

# THE ROLE OF CULTURE IN GOOD CORPORATE GOVERNANCE

Professor Blanaid Clarke

McCann FitzGerald Chair of Corporate Law

*CUCC, Compliance Through Communication* (18 August 2015)

A person's values work even  
when no one is looking.

And most of the time at work,  
no one is looking.

-S. Killingsworth

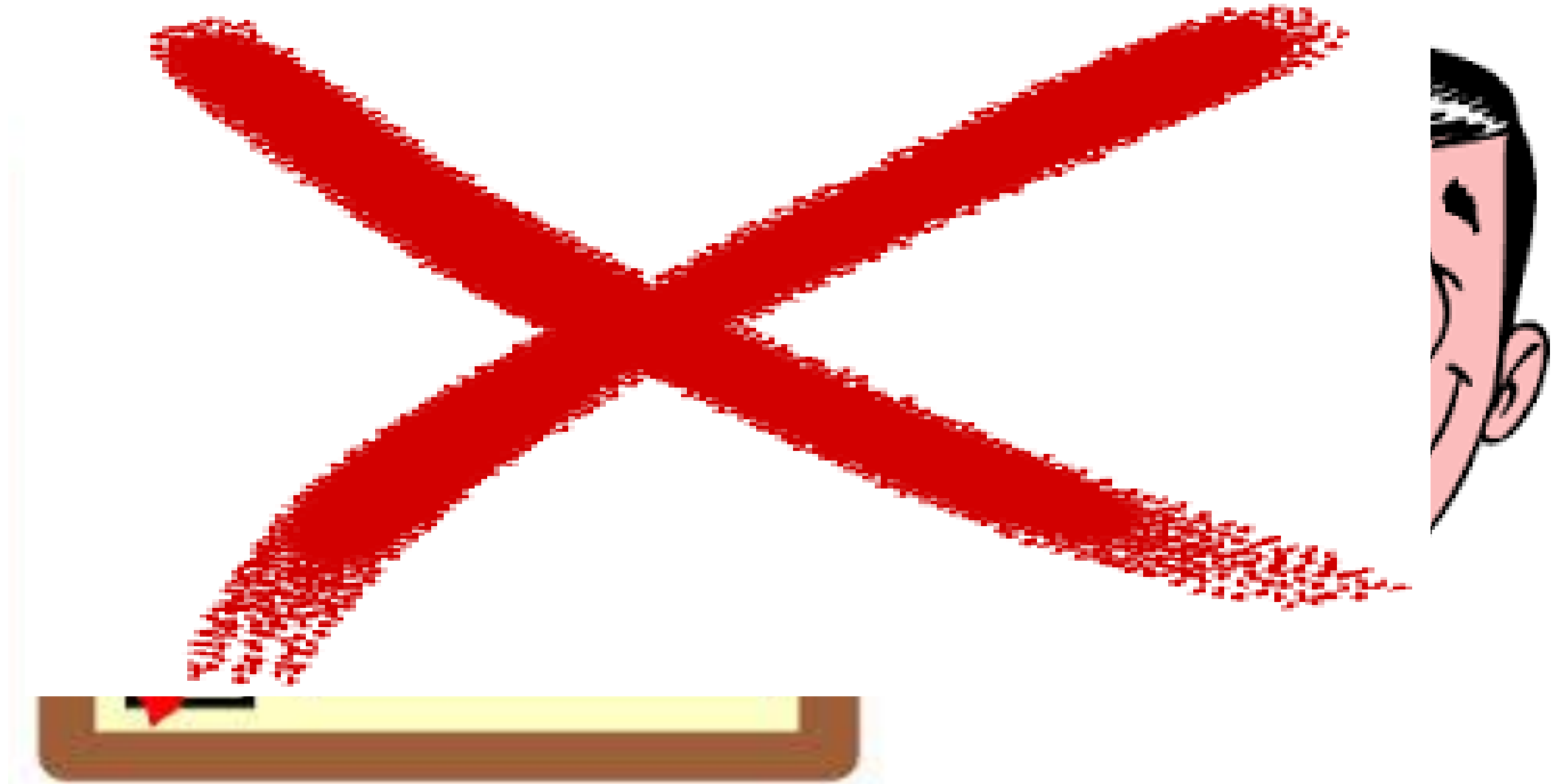


# "Organizational Culture"

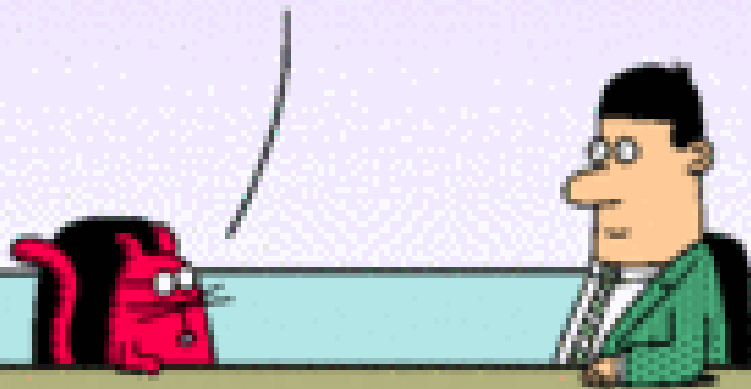
**"A set of norms and values that are widely shared and strongly held throughout the organization"** (O'Reilly and Chatman)



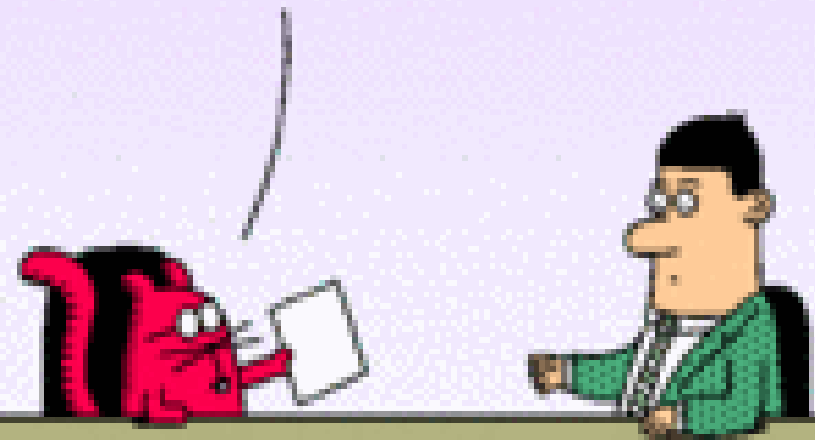
# 10 Easy Steps to being a Better Person



THIS COMPANY IS  
LIKE A FAMILY. OUR  
CULTURE IS BASED  
ON TRUST AND  
RESPECT.



NOW SIGN THIS  
DOCUMENT THAT SAYS  
WE CAN TEST YOU FOR  
DRUGS AND SEARCH  
YOUR COMPUTER AND  
YOUR OFFICE.



scottadams@aol.com

www.dilbert.com

© 1999 Scott Adams. All rights reserved. Dilbert is a registered trademark of Scott Adams.

Presentation considers:

# The Role Of Culture in Good Corporate Governance

“Culture,  
more than rule books, determines  
how an organization behaves.”

- Warren Buffett

Culture is the “underlying values, beliefs, attitudes and expectations shared by the credit union and its officers against which decisions are made and behaviours are formed” (CUCC Compliance manual)

