Establishing a Culture of Risk Ownership

Responsibility, Accountability and Outcomes in a post Hayne Royal Commission World

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This presentation has been prepared for the Actuaries Institute Risk Insights Event in September 2018.
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Insurers disgraced by royal commission evidence

12 September 2018

Flogging of worthless life insurance policies laid bare

By John Collett
15 September 2018 — 12:00am

Sorry, not so sorry: how life insurers really roll

By Adele Ferguson
14 September 2018 — 12:00am

Sorry, not so sorry – or maybe not sorry at all.

303,000 crimes in three years: Insurer scrambles at royal commission

By Sarah Danckert
10 September 2018 — 3:46pm

A life insurance company has admitted to 303,000 criminal breaches of the law through its use of pushy cold call sales force that intentionally upset potential customers in the hope they would

ANALYSIS

Banking royal commission has laid bare the financial industry's toxic culture

By Daniel Ziffer
Updated 28 Apr 2018, 10:38am

Prudential Standard CPS 220

Risk Management

#9 … the Board must ensure that: …
(b) it forms a view of the risk culture in the institution, and the extent to which that culture supports the ability of the institution to operate consistently within its risk appetite, identify any desirable changes to the risk culture and ensures the institution takes steps to address those changes;

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#30 … At a minimum an RMS [Risk Management Strategy] must: …
(e) outline the approach to ensuring all persons within the institution have awareness of the risk management framework and for instilling an appropriate risk culture across the institution.

Regulators worldwide including APRA say culture is critically important!

Risk culture

Risk culture - the degree to which an organisation's culture encourages or limits the taking of risks and the opportunities that arise from those risks.

Examples:

"overly complex and bureaucratic decision- making processes that favour collaboration over timely and effective outcomes and slow the detection of risk failings"

"over-confidence, a lack of appreciation for non-financial risks, and a focus on process rather than outcomes."

"A lack of intellectual curiosity and critical thinking about the 'bigger picture' and the full depth of risk issues "

"The customer voice (in particular, customer complaints) does not always ring loudly in decision-making forums and product design. "

Risk Culture and Financial Services

*"History never repeats
I tell myself before I go to sleep
Don't say the words you might regret
I've lost before you know I can't forget."*

N. Finn, Split Enz song History never repeats, 1981

Conduct risk – how well have we served our customers?

- Claims definition proliferation - harder to assess value

- Policy claims exclusions not obvious

- Policies with very low loss ratios

- Companies with "independent" advisers that sell a significant proportion of product produced by their producer-owner

- Advising clients to transfer from defined benefit to accumulation

Our observations of the past 30 years

Challenges and opportunities

1. Independence doesn't exist as we have perceived it.
2. Individuals ethics are both an input to and outcome of effective culture
3. Structures, processes and systems intended to drive good outcomes can actually do the opposite
4. Failure of leadership has significantly contributed to failure of organisations
5. Unconscious biases and exploitation of known behavioural biases in finance lead to less fair outcomes

1. Independence doesn't exist as we have perceived it

2. Individuals ethics are both an input to and outcome of effective culture

"Sincerity is the key to success – once you can fake that, you've got it made" – Groucho Marx

"What you do speaks so loud, I cannot hear what you say"
- Ralph Waldo Emerson

2. Take Responsibility

" It is not our abilities that show what we truly are, it is our *choices.*"

- Albus Dumbledore

3. Structures, processes and systems intended to drive good outcomes can actually do the opposite

4. Failure of leadership has significantly contributed to failure of organisations

Leadership Failures

- Complacency

- Myopia

- Lack of independence

- Stuck in the past

Some client experiences

" Risk is YOUR priority, its not on my performance objectives"

" The problem was caused by my predecessor. Its not my problem"

