Culture and channelling corporate behaviour

A joint research project by ACCA and the ESRC

FIVE MINUTES ON...

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The 2008 global financial crisis demonstrated very clearly how regulation and existing corporate governance mechanisms failed to prevent dysfunctional behaviour from spreading and seemingly thriving businesses from collapsing. Corporate scandals and public inquiries continue to make the headlines, from discovery of LIBOR manipulations to the culture of greed and short term profit amongst bankers. As a result, the issue of corporate culture – and its role in both corporate successes and failures – is now an emerging hot topic for business leaders, accountancy professionals, governments and regulators all over the world.

ACCA believes that a healthy corporate culture is a prerequisite of good governance and sound risk management. We think it is also essential for good long-term corporate performance. The human factor in organisations is central to understanding how they function; a firm can comply with generally accepted best governance practice and the letter of regulation, but it is ultimately about the people within, and the decisions they are taking.

This study, conducted in collaboration with the UK's Economic and Social Research Council (ESRC), included roundtable discussions from around the world and a global ACCA members' survey. All affirmed the critical importance of tone at the top in setting the ethical compass for the organisation, and being able to shape and drive a strong corporate culture that channels functional behaviour.

Boards must strive to ensure that their organisations get their culture right, so they get the kind of behaviour they want and avoid the sort of dysfunctional behaviour that causes accidents, destroys value and creates reputational damage. Getting this right is not simple, but this report will offer suggestions to make it easier.

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About the report

In 2013 ACCA and the ESRC launched research into the field of corporate culture with the overarching goal of understanding what causes dysfunctional behaviour in organisations.

Corporate culture and the drivers of behaviour are currently key issues for regulators, particularly of financial services organisations. The Financial Stability Board now expects bank supervisors around the world to assess financial services companies' risk culture, and their starting point will be boards' own assessments (FSB 2014). It is likely that boards in other sectors, private and public, will need to make similar assessments. Boards need better guidance; this study aims to assist, by identifying the leading corporate and academic thinking, and providing a practical and insightful framework to help them understand their own organisational culture.

The report investigates what affects decision making processes and what drives individuals' and groups' behaviour. It brings fresh thinking into understanding and assessing culture in organisations, encouraging boards, executives, regulators and others to consider the inherent trade-offs in measurement, regulation, empowerment, leadership and control.

For the full report: www.accaglobal.com/culture

Highlights from the report

Understanding the interaction between culture, behaviour, ethics and performance is clearly on top of the corporate agenda for business leaders, senior accountants and regulators alike. Many people with whom we engaged expressed despair with what they see as a general tendency to apply quick fixes to deep, complicated and often poorly understood behavioural issues. There is now broad agreement that a much more holistic approach is needed; the purpose of this report is to practically contribute to the current debate over growing (and potentially legally binding) cultural assessment requirements.

CULTURE ISN'T SOMETHING YOU CAN GRAB

The conclusions of the ACCA–ESRC project all pointed to the elusive, idiosyncratic, and highly influential nature of corporate culture. **The culture held by a group is a set of shared beliefs, norms and values that defines what is important and what is appropriate for individuals belonging to this group.** Most of it is out of sight and one can only see the tip of a much bigger iceberg when attempting to assess it.

The main challenge is to obtain sufficient evidence and to do so one must move away from standard quantitative methods, appreciate the ambivalence of the subject, and make sensible use of a range of much more subjective approaches. Asking the right questions and looking at the set of trade-offs developed in this report will help boards in getting to know the culture of their organisation, ultimately driving change where it is most needed.

KNOW THE CULTURE YOU WANT

To get to know the culture one organisation may want, the report suggests that boards start by asking themselves:

1. **What are the goals and purposes of the organisation?**
2. **What sort of behaviours does it wish to encourage and discourage?**
3. **How is the 'tone at the top' set out and conveyed through the organisation?**

These questions can help instigate a discussion in the boardroom, and beginning the process of cultural assessment.

