

RISK GOVERNANCE: CULTURE MATTERS

9TH ANNUAL CONFERENCE ON RISK GOVERNANCE



18 SURVEY ITEMS

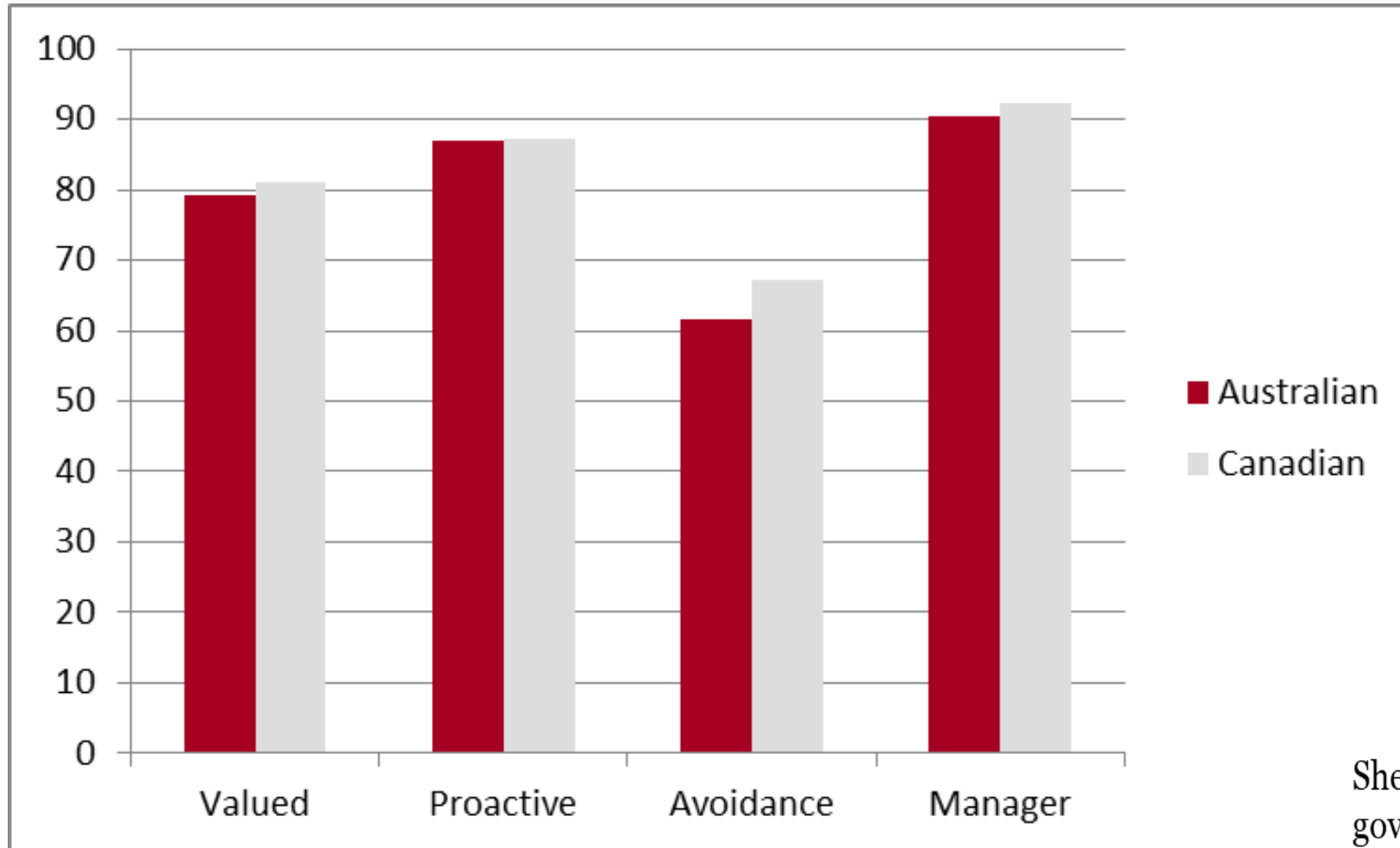
Components of Risk Culture



Sheedy, Griffin, and Barbour. (2017) "A framework and measure for examining risk climate in financial institutions." *Journal of Business and Psychology* 32(1): 101-16.

Risk Culture Factor Scores

% FAVOURABLE



Sheedy, and Griffin. "Risk governance, structures, culture, and behavior: A view from the inside." *Corporate Governance: An International Review* (2017).

Validation?



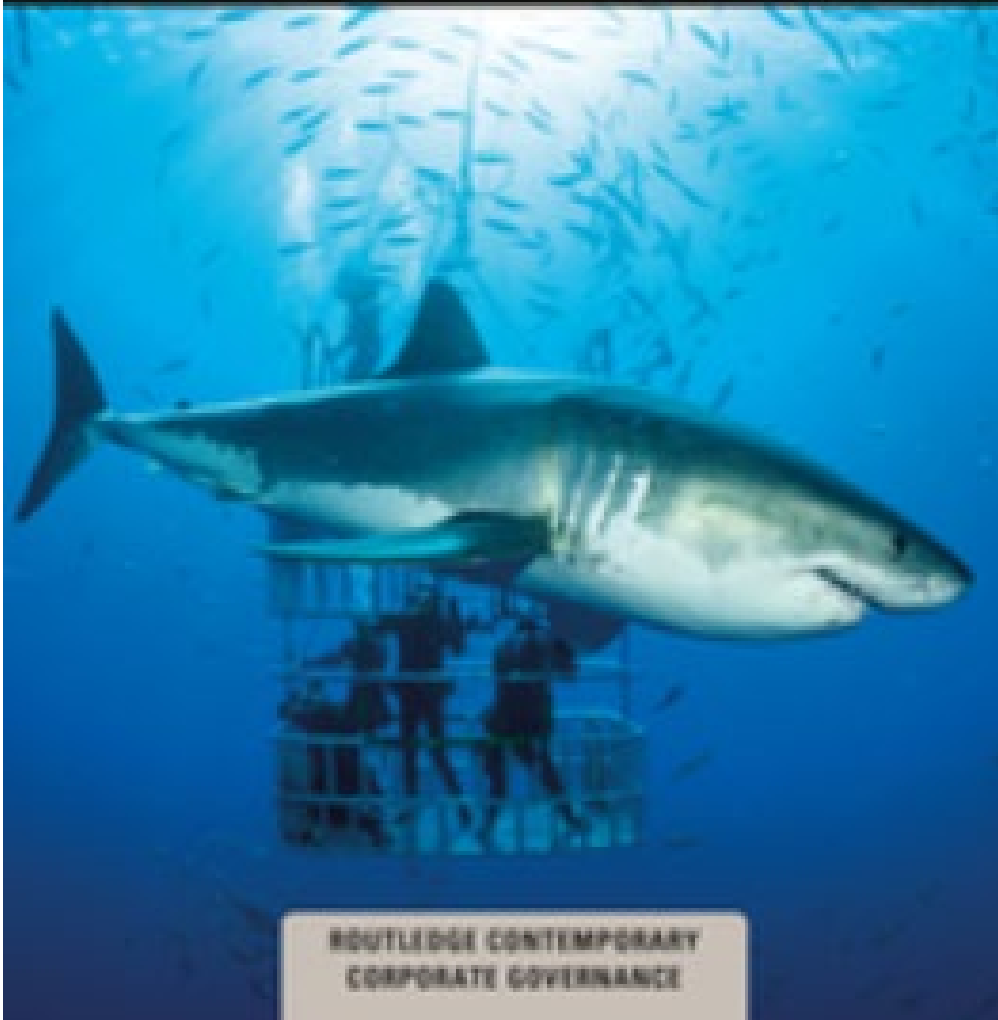
Royal Commission into
Misconduct in the Banking,
Superannuation and
Financial Services Industry