"Risk don't get that we need to have commercial outcomes, and my job is to ensure those outcomes"
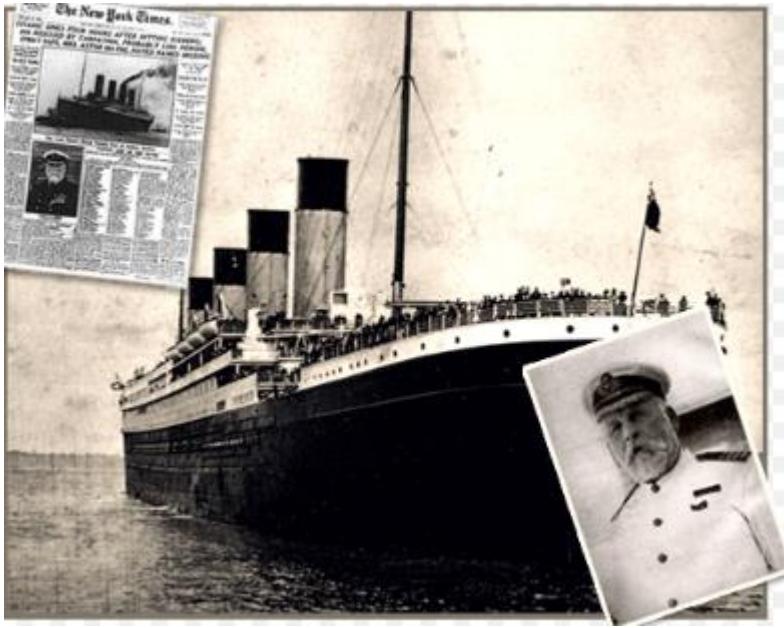
"I didn't realise that my changes would affect other areas"

5. Unconscious biases and exploitation of known behavioural biases in finance lead to less fair outcomes

"Everyone is a prisoner of his own experiences. No one can eliminate prejudices - just recognize them."

Edward R. Murrow

Expertise bias

"I cannot conceive of any vital disaster happening to this vessel. Modern shipbuilding has gone beyond that." - Captain EJ Smith (Captain of the Titanic)

Slow down and pay attention – when do you automatically assume and judge?

Be curious - seek out different views and perspectives, seeing everything different as an opportunity to learn, observe!!

Value and acknowledge difference – create and encourage an environment that recognises importance of diverse views and challenging the status quo

Lead with Empathy - imagine what another person might be thinking or feeling

"How can I address my biases if I don't know that I have them?"

Be Transparent about what you are thinking and how you make decisions (share the why)

Highlight positive role models to counter-balance negative stereotypes

Set clear intentions before making decisions - tell yourself what you intend to achieve. For example, setting clear criteria for role selection

Apply many small acts of encouragement (opening doors to opportunity, gestures of inclusion and caring, and acts of respectful listening)

How culture works

How Culture Works

Inputs : Purpose, Vision, Mission, Values, Strategy

We are currently here:	Levers for Building Adaptive Capacity	We know we need to be here:
Current Culture *Lived Values, Actions, Beliefs and Assumptions*	**Individual** Leadership, mindsets, competencies, behaviours, decisions & actions **Social** Ways of working, relationships, organisational stories & beliefs, events, stakeholders **Structural** Organisational infrastructure, strategies, structures, processes	**Aspirational Culture** *Desired Values, Actions, Beliefs and Assumptions*