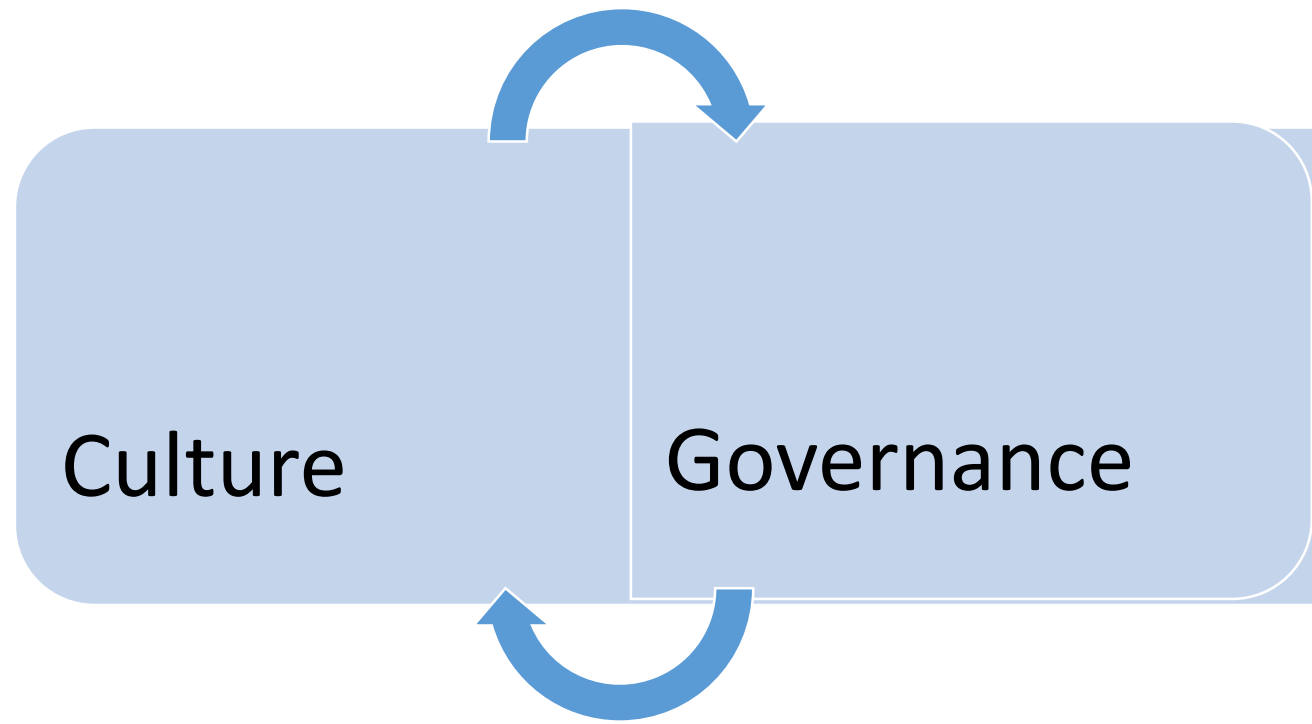
.

“Culture,  
more than rule books, determines  
how an organization behaves.”

- Warren Buffett

**...But an Appropriate Regulatory Framework is  
Required to Encourage and Support the  
Development of an Appropriate Culture.**





Does Corporate Governance Model in Credit Unions Encourage and Support Organizational Culture?

- Risk Management & Compliance Culture – Previous Presentation
- **Board Structure**
- **Role of the Board**
- **Functioning of the Board**

# Definitions

- **Corporate Governance** describes:
  - **“The procedures and processes according to which an organisation is directed and controlled (OECD)**
  - **“How a company is managed in terms of the institutional systems and protocols meant to ensure accountability and sound ethics.” (Financial Times)**

# Changing Models of Corporate Governance



Cadbury  
Corporate  
Governance  
Code (1992)



Sarbanes-  
Oxley Act  
2002



**Avalanche of Reforms**  
in Statute (eg Dodd-  
Frank, CRD IV), Code  
(eg UK Corporate  
Governance Code,  
Central Bank CG Code  
for Credit Institutions  
and Insurance  
Undertakings),  
Recommendations  
(EU Recommendation  
on Remuneration) etc

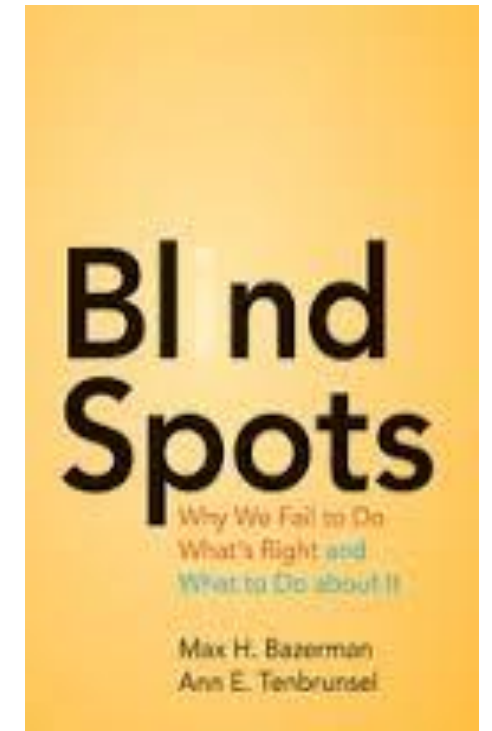
# Governance in Credit Unions

**Legal Requirement** for a credit union to have **governance arrangements** which ensure “effective **oversight** of the activities of the credit union, **taking into consideration the nature, scale and complexity of the business being conducted.**” - s.66A(1) The Credit Union Act 1997 (as amended by The Credit Union and Co-operation with Overseas Regulators Act 2012)

- “The issue of governance of credit unions is at the core of strengthening the regulatory framework and setting out a strategy for the future evolution of the credit union sector.” - Report of the Commission on Credit Unions (2012)

The nature of the decision-makers and the manner in which decisions are made are core aspects of corporate governance.