Elizabeth Sheedy



Risk Governance

Biases, Blindspots and Bonuses



MACQUARIE
University

- Overconfidence
- Availability bias
- Short-termism

Kaplan and Mikes
(2016)

Benefits of Accountability

INVOKES SYSTEM 2 THINKING (KAHNEMAN)

System 1

Intuitive, automatic, effortless



System 2

- Analytical, deliberative, effortful
- Doing a reverse park in a busy road
- Calculating 132×79
- Carefully reading a risk report!

Benefits of Accountability

INVOKES SYSTEM 2 THINKING (KAHNEMAN)

System 1

Intuitive, automatic, effortless



lots of cognitive errors or behavioural biases e.g. overconfidence, groupthink, availability bias, short-termism



How to boost System 2?



Accountability: Perceived expectation that one's decisions or actions will be evaluated by a salient audience; rewards/sanctions will be contingent on this evaluation.

Benefits of Accountability

INVOKES SYSTEM 2 THINKING (KAHNEMAN)



- More information search
- More attention
- Anticipate counter-arguments
- More self-reflective
- More effort and diligence

Lerner, J. S., and P. E. Tetlock. 1999. Accounting for the effects of accountability. *Psychological Bulletin*, 125(2), 255-75, doi:10.1037/0033-2909.125.2.255

Hall, A. T., D. D. Frink, and M. R. Buckley. 2017. An accountability account: A review and synthesis of the theoretical and empirical research on felt accountability. *Journal of Organizational Behavior*, 38(2), 204-24, doi:10.1002/job.2052

Experimental literature: Accountability

Kennedy, J. 1993. Debiasing Audit Judgment with Accountability: A Framework and Experimental Results. *Journal of Accounting Research*, 31(2), 231, doi:10.2307/2491272

Jermias, J. 2006. The influence of accountability on overconfidence and resistance to change: A research framework and experimental evidence. *Management Accounting Research*, 17(4), 370-88, doi:<https://doi.org/10.1016/j.mar.2006.03.003>

Messier, W. F., L. A. Quick, and S. D. Vandervelde. 2014. The influence of process accountability and accounting standard type on auditor usage of a status quo heuristic. *Accounting, Organizations and Society*, 39(1), 59-74, doi:<https://doi.org/10.1016/j.aos.2013.12.002>

Poor executive accountability

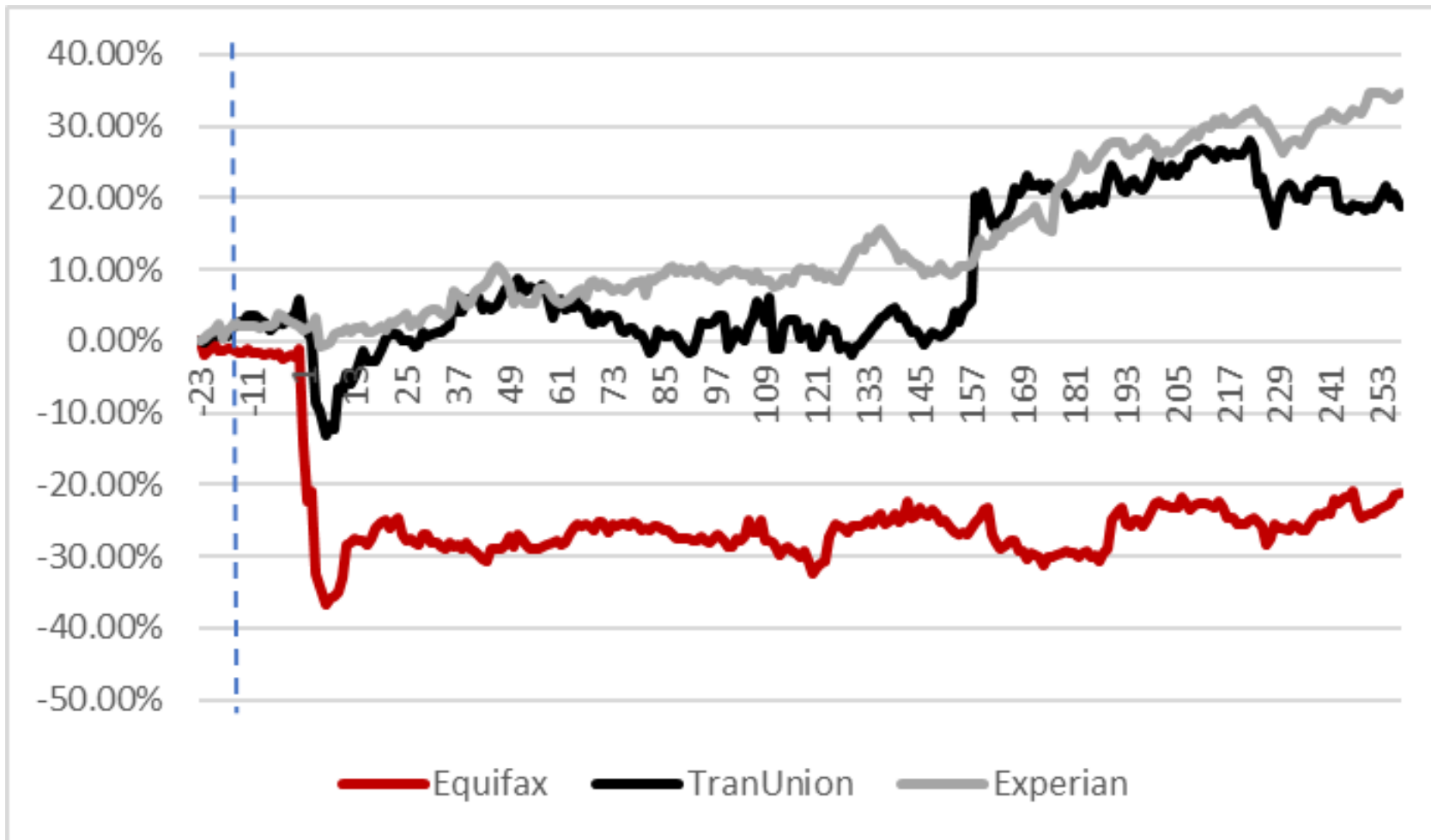
I didn't know
what was going
on



Not my
respon-
sibility

**Stop executives
hiding behind
ignorance and
group decision
making
processes.**

Cumulative Abnormal Returns (CAR)



CAR for Equifax and peer firms from 1 calendar month before the public disclosure of the cybersecurity breach to 12 months after the breach.