Outcomes : Societal, Industry, Organisational, Collective, Individual

"We cannot solve our problems with the same level of thinking with which we created them"
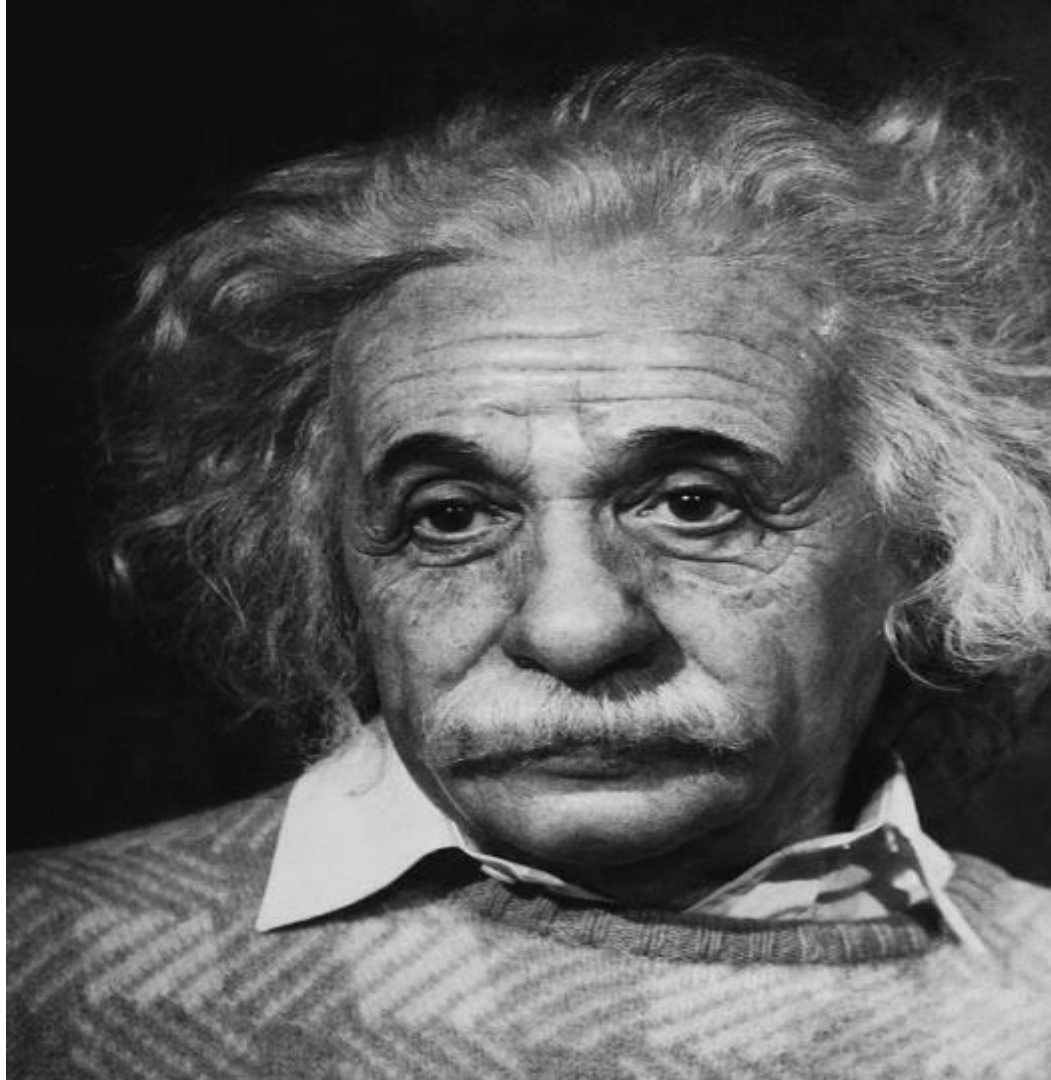
Pop Quiz

When you have been through a transformational change in an organisation, where has your organisation focused its attention:

- **A.** Structural evolution – transforming processes, systems, structures and planning cycles that enhance ways of working and better enable the organisation's aspirations

- **B.** Social evolution – transforming communication channels and forums to enable better dialogue and respectful challenging of ideas across the organisation, to leverage innovation and creativity

- **C.** Individual evolution – building deeper awareness and insight at an individual level to increase responsibility, accountability and capacity to be responsive and adaptive
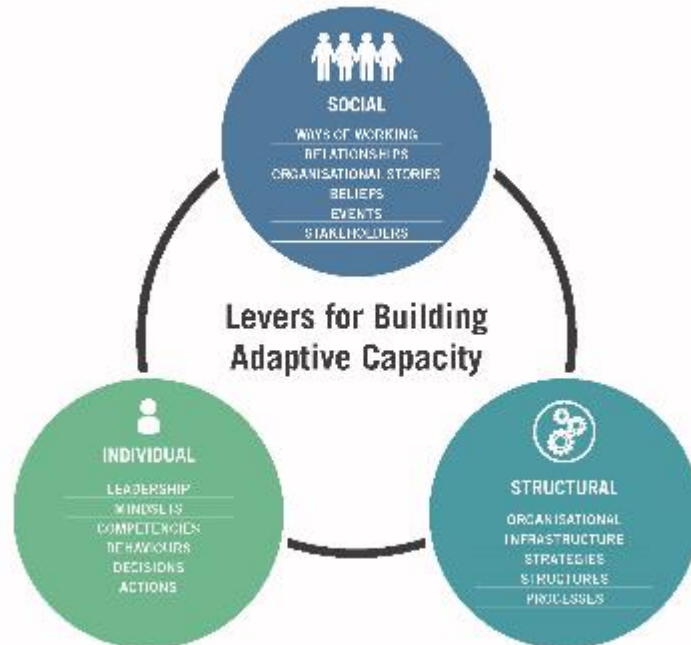
Pop Quiz