Assessing culture should be seen as a journey of continuous improvement rather than an end in itself. The report advises boards to conduct a health check of their organisation's existing culture using a series of cultural trade-offs. They should then consider a series of actions they might take in order to reconcile the culture that exists with the culture that they want.

UNDERSTAND THE CULTURE YOU HAVE

Our investigations led us to conclude that there is no one size fits all when attempting to assess culture. Even within an organisation, different cultures may exist in different areas and teams. Any assessment should therefore be carried out distinctively at various levels of the organisation.

Finding what is optimum and most appropriate involves considering a series of inherent trade-offs such as about conformity and challenge. These can help map out the kind of culture an organisation wants and has.

They form a framework for discussion and by no means suggest that one end of a trade-off is better or worse than the other. Rather, the aim is to strike an optimum and appropriate balance.

CULTURAL TRADE-OFFS FOR THE BOARD TO CONSIDER	
Values as a wealth driver versus values as a protector	Boards could consider what sort of values they want to have and work with in order to ensure that these values are lived throughout the organisation.
Openness to mistakes versus zero tolerance	Boards could consider whether the organisation is open to hearing about mistakes and whether staff believe there is sufficient openness to constructive criticism.
Leadership versus followership	Boards could consider their own leadership style and find out how it is perceived throughout the organisation. How do the board and CEOs want to lead?
Conformity versus challenge	Boards could consider to what degree constructive challenge is encouraged in the boardroom, find out how cohesive teams are within the organisation and whether staff are able to challenge people above them.
Independence versus involvement	Boards could consider whether external directors are sufficiently independent in mind and sufficiently involved or engaged, and what steps could be taken to improve genuine commitment. The size and composition of boards should also be considered in line with their actual operational and strategic requirements.
Enforcing versus avoiding or exploiting regulation	What attitude to regulation should an organisation have? Does it want to support and work with the spirit and the letter of regulation or does it see regulation as something to be avoided or exploited for its customers' interests or its own sake?
Common sense versus rules and procedures	Boards could consider how to get the right balance between allowing people to use common sense and introducing rules and procedures.
Empowerment versus rules and tight rules versus loose rules	Boards could consider how much empowerment and leverage is appropriate for different groups in the organisation (see also innovation and control).
Quantitative measures versus qualitative performance	Boards could consider whether measures used properly reflect the long-term aims of the organisation and whether they could easily get 'gamed' for personal interest.
Innovation versus control	Boards should be aware that control can stifle innovation. The need to encourage innovation should be balanced against the need to have control; they could consider what sort of innovation they want, where it is needed, and what sort of control is appropriate.
Risk seeking versus risk avoiding	How clear is the board about why its members want or allow their organisations, and the teams within them, to take risk? What is the appropriate balance between risk and reward?
Trust versus accountability	Attempts to increase accountability can erode trust as people who are made more accountable may feel less trusted. Boards could consider whether existing accountability systems undermine trust and what could be done to improve trust.
Profit versus public value	Boards could consider whether they think they have the right balance between making profits and contributing to public good and whether they are anticipating changing societal expectations sufficiently.
Human capital versus human cost	Boards may want to consider how the economic austerity will affect how new talents can be attracted and flourish within the organisation.

TAKE ACTIONS TO RECONCILE WHAT EXISTS WITH WHAT IS DESIRED

As boards health-check the culture prevalent in their organisation, they can take various actions to help reconcile what they have with what they desire:

- Align and embed core values at the very top.
- Watch out for the trickle-down effect and dynamics in groups.
- Track how decisions are being made.
- Be honest about the value of regulation and codes.
- Beware of unintended consequences attached to any incentives structure.
- Find out what motivates people.
- Anticipate trends.

Practical guidance

Assessing corporate culture is difficult. Culture is a dynamic phenomenon and any attempt to measure it may result in catching only half the picture. As an overarching goal, boards should aim at breaking away from pass or fail approaches and remember that there is no absolute or 'right' way to assess culture.