Appropriate consequences for poor outcomes?

**Equifax CEO pushed out after data hack
getting nearly \$20 million in bonuses**

New executive accountability regimes



Senior Managers and Certification Regime

- Clear, ***individual*** accountabilities
- All variable remuneration deferred
- Malus clauses address poor risk outcomes



INFORMATION PAPER

Implementing the Banking Executive
Accountability Regime

Benefits of Accountability Regimes

HYPOTHESES

1. New regulations cause senior executives to be more diligent in their risk management.

2. Better risk management behaviour by senior executives causes risk culture to thrive.

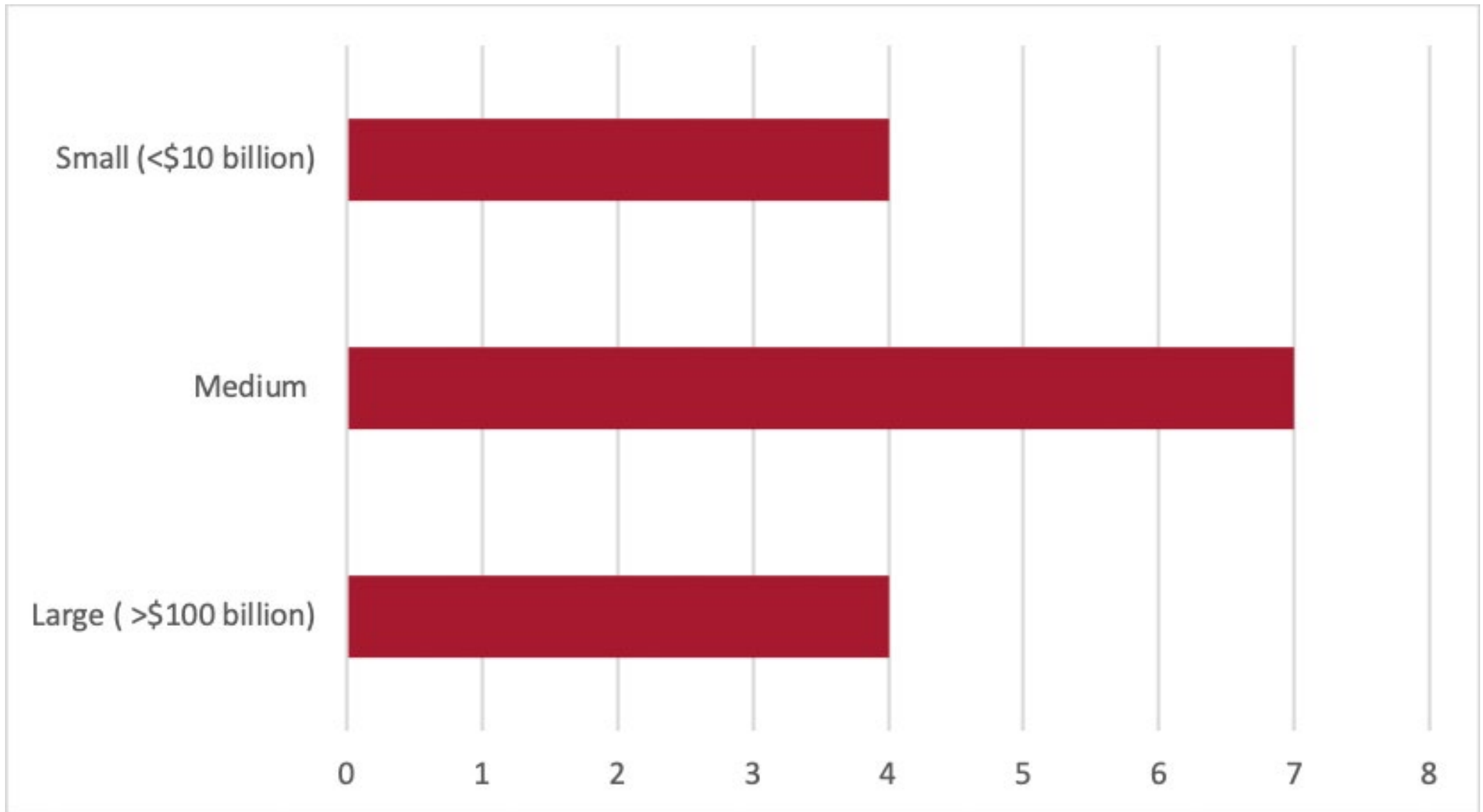
Research on the BEAR

CONFIDENTIAL INTERVIEWS AND SURVEYS

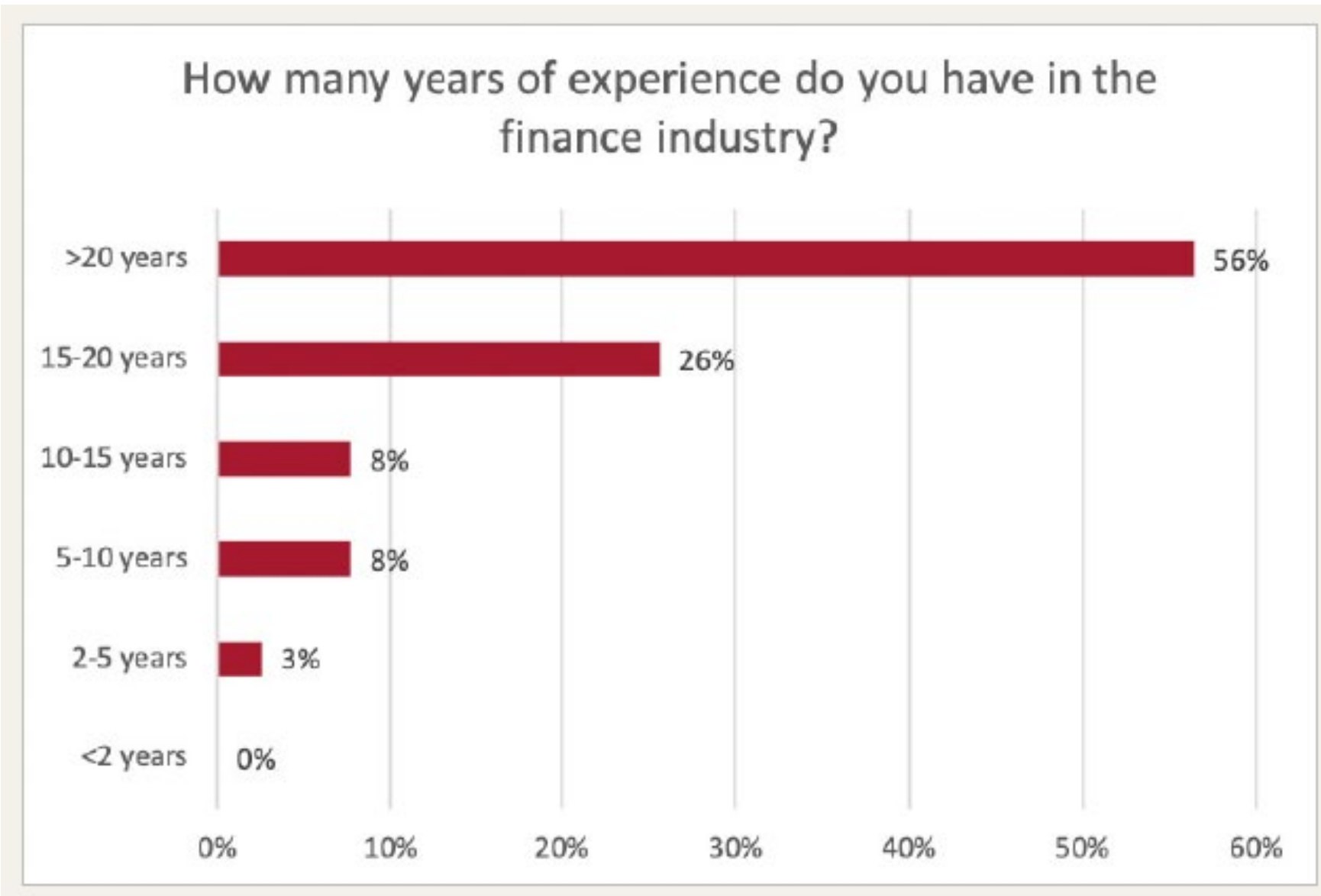
- Confidential interviews with risk/compliance and assurance executives about experiences of the BEAR
- 41 participants representing 15 firms
- Of the 41, 18 were 'Accountable Persons'



Participating Organisations by Size



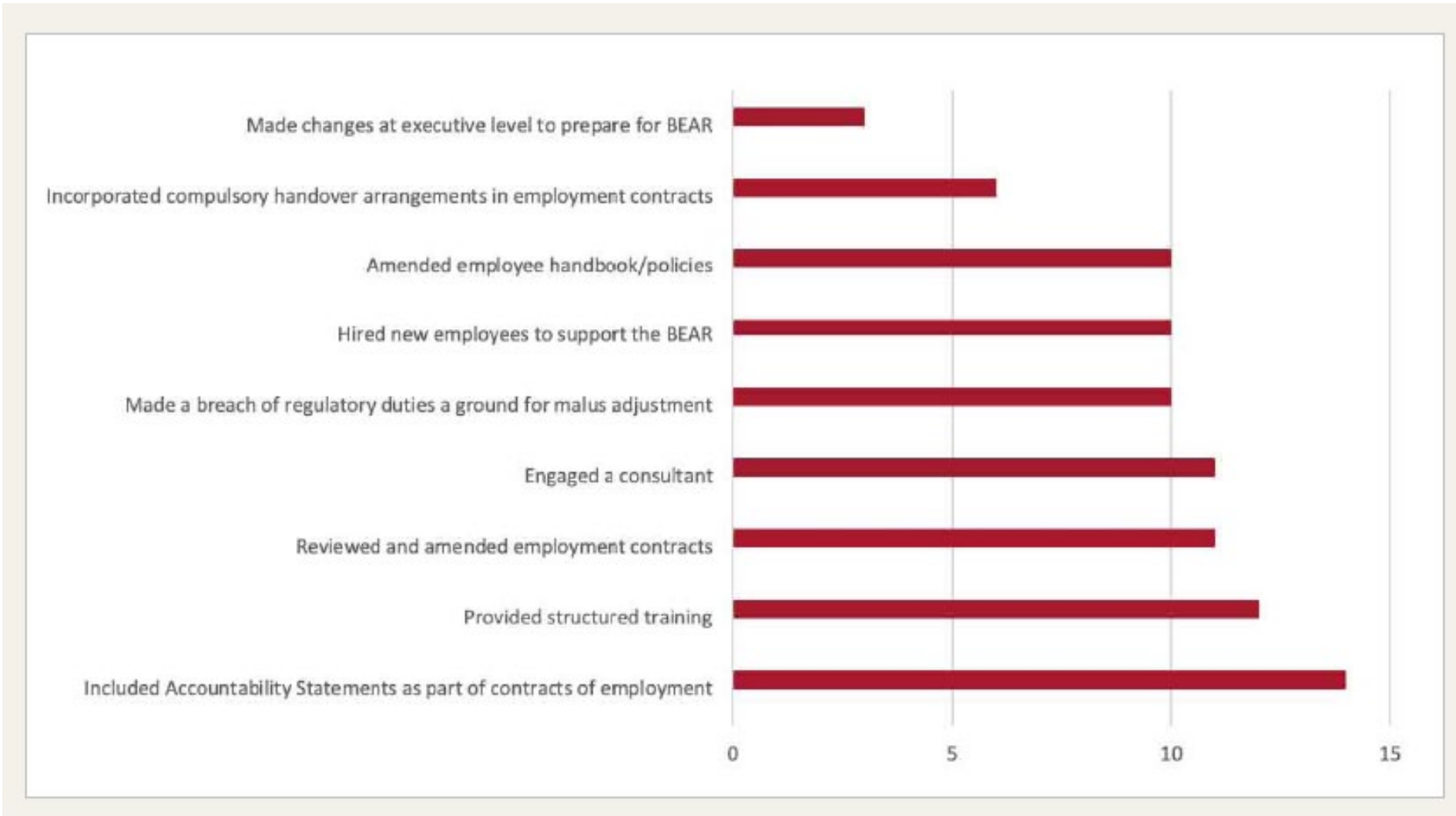
Industry Tenure of Interviewees



Survey Measures

	Average Score for Accountable Persons (standard deviation)	Average Score for Others (standard deviation)	Comment on Statistical Significance
Felt Accountability /7	5.50 (0.68)	5.07 (0.88)	APs score significantly higher than others ^{xxvi}
Work Stress /7	3.87 (1.64)	3.97 (0.85)	Not significantly different
Personality: Extraversion /7	4.79 (1.05)	4.41 (1.42)	Not significantly different
Personality: Agreeableness /7	4.88 (1.10)	5.17 (0.92)	Not significantly different
Personality: Conscientiousness /7	6.15 (0.66)	5.93 (1.15)	Not significantly different
Personality: Emotional Stability /7	5.85 (0.58)	5.72 (0.96)	Not significantly different
Personality: Openness /7	5.44 (0.77)	5.28 (0.91)	Not significantly different
Political Skill /5	4.03 (0.38)	3.92 (0.43)	Not significantly different
Self-Consciousness /5	2.82 (0.65)	2.63 (0.53)	Not significantly different

Implementing the BEAR



Implementing the BEAR

Before becoming an accountable person, which of the following actions did you take?