Research into the heuristics in human decision-making is relevant as is Behavioural Ethics



# Gap between Reality and our Perception of Reality





Research in behavioral ethics has shown that an individual's morality is highly dependent upon situational and social pressures and less attributable to stable personality traits than formerly believed



# Corporate Governance Framework Must Acknowledge and Respond to Challenges to Ethical Behaviour including

- Group Dynamics
  - Misuse of Power
  - Time Pressure
  - Conflicts of Interest
- 
- Judgmental heuristics eg Over-Confidence, Motivated Blindness, Small Beginnings, Rationalization, Incrementalism, Anchoring and Framing



**Ethical  
Fading**

See: Killingsworth “C” Is for Crucible: Behavioral Ethics, Culture, and the Board's Role in C suite Compliance”  
Khaneman and Tversky “Judgment under Uncertainty: Heuristics and Biases”



# Indicators of a Sound Risk Culture

Source: Financial Stability Board (2014)<http://www.financialstabilityboard.org/wp-content/uploads/140407.pdf>

## **Tone From the Top**

- Leading by example
- Assessing espoused values
- Ensuring common understanding and awareness of risk
- Learning from past experiences

## **Effective communication and challenge**

- Open to alternate views
- Stature of control functions

## **Accountability**

- Ownership of risk
- Escalation process
- Clear consequences

## **Incentives**

- Remuneration and performance
- Succession planning
- Talent development

## Tone from the Top

- “The **board and senior management** are the starting point for **setting the financial institution’s core values and expectations for the risk culture** of the institution, and **their behaviour must reflect the values being espoused**. (The Financial Stability Board Thematic Review on Risk Governance)
- Board has “responsibility for the general control, direction and management of the credit union”(s.53(1) 1997 Act)

# Functions of the Board under 1997 Act include:(s.55)



- Strategy setting, reviewing and monitoring the strategic plan and its implementation; **exercising appropriate oversight over execution by the management team of the agreed strategies, goals and objectives;**
- Risk: regularly reviewing and approving all elements of the risk management system
- Appointment & Performance Review of Key Personnel: eg manager, risk management officer and compliance officer

# Functions of the Board under 1997 Act continued

- Policies & Processes: approving, reviewing, and updating, **all plans, policies and procedures** of the credit union, including: lending policies; investment, liquidity, asset & liability and reserves management policies; **standards of conduct and ethical behaviour for officers; remuneration policies** and practices; **compliance plan and policies; risk management policy; conflicts of interest policy;**



Incentives



Communications

# Composition of the Board of Directors under 1997 Act

- “Sufficient **number** [7,9 or 11] and **expertise** to adequately oversee the operations of the credit union”
- **Role of nomination committee** in appointing directors and the requirement to consider the balance of skills, experience and knowledge on the current board of directors and any review undertaken under subsection (11)
- Annual **Board Assessment**

# Composition of the Board of Directors continued

- Directors must have sufficient **time** to devote to the role and responsibilities of director



# Composition of the Board of Directors continued

- **Eligibility:** list of excluded persons eg. Employees, Commission member, adviser
- Directors (and officers) “shall at all times ensure that individually, and collectively when acting in that capacity, they act in a manner **free from conflicts of interest**”
- **Rotation:** election every 3 years (maximum service of 12 in 15 years)



# Statutory Responsibilities of the Chairman

- ensuring that meetings of the board operate in an efficient and effective manner;
- **encouraging constructive discussions and debate at board meetings;**
- **promoting effective communications** between board members and between the board and the management team;
- **causing the agenda to be set** by the secretary and chairing board of directors meetings;
- ensuring that the nomination committee fulfils its responsibilities;
- conducting annual **performance evaluation** of board members;
- assisting the board oversight committee;
- **ensuring that conflicts of interest are appropriately managed** by the board and individual directors



