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Good conduct conversations

By Dr. Roger Miles

Facing up to the new reality of conduct regulation

We saw the first stirrings of "behavior-based regulation" as a response to the Global Financial Crisis (GFC) in 2007–2008. Regulators were stung (reasonably enough) by public criticism that predicating compliance reports on value-at-risk had failed to prevent the crisis. Those same regulators and their government sponsors quickly cast around for a new set of lenses they could use to focus on whatever financial practitioners were *actually doing* that they hadn't paid attention to before. Over the next 14 years, the scope and reach of what we now call conduct regulation have developed hugely. Add a recent nudge from citizens questioning certain brands' corporate social responses to the pandemic, the war in Europe, employment practices, and social justice generally.

In 2022, any talk of good conduct in financial markets must now check the context of what regulators are doing collectively. Central banks, securities, and competition regulators in the United States, Canada, the United Kingdom, continental Europe, and Asia–Pacific's (APAC) prime movers in Japan, Singapore, and Australia all now cite practitioner conduct as a focus of their attention. Conduct is now a global regulatory enterprise, with agencies syndicating their efforts to identify and attack the roots of conduct risk. Regulators take aim at many financial firms' legacies of skewed, consequence-blind systems of value and reward, and any casually obnoxious workplace cultures that arise from such compensation cultures. Regulatory agencies and central banks are not only making common cause, but they're also collectively developing and sharing tools and insights: conduct regulators from different jurisdictions talk to each other all the time, compare each other's behavioral research, share notes on effective methods of prosecuting misconduct, and even collaborate on setting levels of penalties.

With the "conduct project" now enjoying coordinated support from regulators worldwide, it is rapidly expanding its toolkit. Prosecutors in some jurisdictions are already using innovative techniques, while their colleagues in other countries watch, learn, and seek ways to adapt these for local use. Techniques and tools including:

- Culture audits
- One-on-one "walkabout" interviews with front-office staff
- Prosecuting new offenses such as greenwashing (which is misconduct because it's lying about your environmental, social, and governance (ESG) credentials)
- Diversity scorecards

- Personal ethics oaths and/or attestations to ethical values and skillsets
- Artificial intelligence–assisted thematic analysis of conversations from "unstructured data sources," such as the social media hangouts Glassdoor, WhatsApp, GoodJobsFirst, and DidTheyCare.com

Faced with increased scrutiny of how they actually behave in the real world, financial industry folks' first instinct is often to reach for one of their trusted panaceas. Typically, they expand the prescribed list of "acceptable answers to audit questions" (written in a nice, 20-page, conduct risk policy); and/or throw a seven-figure sum at a piece of shiny new regtech, or an advisory firm, or both, to make the problem go away.

While none of those responses is *wrong*, they don't directly address the question, "What's the regulator really looking for?" Funnily enough, this is the first question I'm often asked by practitioners attending my classes. So, let's look at that.

What do conduct regulators really, really want?

Amid the haze of legal opinions and policy documents on conduct risk and the attraction of hiring expensive advisers to create these, financial firms often miss a simple underlying truth. Modern conduct regulators are less interested in the details of specific infractions than in seeing how each financial brand can prove it's putting into action its claims to serve a "useful purpose." The earlier, immediate, post-GFC narrative of pursuing misconduct events is now giving way to a broader challenge from industry regulators: If you're claiming that events of misconduct are rare outliers, that must mean, say, 99.9% of the time, you're usefully serving your customers and clients. So, where is your proof that supports this narrative? In short: show us your "exemplary conduct," meaning how it's readily visible and evidenced in day-to-day business practice.

I don't have a problem with this; actually, I'm all for it. Working with banks for more than three decades, I've never bought into the lazy tabloid media trope that all bankers are conspiring in an evil plot against the public interest. In reality, I find the roots of misconduct are less about conspiracy, and more about banal and short-sighted framing of risk controls, reporting designs, and reward structures. To illustrate this, let's look at a recent —but sadly not unusual—experience from my advisory work.

A certain well-respected trade finance house showed me, with a mixture of pride and anxiety for approval, its new conduct risk policy document. They had paid a leading advisory firm a six-figure sum to draft this document, which ran to about 100 clauses of "good conduct practice." The bank's CEO asked me, "Why aren't our staff buying into this? Why are our staff engagement scores in free fall, when all we're trying to do is offer them some guidance to cope with this tricky topic?"

I looked at the document. Of its 100 clauses, 95 were injunctions: don't do this; if you do that, you'll be punished; if you don't do this other thing, you may be committing a criminal offense. And so on.

They'd expensively missed the point—two points:

1. All a conduct regulator wants to see is *evidence that all staff is engaging intelligently* with the topic of "what good conduct looks like around here." Not just at board level (the "senior management functions layer," if you're a Financial Conduct Authority-regulated Brit), but right down through the organization, no longer just tone at the top. How does *everyone* celebrate good service, ask good questions, and enjoy psychological safety so they can routinely call out any casually obnoxious behavior? And on that last point, where's any sign you have a continuing, all-staff conversation, the one that accepts we all want to do the right thing, and we don't have to reach for the nuclear option—whistleblowing—before we start discussing any such topics? (Yes, of course: I get that whistleblowing is a necessary legal protection. But if your first resort for

resolving staff concerns is whistleblowing, obviously you're already too far along a road of misconduct. Where was your earlier intelligence that something might be going wrong? Do you know where the right places are to look for such early signals? Perhaps, do we need to talk about this?)