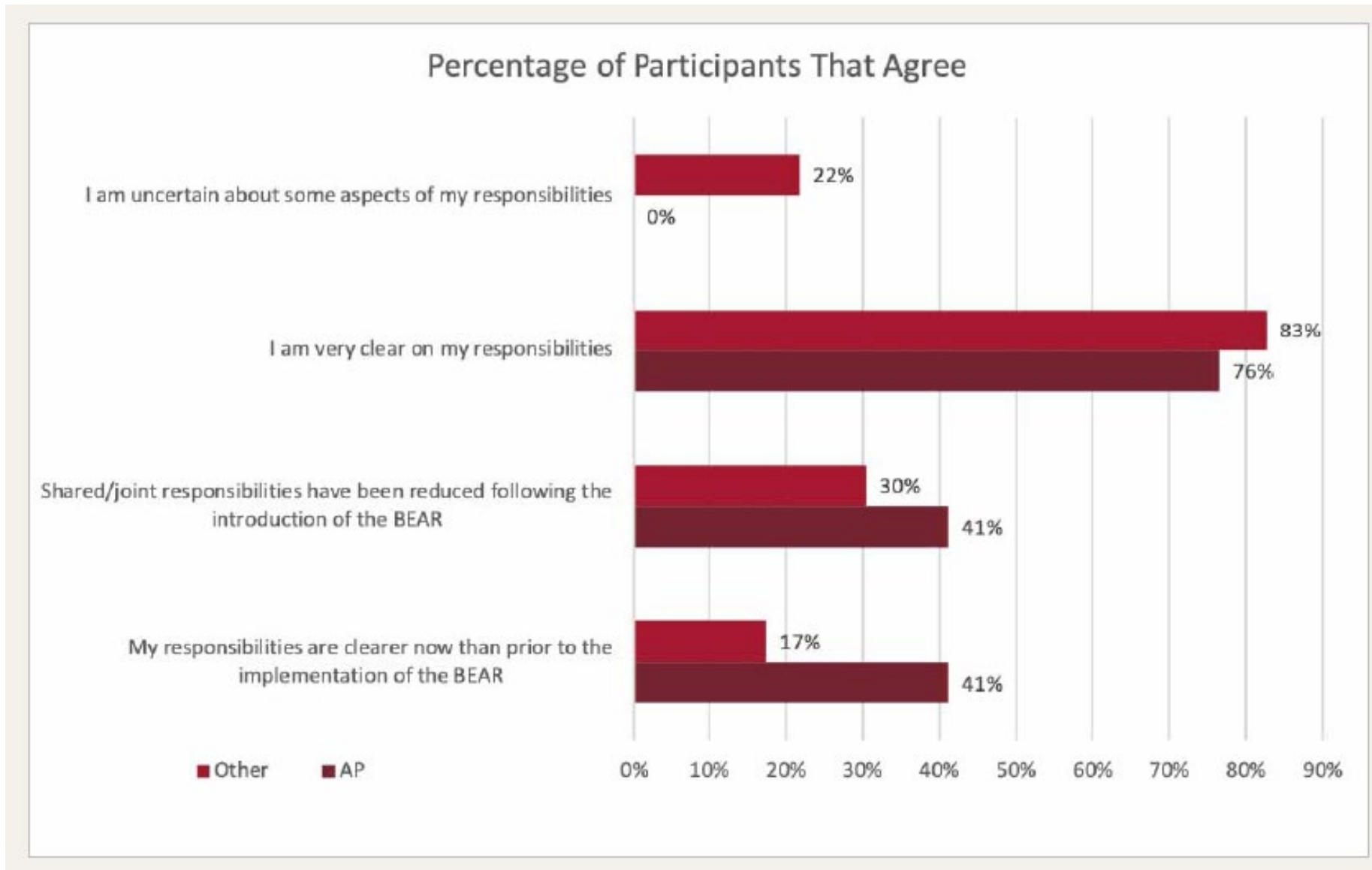
Implementing the BEAR

‘We developed a series of case studies. We had five or six in total. We got a number of [accountable persons] to participate in those workshops. They went for a number of hours, and that actually helped us clarify for ourselves where there's some crossover of accountabilities as to who's responsible for what part. So I think that was incredibly beneficial.’

What is Accountability?

'I think we all have to delegate. We can't delegate accountability but we certainly delegate the responsibilities for doing these things and we have to be reliant on the people and the structures beneath us to do that.'

