Building a risk-aware culture for success

Get up to speed on Risk Management issues

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Does your organisational culture reinforce your strategy and help you take the right decisions on risks?

Establishing a culture in which the right people do the right thing at the right time is critical to your ability to seize opportunities and minimise mistakes. No matter how clearly you define your risk appetite and controls, the people who work for you won't consistently make the right decisions unless corporate culture reinforces 'doing the right thing' naturally.

Our latest Global Economic Crime Survey illustrates this point clearly. It shows that the incidence of fraud in companies with compliance programmes which are reinforced by a code of ethics is 25% lower than it is in companies with compliance programmes unsupported by any ethical guidelines.

But many executives do not understand the impact of their organisation's culture; they simply assume that their employees know what sort of behaviour is expected. And even when a company formally articulates the values, beliefs and practices it espouses, it can unwittingly undermine them. So it is only possible to ensure that everyone adheres to the standards management wants by creating a culture that reflects and reinforces those standards.

Highlights

1. *Envisage your ideal organisational culture:* Define the culture you want to build, drawing on best practice in other industries or parts of the organisation.

2. *Assess your existing culture against that ideal:* Ask your employees, customers and suppliers for feedback, and analyse your findings. Look for any local variations or non-verbal signals that conflict with the ideal to which you aspire.

3. *Plot your position:* Map out where each business unit stands in terms of its attitude to risk and stage of cultural development.

4. *Identify and prioritise the gaps:* Pinpoint the problems and rank them in order of importance. Find out which systems and processes need to be changed to solve them.

5. *Close the gaps:* Be explicit about the kind of organisational culture you want, lead the way and get everyone involved.

Creating the right organisational culture

- A company isn't just what it claims to be in its corporate mission statement or staff newsletter. It also sends out a lot of implicit 'messages'.

- The factors that shape how employees think and behave include how they and their managers interact, both with each other and with suppliers and other third parties; the standards and rules that evolve, such as how hard people work, when they come to work and when they leave; the physical layout of the workplace; the anecdotes which get told and retold; and the behaviour an organisation rewards.

- So how can you create a culture that supports your business strategy, goals and risk appetite? Our experience shows that there are five essential moves:

  - Envisage your ideal organisational culture
  - Assess your existing culture against that ideal
  - Plot your position
  - Identify and prioritise the gaps
  - Close the gaps

Figure 1: Organisational cultures are shaped by a mixture of explicit and implicit messages
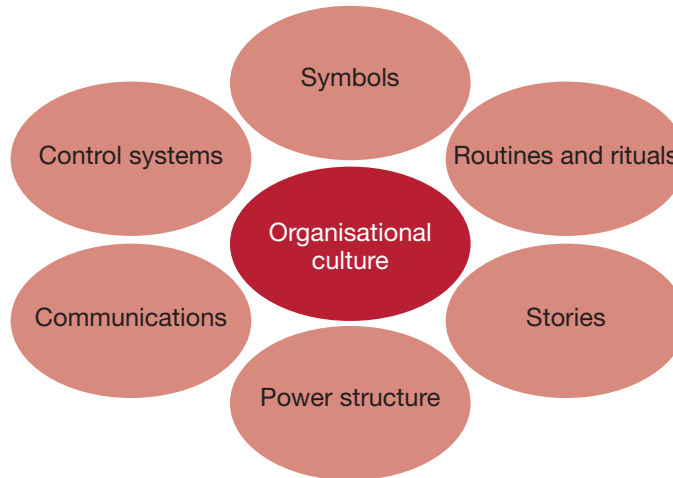
Source: PricewaterhouseCoopers

1 - Envisage your ideal organisational culture

- Recognise the importance of organisational culture. Many executives don't understand the importance of culture and how it can influence a business. But every organisation has a culture; every culture carries different opportunities and risks; and different cultures can produce huge variations in performance.

- Build a picture of the future. Identify the main characteristics of the organisational culture you think you want at this stage – what you want your company to stand for, how you want your employees to behave and the end-state you want to achieve.

- Check out best practice elsewhere. Look at how the cultures of companies in your own industry and other industries help them manage risk. Are there any models from which you can learn?

- Envisage the ideal situation. Define your ideal organisational culture, including the key aspects that underlie effective risk management, given the sort of business you're running.

Figure 2: The key aspects of corporate culture that underpin effective risk management

Leadership and strategy

Risk management and infrastrucure

Integrated risk management

Accountability and reinforcement

People and communications

Behaviour and outcomes

Knowledge, skills and abilities

Supporting infrastructure

Source: PricewaterhouseCoopers

2 - Assess your existing culture

- **Choose your method.** Decide what sort of data you're going to collect. Should it be inferential (e.g., observations of how people behave and customer feedback); qualitative (e.g., interviews and workshops) or quantitative (e.g., employee surveys)? In our experience, a combination of data-gathering techniques is usually best.