“In deciding on the roles, responsibilities and administrative structures and reporting relationships of all officers, the board ...shall ensure that **no single person is responsible for making all of the material decisions** of the credit union or has effective control over the business of the credit union.” (s.55(2))

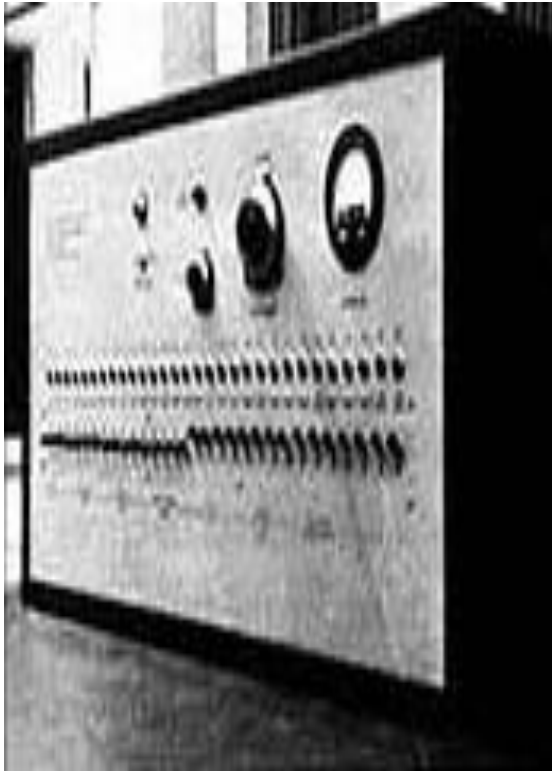


# Heuristics

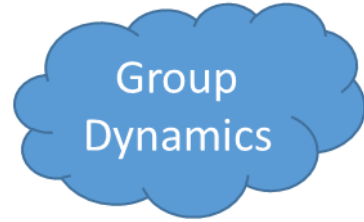
Framing

Small Beginnings,  
Rationalization and  
Incrementalism

## Milgram (1974)



# 8 Symptoms of Group-Think (Janis 1977)



## I: **Overestimations of the Group**—its power and morality

- *Illusions of invulnerability* creating excessive optimism and encouraging risk taking.
- *Unquestioned belief* in the morality of the group, causing members to ignore the consequences of their actions.

## II: **Closed-Mindedness**

- *Rationalising warnings* that might challenge the group's assumptions. (cognitive dissonance)
- *Sterotyping* those who are opposed to the group as weak, evil, biased, spiteful, impotent, or stupid.

## III: **Pressures toward Uniformity**

- *Self-censorship* of ideas that deviate from the apparent group consensus.
- *Illusions of unanimity* among group members, silence is viewed as agreement.
- *Direct pressure* to conform placed on any member who questions the group, couched in terms of "disloyalty"
- *Mind guards* — self-appointed members who shield the group from dissenting information.

# Intrinsic & Extrinsic Incentives



## Board Decision Making under the 1997 Act



Accountability

- Register of Board Approvals
- Board must operate a comprehensive decision-making process and document the reasons for its decisions
- Board Minutes should document “all decisions, discussions and points for further action”, record all dissensions or minority votes in terms acceptable to the dissenting person or minority voter, and “provide sufficient detail to identify the nature and extent of the discussion on any matter and the decision or other outcome.”
- Where the board causes any matter relating to its functions to be performed or carried out on its behalf, it shall continue to have responsibility for the matter.
- Board should consider whether it would be appropriate to establish risk, audit and remuneration committees ...In deciding on the composition of each committee the board should have regard to the need to ensure that no one individual director has effective control over the business of the credit union. (Guidance on s.56A)

## Compliance under the 1997 Act

Accountability

Communications

- A credit union must have in place the oversight, policies, procedures, practices, systems, controls, skills, expertise and reporting arrangements to ensure compliance with the requirements set out in Part IV
- The Compliance policy should include “the process to ensure that a culture of compliance is promoted at every level within the credit union; “ (Central Bank Guidance 3.2.1)
- Board approved annual compliance statement must be submitted to the Central Bank certifying its compliance with Part IV (Management of Credit Unions) of the 1997 Act (s.66C).