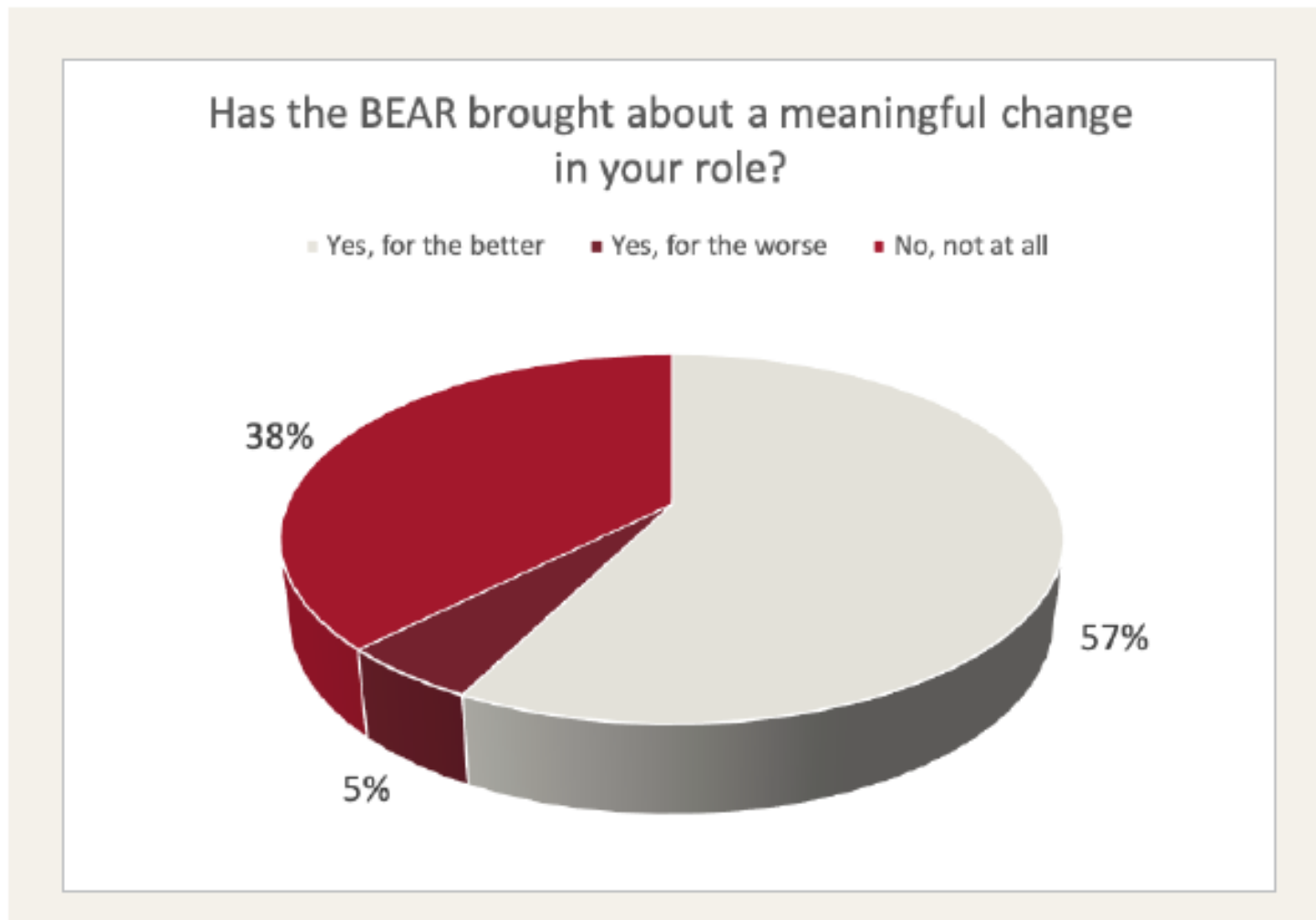
BEAR brings clarity to accountability



Benefits of clarity of accountability

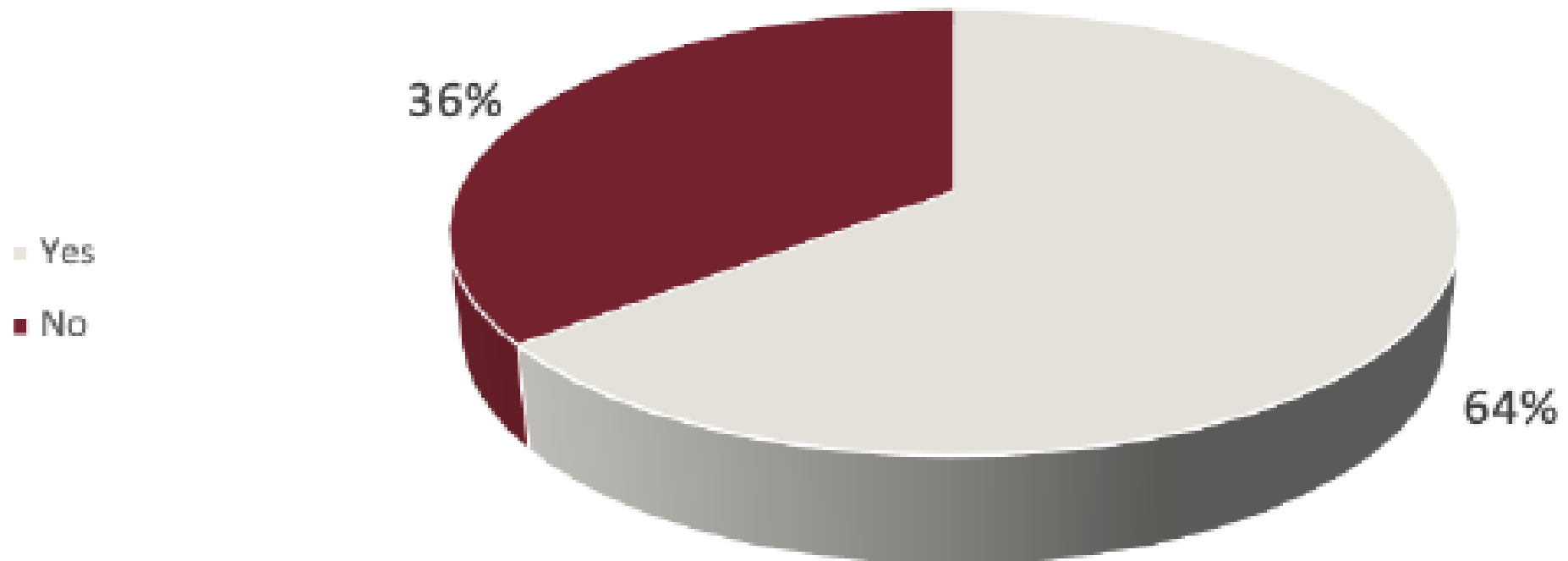
REACTING TO CRITICAL INCIDENTS, RED FLAGS

AP18 It's given a frame of reference for those "Oh" conversations.



Voice of risk is enhanced

Is there greater involvement of compliance/legal/risk with decision-making?



Taking 'reasonable steps'