Boards may want to consider the following when trying to get culture right and to channel functional corporate behaviour:

Align and embed core values at the very top.
- Do people who do not 'walk the talk' (act in accordance with the company's stated values) get promoted?

Watch out for the trickle-down effect and dynamics in groups.
- What can prevent the desired tone from being established and maintained? Does the organisation have a whistle-blowing (or 'speak up') system in place that staff believe they could use without fear of retribution?

Track how decisions are being made.
- How aware are decision-making groups, from board level downwards, of the risks of cognitive bias and groupthink? How is diversity of thinking and challenge encouraged?

Be honest about the value of regulation and codes.
- Do management practices drive people to do things that they regard as unethical?

Beware of unintended consequences attached to incentives structures.
- Is it understood how incentives (deliberately created or not) work in practice? Can they be mapped and assessed in relation to the business model and organisational aims? Do they ultimately encourage ethical behaviours?

Find out what motivates people.
- Are incentive structures in place actually fit for purpose? Do they promote long-term sustainable performance or do they encourage immediate self-gain only?

Anticipate trends.
- Is the organisation open to new creative ways of thinking or is it constrained by a fear of the uncertain? How aware of global market trends are management and human resources staff?

Methodology

The project's methodology and evidence included:

- looking at a body of academic literature from different social science disciplines as well as reports and investigations into various scandals and corporate failures (see Appendix 1 of the main report)
- discussions with over 150 people with expert knowledge, from business, academia and regulatory organisations on five continents in roundtable discussions and other meetings; participants included executive directors, chairman and non-executive directors, internal auditors, risk managers, researchers from international organisations and board information consultants (see Appendix 2 for a summary of findings)
- an online survey from among ACCA's global membership in April 2014, with close to 2,000 respondents giving their views on culture, leadership, incentives and motivation (a complete analysis of results will be available by Q1 2015)

This report is supported by three other works:

- ACCA (2014) *Culture and Channelling Corporate Behaviour, Appendix 1: Review of the Academic Literature on Organisational Culture.*
- ACCA (2014) *Culture and Channelling Corporate Behaviour, Appendix 2: Findings from the ACCA–ESRC Roundtable Discussions.*
- ACCA (2015) *Culture and Channelling Corporate Behaviour, Appendix 3: Results from the ACCA–ESRC Member Survey.*

For further details about these works and their publication, visit **www.accaglobal.com/culture**

About ACCA

ACCA (the Association of Chartered Certified Accountants) is the global body for professional accountants. We aim to offer business-relevant, first-choice qualifications to people of application, ability and ambition around the world who seek a rewarding career in accountancy, finance and management.

Founded in 1904, ACCA has consistently held unique core values: **opportunity, diversity, innovation, integrity** and **accountability**. We believe that accountants bring value to economies in all stages of development. We aim to develop capacity in the profession and encourage the adoption of consistent global standards. Our values are aligned to the needs of employers in all sectors and we ensure that, through our qualifications, we prepare accountants for business. We work to open up the profession to people of all backgrounds and remove artificial barriers to entry, ensuring that our qualifications and their delivery meet the diverse needs of trainee professionals and their employers.

We support our **170,000** members and **436,000** students in **180** countries, helping them to develop successful careers in accounting and business, with the skills needed by employers. We work through a network of **91** offices and centres and more than **8,500** Approved Employers worldwide, who provide high standards of employee learning and development.

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About ESRC

The Economic and Social Research Council (ESRC) is the UK's largest organisation for funding research on economic and social issues. It supports independent, high-quality research which has an impact on business, the public sector and the third sector. The ESRC's total budget for 2013/14 is £212 million. At any one time it supports over 4,000 researchers and postgraduate students in academic institutions and independent research institutes.

The ESRC's research makes a difference: it shapes public policies and makes businesses, voluntary bodies and other organisations more effective as well as shaping wider society.

www.esrc.ac.uk