# Standards of Conduct and Ethical Behaviour of Officers should include: (Central Bank Handbook)



Accountability

- **organisational arrangements, reporting lines and arrangements**
  - process for the **approval, review and update of the standards by the board**
  - The board should ensure that the standards are **communicated** to all officers and declarations should be signed by all officers.
- 
- **general standard of care** of officers
  - requirements to **act with integrity and honesty, avoid conflicts of interest and act in compliance with applicable legal and regulatory requirements and guidance** such as health and safety and confidentiality requirements
  - **list of types of unethical conduct and unauthorised activities** eg abuse of personal privileges;
- 
- **whistleblowing** procedures;
  - **consequences of breaches and derogations;**
  - **significant deviations from the standards should be communicated to the board.**



Communications

# Central Bank's Fitness and Probity Regime

A person must:

- be competent and capable;
- act honestly, ethically and with integrity;
- be financially sound.

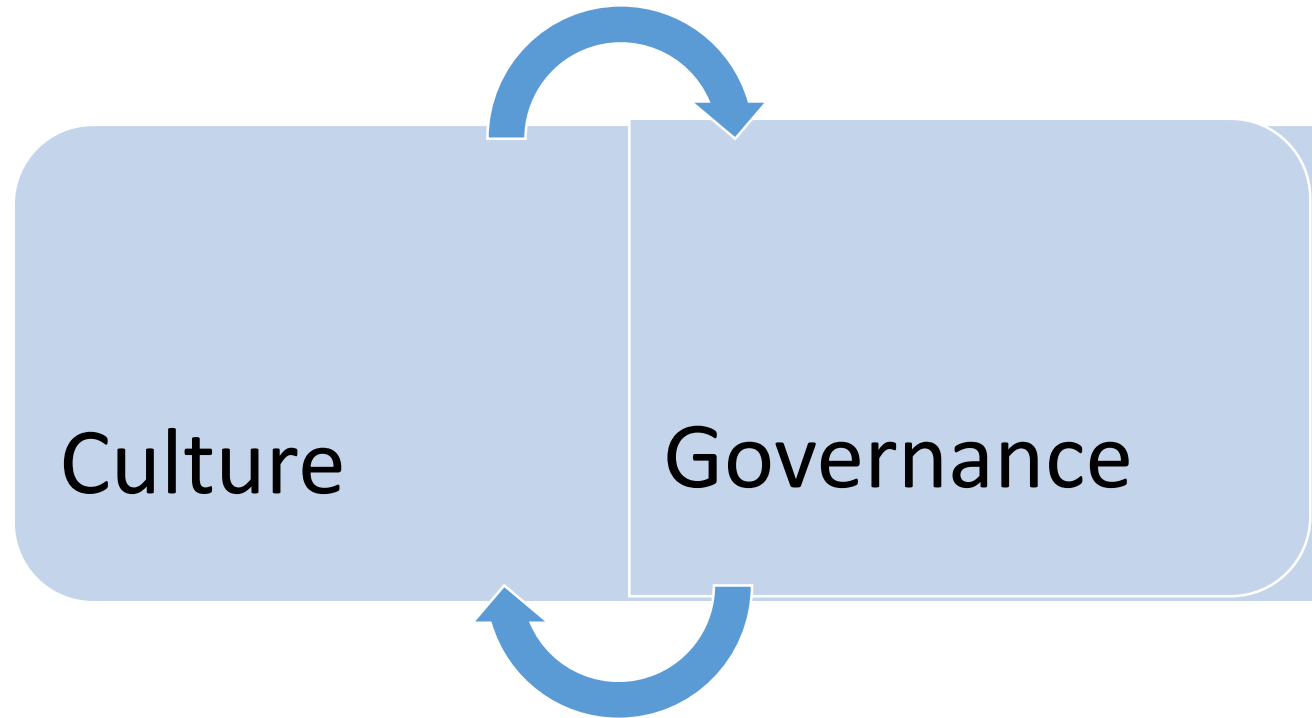




# Tone All the Way Through

You're only as good as the leaders you have underneath you. You might think that because you're projecting our values, then the rest of the company is experiencing the values. What you realize is that the direct supervisors become the most important influence on people in the company. – Victoria Ransom, Wildfire Co-Founder

# Conclusion



Corporate Governance Model in Credit Unions Does Encourage and Support Organizational Culture

But...

# Corporate Governance – “Its not Rocket Science...” J.Coates

