BANK OF ENGLAND

Press Office
Threadneedle Street
London EC2R 8AH
T 020 7601 4411
F 020 7601 5460
press@bankofengland.co.uk
www.bankofengland.co.uk

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Andrew Bailey speech: Culture in financial services – a regulator's perspective

In his last speech as Chief Executive of the Prudential Regulation Authority, Andrew Bailey explains the importance of culture to both prudential and conduct financial regulators and the challenges for supervisors when looking at the culture of firms.

For the avoidance of doubt – and in view of recent history – I want to start with what I intend as an unambiguous statement, namely that the culture of firms and the people that make them up - and of course therefore the culture of industries insofar as it can be generalised – is of the utmost importance to financial regulators. Culture matters a great deal. And this is true for both conduct and prudential regulators…

…As supervisors, we cannot go into a firm and say "show us your culture". But we can, and do, tackle firms on all the elements that contribute to defining culture, and from that we build a picture of the culture and its determinants.

Andrew sets out risks to good governance of firms, which can lead to bad outcomes.

Culture has a major influence on the outcomes that matter to us as regulators. My assessment of recent history is that there has not been a case of a major prudential or conduct failing in a firm which did not have among its root causes a failure of culture as manifested in governance, remuneration, risk management or tone from the top. Culture has thus laid the ground for bad outcomes, for instance where management are so convinced of their rightness that they hurtle for the cliff without questioning the direction of travel. We talk often about credit risk, market risk, liquidity risk, conduct risk in its several forms. You can add to that, hubris risk, the risk of blinding over-confidence.

Andrew clarifies the role of regulators when dealing with the question of culture

As regulators, we are not able, and should not try, to determine the culture of firms. We cannot write a regulatory rule that settles culture. Rather, it is the product of many things, which regulators can influence, but much more directly which firms themselves can shape. We seek to ensure that firms have robust governance, which includes appropriate challenge from all levels of the organisation; and promote the *acceptance that not all news can be good and the willingness to act on and respond promptly to bad news. We insist that remuneration is structured to ensure that individuals have skin in the game, namely that a meaningful amount of past remuneration is retained or deferred and, for senior people, is at risk should problems then emerge. We require that risk management and internal audit in firms are effective and act to root out poor incentives and weak controls. All of this is important and central to what we do as regulators, but let me reinforce the point that culture begins and lives, and I am afraid dies, at home, with firms.*

Andrew also sets out his views of the new Senior Managers Regime

There is, let me be clear, no magic bullet to change culture, but the new regime is a big step forward in my view. This is because at its heart it embeds the notion of personal responsibility for the affairs of the firm at the level of senior management.

Andrew Bailey will take up his new role as CEO of the Financial Conduct Authority on 1 July.

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