2. At an even simpler psychological level—hardly a PhD-level insight, really—a habit of framing conduct briefings in negative terms will create the corporate habit of mind that conduct is a topic inherently to be feared. The language we use to describe a thing has a powerful framing effect; that is, our choice of words conditions and reflects how we conceive a given topic. When that topic is firms' behavior in financial markets, as an industry, sadly, we've tended to deploy the language of armed conflict to describe what we're doing: "entrenched position," "corporate raider," "lines of defense," "hostile approach." Even for something as innocuous as your conduct initiative, if you're framing the conversation with words like "compliance" or "lines of defense," don't be surprised if people get anxious: without meaning to, you've told them they should be compliant (i.e., meek) or defensive (i.e., in a crouching posture) about it. For this reason, I never use these words when workshopping anything conduct- or culture-related. Instead, I create a safe discussion space, then start people off on a frank, jargon-free, small-group conversation about "what actually happens around here."

The future of conduct and culture assessment is a simple conversation

This may be one reason banks tend to invite me repeatedly. People—shock, horror—*enjoy* attending a session where they can discuss good behavior freely, on their terms, and without being lectured by a compliance officer.

To reduce this to its simplest terms: Most, if not all, financial services workers are, we'd hope, functional adults. (Yes, there's a smattering of sociopaths, who thankfully don't represent the majority, and whom we can generally spot a mile away.) The functional majority arrive at work wanting to feel they're doing something useful for the customers. They want to work with and for the benefit of others as much as for their own paychecks. Perhaps, dare one suggest, a sense of wider benign consequences—that finance is helping the economy to thrive, and so on.

Is it heretical—especially to *CEP* readers—to suggest: (1) people don't need the compliance function to patronize them with lists of characteristics of good behavior; and (2) this approach is a demotivating way to frame the conversation? The problem I have with (2) is by doing this, no doubt thoughtlessly, the session leader has started the conversation in a place we can all agree is the worst possible tactic: insulting everyone's parents.

Wait...*what* did he just say? Think about this for a second. In childhood, most of us learn to tell right from wrong. You could call this "practical ethics" or just being a socially functional human being. Our inner sense of fairness is usually profoundly tied to our understanding of reciprocity, grounded among family and friends. On the simplest level of starting the conduct conversation, all that should be necessary is to put people back in touch with that inner voice. All of us (OK, maybe not the sociopaths) have an intuitive prompt to "do what's right" that, unfortunately, the command-and-control tendency tends to override when people arrive at work. By overwhelming people with well-meant but clumsy compliance checklists, by "we know best" lecturing, firms' compliance officers all too often succeed in merely switching off employees' intuitive urge to engage in a conversation about what good conduct means to them. Our job, or mine at least, is to switch it on again.

In a perfect world, this really should be a painless intervention. The fact that certain firms' managers perceive speaking up as a threat suggests that specialist psychological insights may indeed add value, on occasion.

The future is walking and talking

This is why the "walkabout" test I mentioned above is so effective, now being trialed among conduct regulators in APAC. It raises a stunningly simple but, for many, disconcerting question: "Tell me about one of those corporate values that you subscribed to on your first day with this firm; now, *show me a piece of work you're doing today that puts that value into practice*."

I love this question because:

1. It's completely jargon-free (unless you count "values" as jargon, in which case, we badly need to have a chat about some basics of corporate communications); and

2. If you haven't already given the question some thought *before* the regulator's case officer appears at your desk to ask it, it's way too late to try to invent an answer on the spot!

This culture audit question is a brilliantly simple test of whether there is any routine conversation about purposeful work and consequences and, "What are we here for, beyond merely rewarding ourselves?" It's also an open-goal opportunity to talk positively about the real-world benefits of your work in financial services. What it's not is an invitation to give a technical definition of "events of misconduct."

Team leaders and senior managers who buy into the new, positive framing of the conduct conversation will see immediate trade-offs. One easy way to roll out this initiative is for senior people to walk the floor and engage staff at all levels in regular, blame-free, unstructured conversations. Think of this as gathering anecdotes about risk culture if it helps. Talk and listen unthreateningly about what we do here, about taking risks wisely, and how we can best work together to improve anything that needs improving.

Through such conversations, leaders can start a whole new level of engagement and commitment to think about "exemplary conduct." Not all that past work of defining "events of misconduct" is irrelevant, but the future is an altogether brighter conversation that engages and enthuses everyone—as long as firms are ready to exercise the cognitive skills needed to grasp it.

Takeaways

- Conduct regulators have moved on. They syndicate globally, commission behavioral scientists, and use artificial intelligence to find misconduct among "unstructured data" in all kinds of social spaces.

- It's not all bad. The financial sector and its regulators are moving the narrative onward—beyond "conduct risk infractions" and toward "exemplary conduct."

- The onus is on *all* your employees to talk about "values in action," celebrate exemplary conduct, and be quicker to call out casually obnoxious behavior.

- Let's speak plainly about good behavior—really, people, we *already know* what it looks like. And let's stop using military metaphors; all that "lines of defense" stuff repels most people.

- Leaders: Walkabout and listen more. Practice saying, "I don't know." Give people credit for being functional adults—let their thinking help to refresh yours.