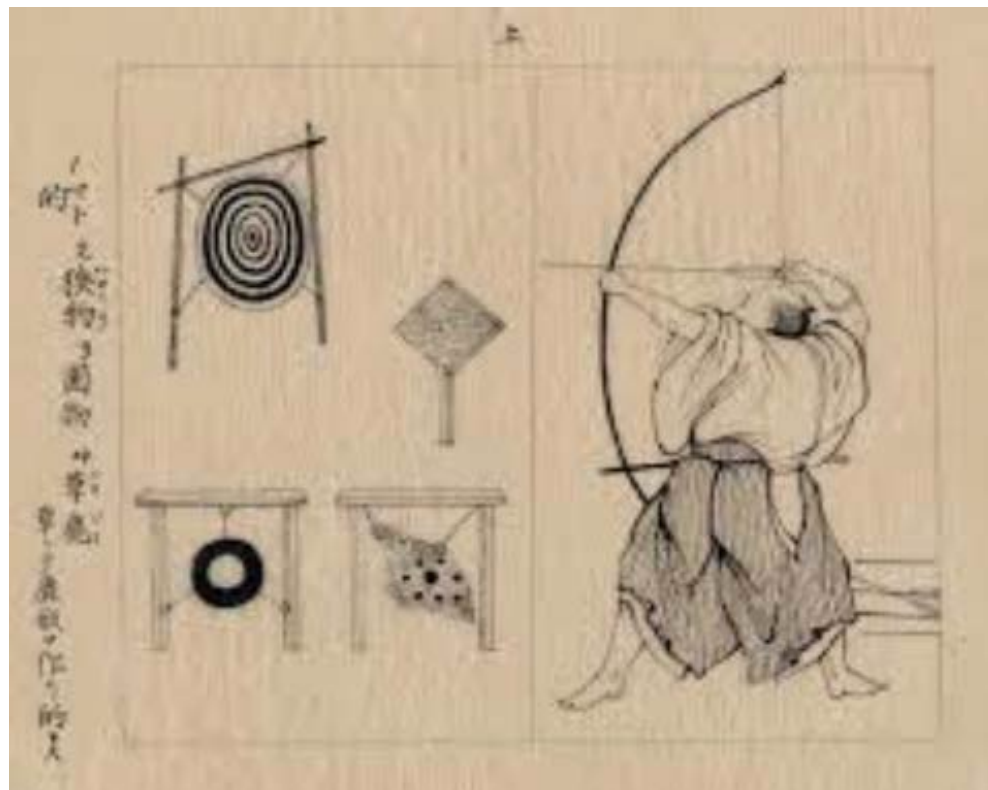How successful was the cultural transformation?

From your answer above, were there any missing ingredients and what was the consequence of this?

Conclusion

From the interviews and case studies we have conducted across a wide range of organisations and our own experiences working with culture, we believe that engaging all **three** (a, b and c) is the only viable option to be able to achieve sustainable cultural evolution.

Establishing an effective risk culture

Levers for Building Adaptive Capacity

SOCIAL
WAYS OF WORKING
RELATIONSHIPS
ORGANISATIONAL STORIES
BELIEFS
EVENTS
STAKEHOLDERS

INDIVIDUAL
LEADERSHIP
MINDSETS
COMPETENCIES
BEHAVIOURS
DECISIONS
ACTIONS

STRUCTURAL
ORGANISATIONAL
INFRASTRUCTURE
STRATEGIES
STRUCTURES
PROCESSES

Form follows consciousness

The quality of results produced by any system depends on the quality of awareness from which people in the system operate. The formula for successful change is not 'form follows function', but 'form follows consciousness'."

