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Cultural star-gazing

The Financial Conduct Authority's latest discussion paper on culture points to a new focus on the purpose underpinning regulated entities: "firms need to offer meaning, not just money" and bring the purpose of society, employees, the firm and shareholders into 'astral' alignment. But are such aspirations rooted in business realities or a case of starry-eyed dreaming? asks **Julian Sampson**.

Why do we come to work? What is the objective of a financial services firm? Who do we serve?

These are some of the questions asked in the FCA's recent discussion paper DP20/1 'Transforming culture in financial services – driving purposeful cultures', released in March just passed. As with all discussion papers, the FCA is at pains to point out that this is neither rules nor proposals, merely ideas that have been kicked around by them and an assortment of academics, firms and trade bodies with whom they hold regular roundtables. But don't let that disarming openness fool you – this DP provides clear insight into the future direction of regulation in the United Kingdom, and arguably a perspective on some more general trends in wider society.

DP20/1 fits into a pattern of recent FCA policymaking: of issuing a general discussion paper ahead of specific rules. Thus in 2018, DP18/2 ('Transforming culture in financial services') (see our previous *Compliance Monitor* article in the May 2018 issue) dealt extensively with the issues of accountability and responsibility. That was followed by the extension of the Senior Managers and Certification Regime (SMCR) to all firms in December 2019. So, expect to see hard rule proposals in this area in 12–18 months' time.

So, what's it all about?

In his introduction to the paper, Jonathan Davidson, the FCA's executive director of Supervision – Retail and Authorisations, defines the purpose of an organisation as "what a firm is trying to achieve – the definition of what constitutes success". This purpose could relate to any number of things. As he says, "it could be social, ethical, consumer-driven or people driven." Most importantly, this purpose is the reason people come to work. And it's not all about the money. Tellingly, he says "while financial reward clearly plays a role, people also work to achieve individual fulfilment and a sense of personal satisfaction. If organisational purpose resonates with individual purpose, then employees will be more engaged, and teamwork and performance will be stronger."

So, Davidson's prescription is as follows – your firm must have a purposeful culture, and that's more than being there just to engage in the low down and grubby business of making money. Gazing heavenwards, he says that to do this, "the stars of employee purpose, social purpose, firm purpose and shareholder purpose all need to align." This cosmic coincidence is not, he says, "just an FCA objective, but is increasingly a broader societal expectation". He cites as examples of these expectations the "ever more insistent calls for firms and their leaders to step forward on climate change, on diversity and inclusion, on environmental, social and governance issues, on ethical use of data, on acting in the best interests of customers and not just to act so as to optimise profitability".

And if you don't do this, the prospects for your firm are poor. Your employees will be dissatisfied and lack motivation. As he says, "firms need to offer meaning, not just money." Your customers will desert you – "consumers who experience firms acting purely and selfishly for profit lose trust and may vote with their feet." And, crucially, "shareholders that are more sensitive to reputational and regulatory risk may decide they want to invest in firms that have healthy and sustainable profits." Because, by definition, your own lack of – or merely material – purpose will mean that your own profits are neither healthy nor sustainable.

And then comes the sting. As Davidson says, "if a firm's purpose and associated business model is contributing to, or exacerbating, the risk of potential harm, then firms can expect increased supervisory scrutiny." So, if the FCA doesn't like your purpose, they'll be on to you.

And there are many who would raise three cheers for the FCA. Such are the issues facing us all today that our traditional purposes are no longer enough. It's more important that we have a sustainable world in which to live rather than we all have a bit more money. It's a more important priority that we cease to earn income from extractive industries than that we spend time focussing on the minutiae of detailed compliance. Unless we start thinking long term – and the tyranny of the short term runs through the whole DP – we'll all be dead, or at least far poorer in a much wider sense than we ever would have been due to an old-fashioned financial scandal. So, firms really should consider wider societal goals as part of their purpose.

But really? Is that right? Should we accept this position as though it were tablets of stone, or does it bear closer scrutiny? There are a number of issues with this focus on broad purposes away from profit, and these are discussed by some of the DP's contributors who hold senior positions in firms. While they are careful not to disagree with Davidson's starry-eyed objectives, they do sound a note of caution.

In arguing the positive benefits of having a unifying purpose, Davidson cites another astral example. He says: "There is an oft told story that JFK visited NASA in 1962 and asked a janitor, 'what are you doing?'; the janitor answered, 'Mr President, I'm helping to put a man on the moon'." For Davidson, the fact that the lowly janitor had bought into the wider purpose of NASA is proof positive of the value of a unifying and motivating purpose for an organisation as a whole. As he says: "as a leader, imagine how it would feel to know that your employees feel that level of inspiration as a result of being part of your organisation."

