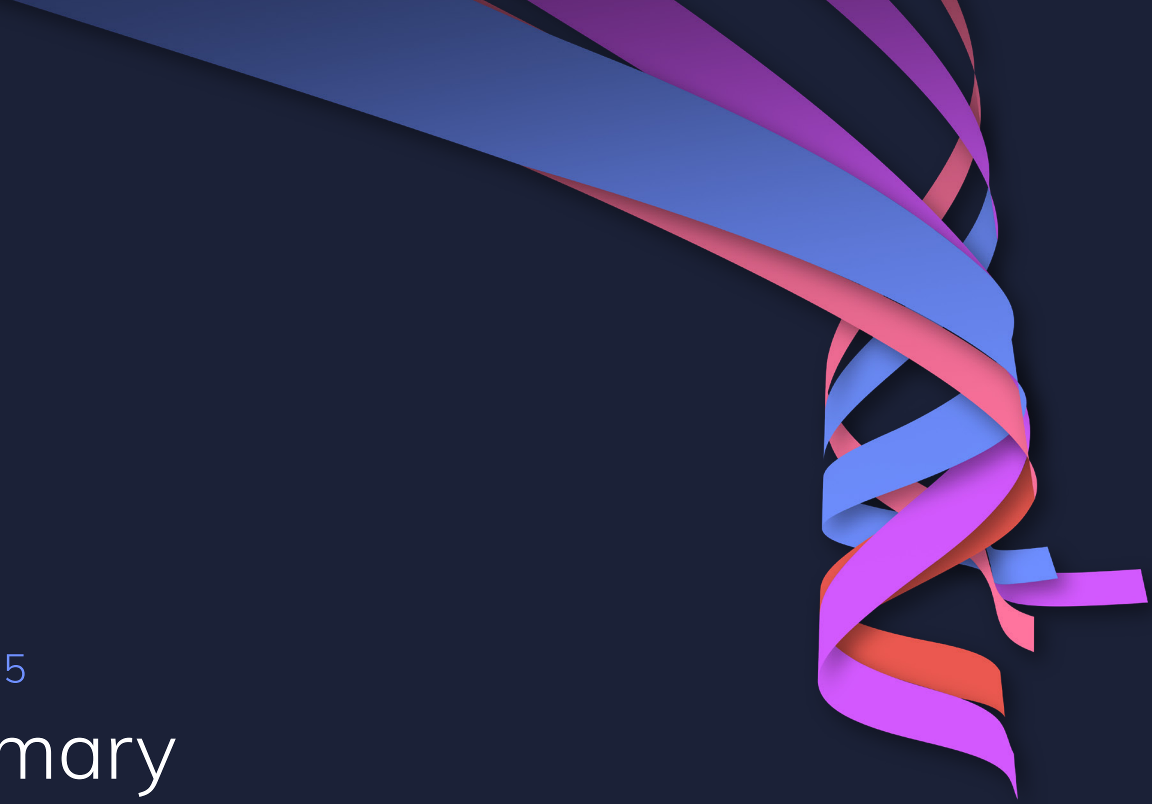
To determine whether their firms currently lie inside or outside of the regulator's desired behaviour, firms should consider a cultural review, including diversity and inclusion assessments.

By deploying a regulatory-aligned framework, firms can assess if they demonstrate positive indicators around diversity and inclusion. At the same time, they will gain the intelligence to evolve and futureproof policies, controls and procedures for dealing with behaviour and conduct.

> **"Any firm looking to up its game on diversity and inclusion would be well advised to look at the FCA's own approach."**

The FCA is passionate advocates for diversity who aim for best practice in their own organisation. Here are the three guiding principles:

- Diversity is integral to attracting and recruiting and developing talent regardless of their seniority or position in the firm.
- Relevant executive committees take strategic decisions on issues affecting equality, diversity and inclusion, with a senior executive level responsibility for taking forward plans and actions.
- All senior leaders have an objective to promote diversity and inclusion within the firm.



SECTION 5

Summary

Culture, diversity & inclusion: key lessons

- Misconduct in financial services is under increasing scrutiny.
- Misconduct is linked to cultural issues within organisations.
- The FCA has culture as one of its supervision priorities.
- There is a disconnect between the attitude of firms and the FCA towards culture and diversity.
- Firms need to understand their culture and find ways to measure and report on it.
- One tangible indicator the FCA will assess is a firm's approach to diversity and inclusion.

Firms that act now on diversity and inclusion will:

- Mitigate the risk of poor decision making, non-financial misconduct and reputational damage.
- Provide a tangible, measurable ways of demonstrating a healthy culture to the FCA.
- Gain a competitive advantage over their peers and improve the outcomes for customers.

Questions for leaders of financial services firms

Given the urgency of the issues highlighted in this report, there are some pertinent questions for leaders to ask about their own organisations. This is by no means an exhaustive list, but it is a sound starting point for considering how your own organisation should react.

Purpose

- Is your organisation's purpose aligned to the diversity of your customer base?
- Is your firm's purpose understood and believed in by all your employees?

Leadership

- Are your employees fully up to speed on SM&CR and FCA supervision?
- Does your firm understand its culture? Do you currently measure and report on the culture of your organisation?
- Can your firm demonstrate to the FCA how senior management behaviours and intentions shape culture and translate into actual good outcomes for customers? For example, do you undertake behavioural assessments in addition to 'internal control' or 'regulatory' testing? If you only measure controls, how do you demonstrate senior management behaviours are driving the right outcomes?
- What is your current approach to diversity and inclusion? Who owns it? How effective is it?

Management

- How recently have you reviewed your recruitment and talent management practices? Can you do more to increase the diversity of your workforce – at every level?
- Are you hiring for cognitive diversity and moral integrity?

Actions for leaders of financial services firms

Ultimately, it is up to leaders themselves to decide how to approach the issues of conduct, culture, diversity and inclusion. These are the most important lessons for leaders to take from our research and analysis. Leaders need to:

- Understand they have a personal and corporate responsibility under the SM&CR right now.
- Treat non-financial misconduct with the same seriousness that financial misconduct merits.
- Acknowledge the danger of reputational risk from non-financial misconduct and scandals.
- Recognise the direct link between a poor corporate culture and bad customer outcome – and between a diverse corporate culture and a good customer outcome.
- Understand diversity and inclusion is a key indicator and influencer of a company's culture.
- Be demonstrably accountable for their working culture and act to enhance diversity and inclusion in their organisations; from the Board all the way down the chain.

Get in touch

If you're interested in exploring the issues raised in this report, or any broader diversity talent issues, come and talk to us. Our diversity and inclusion consulting diagnostic is regulatory-driven and based on conduct and cultural issues.

We can help you to assess positive and negative indicators of diversity and inclusion within your organisation. It's not about process provision. It's about the behaviours, conduct and the environment in which your people are working to best serve the customer and deliver good outcomes.

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