- **Analyse the evidence.** Collate and analyse your findings. What do they tell you about how people see the company and its attitude to risk? Do they think it's highly centralised or fragmented? That it encourages individualism or collaboration? That it's a money-making machine or a company with a strong social conscience? That it's over-cautious or that it takes too many risks?

- **Spot the differences.** Bear in mind that most companies don't have a single culture; they're a mix of different subcultures – and when different subcultures clash, employees get confused. Some behavioural traits (such as how well people tolerate uncertainty, whether they focus on the short or long term, and whether they live to work or work to live) vary substantially from one country to another, for example. All these traits inform individual attitudes to risk.

- **Consider the hidden clues.** Don't forget to take the tacit messages into account – the rituals, stories, norms, power structures, informal networks and other features that influence or reflect your company's culture.

Developing a values-based approach to business ethics

The senior executives of a global industrial products company wanted to improve its internal processes for ensuring that staff acted ethically, as well as enhancing its external image. They recognised that the historic approach, which was heavily rules-driven, had inherent limitations. The company is now developing a small number of ethical principles to which every employee can subscribe. These principles will sit above the company's code of conduct, providing a mechanism for communicating how people should behave and encouraging them to make the 'right' choices. The board anticipates that the principles will also play an important role in helping the company convey what it stands for to the outside world and making its brand synonymous with leadership in ethical business conduct.

Monitoring the behavioural evidence

Realising that it was spending more and more money on risk management and compliance, without a corresponding reduction in the number of problems it encountered, one leading bank decided to review its organisational culture. It began by assessing its existing internal audit procedures to see what, if any, behavioural evidence was already being collected. It then developed a behavioural risk assessment plan, including a set of questions for interviewing employees, data sampling guidelines and a scoring template, and tested the plan in a number of business units, before rolling it out across the entire firm.

The bank now monitors the cultural and behavioural factors that affect how it manages risk and compliance on a regular basis. It also reports its findings to the business units, provides them with practical guidance in addressing cultural challenges and benchmarks its progress in creating a culture that supports its risk processes and controls. This has enabled it to reduce the frequency and severity of the problems it encounters, reduce its remediation costs and strengthen its reputation.

3 - Plot your position

- **Plot your position.** Evaluate where you stand – or, rather, where the different parts of your business stand – in terms of how they manage risk. Here's one model for assessing the stage of development your organisation has reached.

- **Use the internal information you've collected to identify how employees think about risk within their respective business units.** Look for recurring features; these are the core elements of which they're aware.

- **Now ask your customers, suppliers and other stakeholders what they think.** Do they see your organisation in the same light or are there major differences of opinion? Map the responses you get on the grid to identify which quadrant each business unit belongs in.

Figure 3: The four stages of competence

	Conscious	Unconscious
Competent	**Smart Player** The smart player is consciously competent. It's typically a company with good risk controls and good risk managers. But though its risk management skills are strong, they aren't yet 'second nature'. The people who work for it understand the kind of risks and amount of risk they can take, but risk management is something they still have to think about.	**Instinctive Expert** The instinctive expert is unconsciously competent. It has defined the risks it's prepared to assume, built robust risk-information and monitoring systems, and communicated its attitude to risk to everyone in the organisation. Risk management is now so completely embedded in the business that it's automatic. Everyone knows what to do, and does it as a matter of course.
Incompetent	**Anxious Operator** The anxious operator is consciously incompetent. It's a company that is well aware of the risks it faces, but it either hasn't got the right people, procedures or measures for managing risk or else it's still struggling to implement them. It's likely to be a new company or one that's going through massive changes, so management has other things on its mind. But the longer the company 'muddles through', the bigger its problems will become.	**Inadvertent Amateur** The inadvertent amateur is unconsciously incompetent. Such a company doesn't even know what it doesn't know or can't do well. It doesn't understand the risks it faces (although it may believe that it does), and has no systems, processes or controls in place to manage risk effectively. Its exposure to risk is typically very high, and it's probably heading for a crisis.

Source: Competence learning model adapted by PricewaterhouseCoopers

4 - Identify and prioritise the gaps

- **Locate the holes.** Draw up a list of the problems the analysis you've undertaken has exposed, using examples of real issues that arose as a result of having an inappropriate organisational culture. Work out which corporate structures, systems and processes will need to be changed to resolve these problems – e.g., recruitment, training and performance management.

- **Assess how the changes will affect different stakeholder groups.** The changes you plan on making will probably affect some people more than others – and people want to know about the changes that will most affect them. The sales function is often a source of risk, for example, because employees may be tempted to promise more than the organisation can deliver to close a sale. So tailor your communications programme to the needs of each stakeholder group.