This can hardly be a helpful illustration. As a leading public sector organisation of its day, I doubt whether there was ever any shortage of funds at NASA. I'm sure that if firms were similarly unconstrained, they too would be able to take a wider perspective. In 1962, putting a man on the moon must have been the sole and overriding purpose of NASA. This is not a useful example when Davidson is asking firms to consider "any number" of things in its purpose. If firms were to be so focused on one thing, as the janitor knew NASA was, what would that be? Back to that later…

And what of the motivation of staff? How do we know what brings people to work? A recurring theme in the paper is that staff, customers and shareholders are not solely motivated by money. Money is only one of many considerations that bring people in to work. How do we know this? It's not clear from the DP what the evidence is, but surveys have been done in this area that support this premise. But I'm a bit sceptical of this sort of polling evidence. What would anyone say when asked "is money the most important thing bringing you in to work?" Who wouldn't say that it was one of many factors? But what would their reaction be if they were told that they were going to take a pay cut and that the difference in their pay was going to be donated to good causes? Would they still feel quite so motivated? Maybe I'm too cynical, but surveys such as these suffer from the same frailties as election polling. People want to tell the pollster that they are voting Labour, but when it comes to the crunch they don't. Similarly, you shouldn't feel you're missing out when you read surveys that tell you that everyone but you is having sex three times a week. People lie.

But is it different for young people? Are they motivated another way? Are they really only happy to work for businesses with wider social purposes over and above making money? Not those that I've seen – the start-up entrepreneurs working in the digital economy, aiming to be the next Bill Gates or Steve Jobs. We all may admire their altruism, but it's their billions that got them there and allowed them to have enough to be able to give it away.

And that's the point made by some of the business contributors to DP20/1. Several make the point that profit is not a dirty word – it's the foundation of everything. As Joe Garner, the CEO of the Nationwide Building Society, says: "There's nothing wrong with making a profit. In the same way that profit without a higher purpose does not work, purpose without profit doesn't work either." Even when he qualifies his remarks by saying that "when profit moves from being an outcome to the primary purpose of an enterprise – that's when things go wrong" he still points out that "without profit, no business can exist for very long".

Garner argues that business does indeed have higher goals than making profit – to serve customers and improve society. But he recognises "that businesscan only move up that hierarchy of business purpose if an organisation is making sufficient profit to be able to".

And what of those wider objectives? While Davidson mentions a long list of purposes – "social, ethical, consumer-driven or people driven" – the business contributors to DP20/1 are far more focused in their objectives. Garner speaks of serving customers in the first instance, and then improving society. He acknowledges that this is from the perspective of a mutual society "founded for a social purpose to 'improve living conditions for the industrious classes'… This makes it easier for us to put £40m of capital to help fund the development of a community in Swindon…"

Garner's more acute business focus is echoed by Amra Balic and Anthony Manchester, respectively the managing director, head of EMEA Investment Stewardship and managing director, Global Public Policy Group, at BlackRock. They recognise the importance of purpose, but for them it is not a shopping list of well-meaning objectives – it is central to the business. Thus: "we think of… 'purpose' as another way of expressing 'long-term strategy'." And when speaking with invested companies, "we do not tell their leaders what their views should be, nor do we make value judgements about their chosen purpose. Instead, we encourage long-term thinking so that the companies do not succumb to short-term pressures to distribute earnings, and, in the process, sacrifice investments in employee development, innovation, and capital expenditures that are necessary for long-term growth."

And that's one of the big stumbling blocks to achieving this: short termism. Davidson recognises this as one of the things that "gets in the way". Will Goodhart, CEO of the CFA Society of the United Kingdom, writes that "identifying purpose, setting incentive structures that are aligned to purpose and then living up to the promise of purpose takes time – time that a CEO may not feel that they have." Michael Cole-Fontayn, chair of the Association for Financial Markets in Europe, and Mark Yallop, chair, FICC Markets Standards Board, write about this too. Wholesale firms "are still overwhelmingly judged on short-term results… the conflicts between long-term aspirations of corporate purpose statements and the short-term demands of markets that wholesale firms are engaged in are extremely hard for single, or small groups of, particularly publicly quoted firms, to reconcile… long-term, sustainable business is easier to achieve in some types of wholesale financial services business than others."

These are not the last roars of dinosaurs being dragged unwillingly to a bright new dawn, but proper considerations made by people who actually have to implement this. The recognition of the importance of the short-term allows firms to survive through the medium to the long term. That may mean some dilution of purposeful objectives, but at least you're surviving to implement them.

So where does that leave us? Certainly, firms should think about what their purpose is, and not be ashamed to define this in commercial terms. Customers come first. Wider social goods are all very well and, if you want to promote them, there's one thing that we can do which will help – pay your taxes.

And, as Jonathan Davidson orbits these issues, looking into his heavenly charts to divine when and how it is that "the stars of employee purpose, social purpose, firm purpose and shareholder purpose all need to align", he should perhaps look at those firms that do have satisfied long-term employees, make a contribution to the wider society (by paying their taxes, and maybe more besides) and have a stable shareholder base. What is it that these firms have? What are they focused on? What would their janitors say when asked what they're there for? I'd guess that the one thing those janitors would say they have in common is this: they're there to make a profit.

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