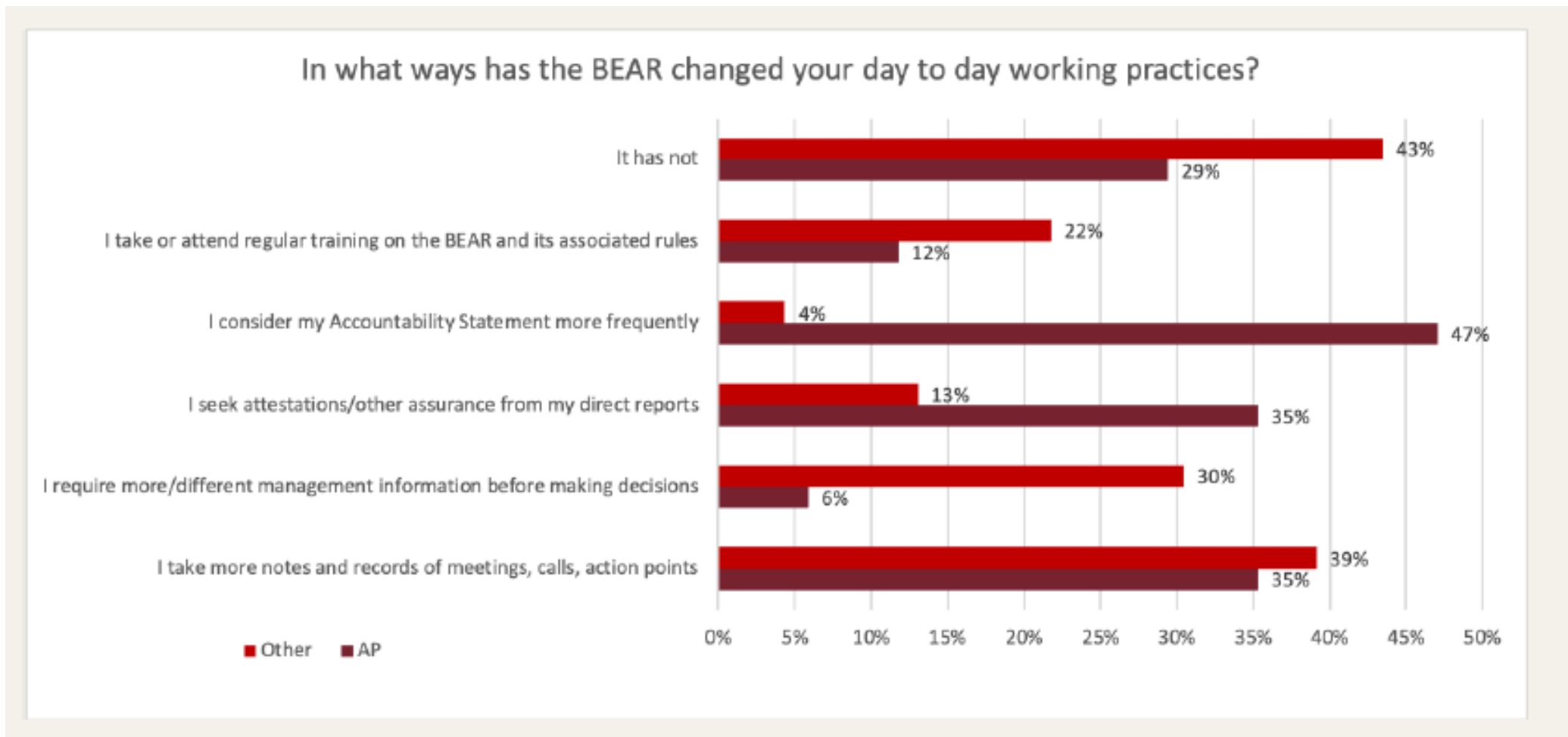
- O11 *Even if they're not using BEAR explicitly, you might now start to hear people mention a phrase like 'reasonable steps'. You'll certainly hear people stopping the conversation to ask about decision rights and accountability. And you'll certainly get more people concerned to think about what the governance mechanisms are around some of the decisions that they're taking.*

Line 1 stepping up

RESPONDING TO ISSUES

- AP8 *Was there one single thing that's come out of this? I think it's that really good reminder that your first line of defence, if that fails, nothing else can hold up. I think BEAR does really speak well to you are accountable. That to me, if you tried to keep it simple, that's what I think it's really reinforced, that first line it's our people.*
- O10 *I think generally once we create the transparency, that's the most important step. Because after that people tend to get onboard and get stuff done, but it's about getting that problem on the table. I think BEAR's helping with making sure we're doing that.*