Otto Scharmer

Taking responsibility

No single drop of water thinks it is responsible for the flood

Effective Risk Culture initiatives #1

Risk Culture initiatives	When this is effective	When this is ineffective or detrimental	Mitigation / Improvement Required
Train & educate for awareness, skills, knowledge, ethical behaviour	Increase awareness Set clear expectations Improves knowledge	Complexity and hard decisions Can create complacency Outdated quickly	Identify unconscious biases, cognitive limitations and consequent risks
Additional internal risk or compliance roles	Symbolic importance of risk management Greater oversight	Outsource responsibility for risk to the compliance team Don't see risk as my role Quality vs quantity of resources	Partnership between risk and business Responsibility mindset and awareness of how behaviours influence others, impact on culture.
Risk culture assessment	Openness to feedback Identifying gaps External perspective	Limited scope Only measures outputs rather than root cause	Culture of learning and feedback Forward looking indicators / warning signals
Leader role modelling (lead by example)	Highly respected leaders Role modelling is genuine Tone from the top AND Tune from the middle	Role modelling is not consistent Cultures / individuals that aren't influenced by leadership	Zero tolerance for senior leadership inappropriate risk behaviours Authority to hold individuals accountable, set strong boundaries
Communication	Focus on success Focus on learnings Regular reinforcement	When not aligned with reality (often just focus on positives) can create cynicism	Realistic and optimistic - share the challenges honestly AND share the progress. Acknowledge appropriate risk behaviours

Effective Risk Culture initiatives #2

Risk Culture initiatives	When this is effective	When this is ineffective or detrimental	Mitigation / Improvement Required
Independent reviews	When truly independent Fresh pair of eyes can identify blindspots	Not truly independent / reviewer is subject to influence of reviewee / dilutes message Can only go so deep	Independent body (e.g. regulator) assign independent reviewer Roles with dual reporting lines – to regulator and to organisation
Internal Control Registers	Provides internal authority Genuine independence of person signing off - Internal Control Registers	Seen as a tick the box Pressure to sign off Focus only on my patch; narrows thinking	Include regular "risk deep dives" Consider systemic risks and consequences of your actions for other areas
Recruit for desired risk behaviours	Increases awareness of risk culture focus Builds right capability	Past experience is not always indicator of future behaviour	Recruit based on mindsets and values as well as experiences / behavioural attributes
Incentives / punishments	Identify behaviours and outcomes that organisation really values	Punishments not enforced Conflicting incentives Unintended consequences Incentivises self interested behaviours	Rethink incentives! Zero tolerance for obviously bad behaviour Symbolically remove 'rogues'
Include risk as part of strategy sessions	Signal that risk is also about opportunity Encourages enterprise approach	If risk is rubber stamped / glossed over	Include a 'risk advocate' in strategic conversations, NOT someone from the risk function Mindset that risk creates opportunity AND must be managed effectively

What stage of Risk maturity is required?

Maturity level→ Item	Unaware	Reactive	Mechanical	Pro-active	Mature risk culture
Beliefs / mindsets	Risk management is just a concept	Risk management received with cynicism, a management whim	Importance of risk management accepted	Actively aware of and owns risk as part of work	Risk = opportunity
Organisational attitudes	Individuals blamed when risks eventuate	Must eliminate losses; very top down approach	Workforce more involved but with limited understanding	Workforce involvement promoted, though team leaders still take responsibility	Partnership between management and workforce; shared responsibility
Individual behaviours	Takes many risks without realising it, blissful ignorance	Meets minimal legal compliance reqmts; Ignores until reporting time	Day to day risks are managed effectively	Regular discussions on risks, active prioritising to manage risks	Workforce drives risk assessment, shares insights across business
Systems / structures	None, no communication or training	Compliance reports, detailed reviews of failures	Performance management systems. Risk dashboards	Active feedback loops, actions beyond reporting	Culture reviews. Employee perception surveys. Behaviour based training
Risk function	None	Compliance function. Influences through authority.	Function accepted, carries out organisation reviews, focus on improving procedures	Partnership with management, compliance at business line, influences via relationships.	Risk function co-operative and supportive as managers and teams take responsibility. Forward looking.

Moments of Transcendence

Chief Risk Officer Perspective

"The Regulatory direction and the findings of the Royal Commission mean that the role of the Chief Risk Officer is quickly heading towards becoming the Chief Cultural officer"

– quote from a client in a financial services organisation

Discussion – Q & A

- What do you notice in your organisation or client organisations that inhibits effective risk cultures?

- What questions do you have?

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