- **Read the hidden signs.** Identify any non-verbal features that conflict with the risk-aware culture you want to create.

- **Define your criteria for success.** Select the criteria you'll use to assess the success of your change programme and put tools in place for measuring your progress.

- **Be realistic.** Recognise that you've got to begin at the point where your people are – not at the point where you wish they were.

Working on its weaknesses

When internal audit suggested that cultural changes might improve the way in which a major financial institution managed risk, the board commissioned a team of independent experts to help it investigate the situation more thoroughly. The team began by analysing the results of an employee engagement survey the institution had recently conducted to get a better understanding of attitudes to risk within the different business units. This enabled it to identify a number of opportunities for improving the process for making decisions about risk and holding people accountable for the choices they made. It also highlighted several areas that warranted further work, including the development of more comprehensive employee surveys and information reviews.

5 - Close the gaps

- **Take the lead.** A change of culture must be led from the top; it can't just be 'managed'. If you want to start your company off in a new direction, you'll have to march in front.

- **Get everyone involved.** Tell people what's changing, why, what you want them to do and how you want them to do it, using clear examples drawn from within the company. Use presentations, staff magazines, workshops and short briefings to spread the word. If you don't let employees know what you want, you can't blame them when they do something different.

- **Appoint some 'culture carriers'.** Find a few people who are eager to make progress, put them on specific projects and give them your wholehearted support. You can use their successes to convince any sceptics that the changes really work.

- **Provide training.** Give your employees the resources with which to acquire new skills. And remember that the hardest thing about changing a culture isn't teaching people new ways of thinking, but getting them to abandon old ways.

- **Combine the carrot and stick.** Align your reward and disciplinary systems with the culture you want to create. If people don't have an incentive to do the right thing, or don't incur a penalty for doing the wrong thing, they won't change.

- **Track your progress.** Measure how well you're doing and take corrective steps, if necessary. Use workshops and follow-up surveys to assess how well the changes have stuck.

Putting an ethical culture in place

Faced with a regulatory investigation and major criticism from key stakeholders over various ethical shortcomings, the board of a global automotive company recognised that it needed to make sweeping changes to the way in which its code of conduct was applied. In particular, employees required extensive training both to implement new controls in key processes such as sales and marketing, accounting and human resources, and to encourage a totally different attitude.

The chief executive took the lead in driving these changes by personally explaining them to employees in 'town hall meetings'. He also made cultural change a regular item in board meetings, tasked senior managers with implementing the details of the change programme in their own areas of responsibility and linked their bonus payments to their progress. Lastly, he set up a transparent reporting system to enable top management to monitor the results and ensure that ethical standards were maintained throughout the business.

How PwC can help

Be consistent

- People and organisations are creatures of habit, and changing habits is much harder than changing structures or systems.

- If you don't tell your employees what you want and how you want them to do it, don't be surprised if they do the wrong things.

- Ask yourself whether your company's mission statement, management style, communications and performance measurement and compensation systems are fully aligned.

- Do the atmosphere in the office, the stories that circulate and other such cultural signals reinforce the attitude to risk you desire?

PricewaterhouseCoopers works to solve complex business issues – locally and globally. Our teams draw upon skills in risk, regulation, people, operations and technology to capture opportunities, navigate risk and deliver lasting change across business networks.

We have assisted numerous organisations in defining and developing an organisational culture that supports their risk appetite and encourages their people to do the right things in the right ways. We can help you:

- To assess your organisational culture

- To understand how your employees perceive and manage risk

- To build a risk-aware culture, drawing on best practice elsewhere

- To encourage your employees to take the most appropriate risks, given your business strategy

- To ensure that your employees understand the practical and ethical guidelines within which you expect them to operate.

If you would like to discuss how to create a risk-aware culture in more detail, please contact one of our partners (whose details are listed on the next page) or visit *www.pwc.com/getuptospeed*

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Get up to speed - Other topics

Crisis management

An unanticipated crisis can cause immense disruption, cost a lot of money to rectify and damage your company's image if you end up on the front page of the newspapers. This paper examines how companies can take sensible precautions, recover control and extract value from the situation.

Risk appetite

Most risk management systems aim to avoid risk. But if a business doesn't take risks, it can't grow. This paper looks at how you can make risk work for you and how to take the right risks and manage them successfully.

Operationalising risk management

Most companies have responded to more regulation and increasing scrutiny from stakeholders by establishing independent oversight functions and additional layers of control. This paper looks at the steps you can take to make risk management and compliance a part of your day-to-day business, and reduce unnecessary overheads while at the same time adding value to your organisation.

Risk performance management

Many companies could enhance their corporate performance dramatically by using key risk indicators that look forward, rather than focusing on the past. This paper provides guidance on how to eliminate reporting silos and build a more rounded picture of what's happening in your business.

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