Working practices change

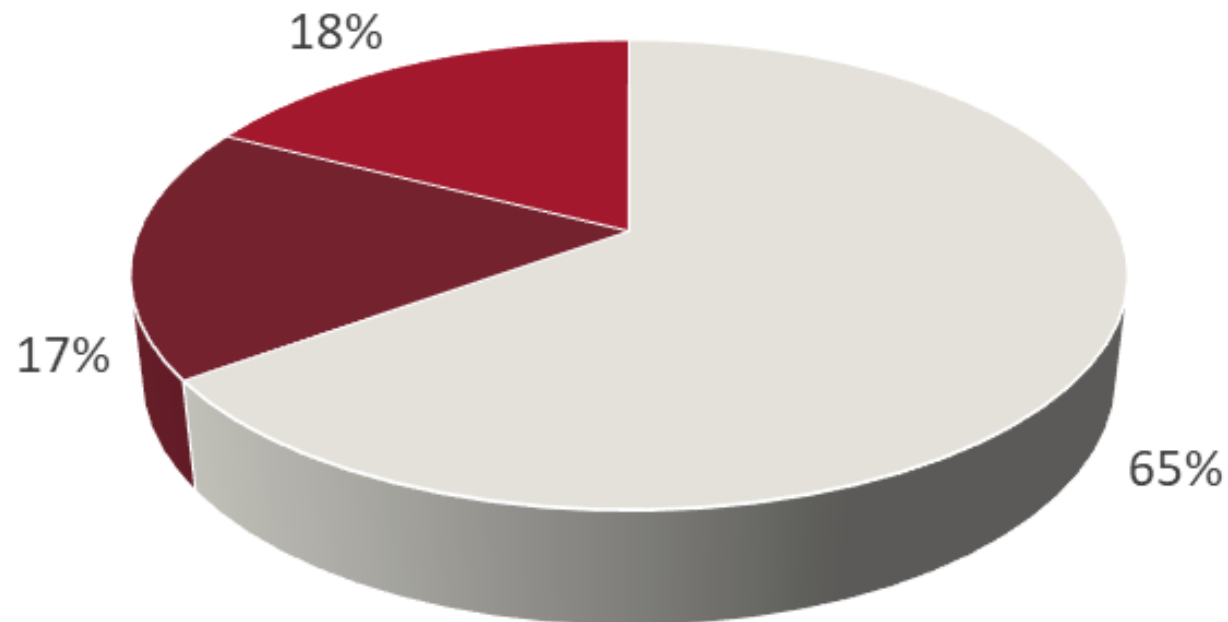


Benefits of clarity of accountability

REACTING TO CRITICAL INCIDENTS, RED FLAGS

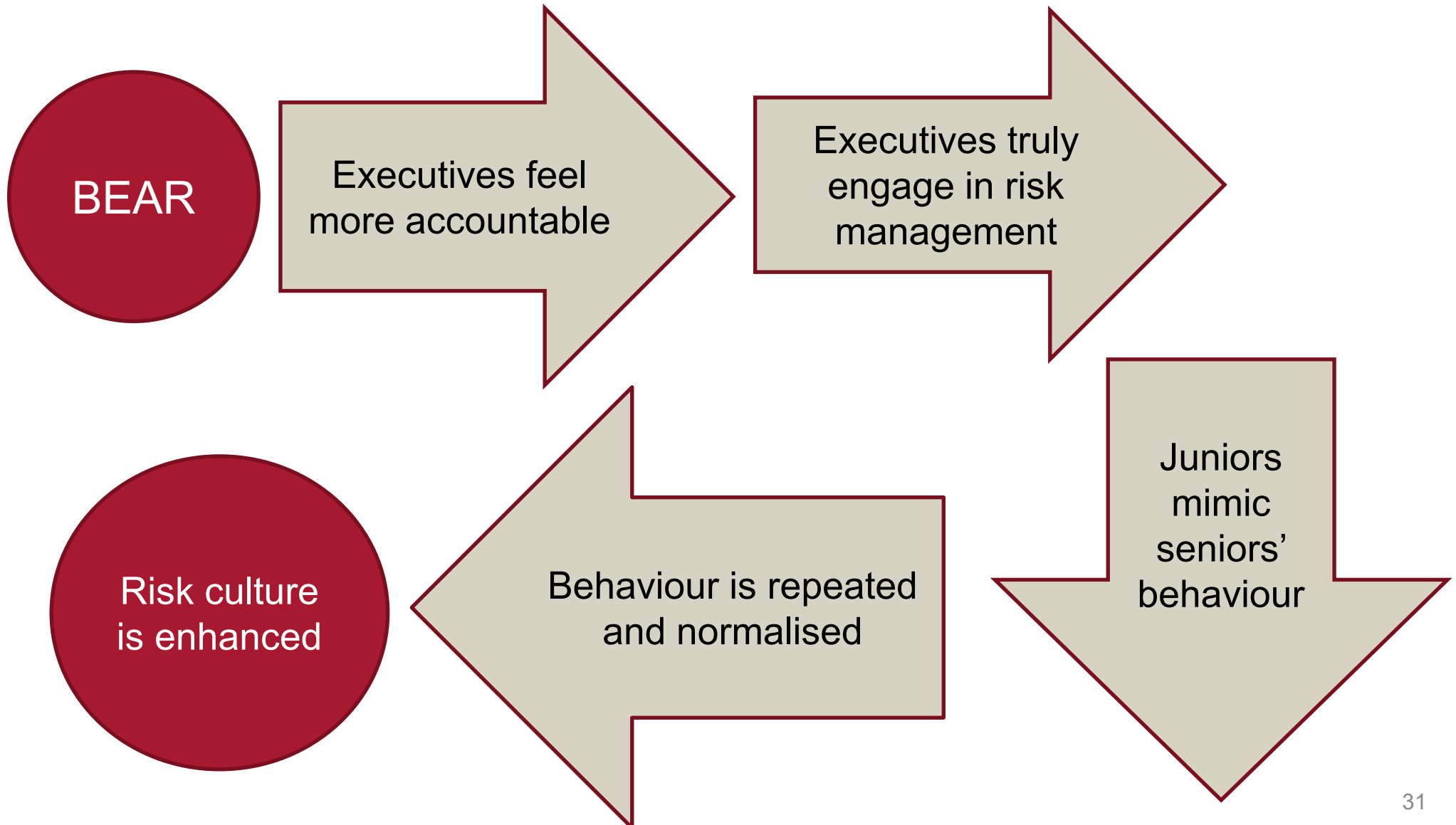
Has the BEAR changed the culture at your organisation?

■ Yes, for the better ■ Yes, for the worse ■ Not at all



Normalising good risk management

BUILDING RISK CULTURE

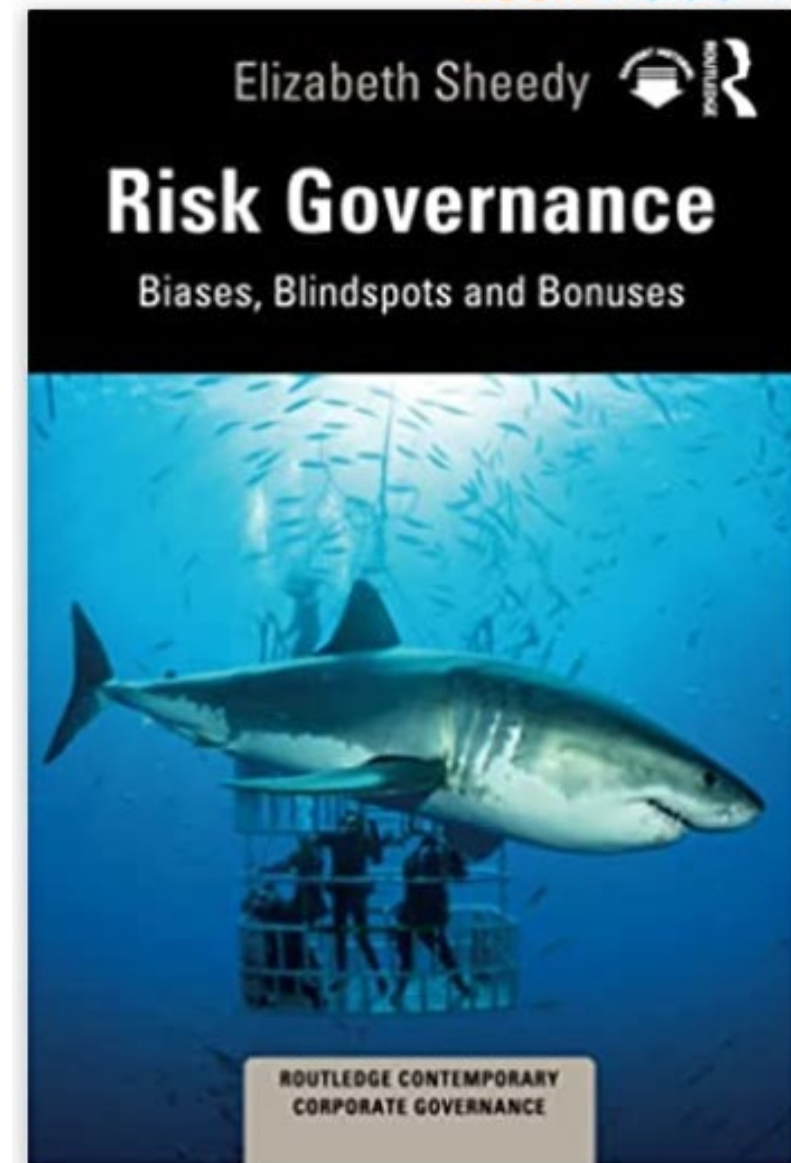


More information

Regulating Accountability: An early look at the Banking Executive Accountability Regime (BEAR)

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December 2020



MACQUARIE BUSINESS SCHOOL



MACQUARIE
University