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Editorial

Executive summaries

Risk, ethics, leadership and the holy grail!

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Cass Business School

The impact of the recent financial crisis on organizations has been to drive a set of immediate responses that might not be the best long-term solution. The laudable desire to stop things going wrong could be leading some to focus on the "quick fix" while missing the underlying causes. People do not generally deliberately do things wrong, so maybe it is because they do not realize what they are doing is wrong that is the cause. This often places organizational failures within the responsibilities of leadership, not "bad" employees. Having employees who care about the organization and know what its objectives and values are will not only enable more effective risk management but also potentially add to profitability. Revisiting what we are seeking to achieve via leadership and how we do it may provide the long-term solution to many of our organizational challenges, not just those related to risk.

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Risk, ethics, leadership and the holy grail!

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Abstract
The impact of the recent financial crisis on organizations has been to drive a set of immediate responses that might not be the best long-term solution. The laudable desire to stop things going wrong could be leading some to focus on the "quick fix" while missing the underlying causes. People do not generally deliberately do things wrong, so maybe it is because they do not realize what they are doing is wrong that is the cause. This often places organizational failures within the responsibilities of leadership, not "bad" employees. Having employees who care about the organization and know what its objectives and values are will not only enable more effective risk management but also potentially add to profitability. Revisiting what we are seeking to achieve via leadership and how we do it may provide the long-term solution to many of our organizational challenges, not just those related to risk.

Over the past few years in the financial services sector, many organizations say that they have been trying to change their culture and manage risk more effectively. This, they say, is driven by the need to ensure that nothing can ever go wrong in their organizations in the future. What they really mean is that never again will things go so very badly wrong as they did in the financial crisis. Having nothing go wrong in an organization populated with human beings is an impossibility. Things will go wrong. What they are really seeking is the prevention of the fall of one domino hitting another and starting a ripple effect across the globe which spreads and multiplies the damage.

Some might suggest that we should aggressively seek to prevent any errors occurring, but that will result in a culture where making any mistake is seen as seriously career limiting. This will then inevitably lead to people at all levels either not doing anything in an attempt to avoid mistakes or trying to cover up the inevitable mistakes that do occur even if the organization needs to be aware of what has happened. Eventually, one of these will get through the system and cause a major issue, particularly in combination with other small mistakes. Combinations of a number of small mistakes can result in disasters. The sinking of the Titanic was one of these. For example, had a last minute change in the crew officers not occurred the key to the binocular cabinet would not have been taken off the ship, and the ice look-outs would have had binoculars and the disaster might have been averted.

The chief risk officer of a well-known global bank said to me over lunch one day, "You know Chris with 80,000+ people worldwide it's clear that someone somewhere must be doing something wrong 24 hours a day. My systems just stop a problem from becoming a disaster, but if I could stop people from doing things wrong in the first place then I would sleep easier at night." That was just before the financial crisis; which rather proved the point.

From my perspective, the political hype about the widespread risk taking in banks, the regulators' ever-louder calls for "better culture" (when most of them have no idea what that means in practice) and some institutions' use of the traditional knee-jerk responses via online tests and workshops have in themselves created a dangerous culture. This is the "we must be seen to do something so just do anything that comes to mind even if we have no idea at all if it will have any real effect" view. In reality, they are both counterproductive and dangerous. Counterproductive, as it distracts time and resources from actions that could make a real difference, and dangerous as it inevitably creates a false sense of security, e.g., that everything is now safe as everyone has been through a risk workshop and signed an undertaking. If only it was that simple.

In my view, a much deeper analysis of why things go wrong in organizations would have enabled much greater impact and value in risk management and development of ethics. This would have shown that a proportion of errors will occur statistically in any set of operations and that while the desire may be to stop all errors the reality is that some will occur. It is then a case of minimizing the number that do and then minimizing the damage that those errors cause by dealing with them and containing the impact.

The reality is that virtually no one goes to work with the intention of making errors. It is not something anyone other than the criminal or malicious would do. Thus, other than that extremely small group of individuals any other mistake is just that — a mistake. However, it is not quite that simple. If we delve deeper into these "mistakes," we find that they fall into two categories: things that people did but should not have done and things that people did not do and they should have. This does not apply only to financial services. In the vast majority of serious organizational failures over the past 50 years, from the financial crisis to Gulf of Mexico or Bhopal to air accidents, the causes of each can be attributed to one of these failures. Example of things that were not done but should have been are: "yes lets reduce the maintenance on this refinery to save money and make more profit," or "yes lets deal in these products without really taking time to assess the risk as they make a lot of money." Conversely, there are the things done that should not have been done, such as "it might be immoral but as it makes money and it's not illegal then let's do it."

Time and again, in organizations across the globe, things that should not have happened do for one of these reasons, or indeed a combination of both come together and bring about a disaster. Given that we cannot prevent these things totally, the logic is to minimize them and then ensure they are contained.

Minimization is not only a systems issue — it is, in reality, more of a leadership issue. Systems only catch what has been started, whereas leadership, both directly from leaders and indirectly via culture, creates a psychological framework that minimize even the starting of actions that might lead to mistakes and problems. This is often called the "moral compass" that some organizations occasionally seem to mislay at their cost.

The other complication is that the location of the risk has moved in the past few years, making an effective solution more difficult. This has been driven by a greater awareness and understanding of the dangers of getting it wrong at the top of organizations, which has moved the potential risk profile downwards.

Research from CEB/SHL data for the Wall Street Journal from December 2013[1] help clarify this. They examined 20,000 managers on their approach to decision-making (understanding risk and its impacts) and communications (making sure everyone is clear on key objectives and caveats). What they found from the data in Europe, for example, was that at the most senior levels just 1 in 21 leaders was perceived as presenting a risk to the organization. The global average is 1 in 14. At the next level down this rose to an average of 1 in 14, by the middle management level it was 1 in 8, and potentially even higher when you get to the junior management level.

Junior management levels are undoubtedly worse because of lack of experience. But the greatest danger is at middle management level, because they are able to make operational decisions that initiate potential disasters of numerous types. Moreover, they are in key positions to monitor and develop junior leaders. The CEB/WSJ, to some degree, lays the blame for this at the door of over-promotion of technical experts. I would rather say it is a failure to make sure that any technical experts who are needed in such roles are also effective leaders.

Regulation may deal with certain issues but it is impossible to regulate for every eventuality, and there are many things that one of your people could do that might not be contrary to legislation or regulation but might be seriously damaging to your reputation. Reputational risk is an even more complex issue. It links not to defined rules but variable

[1] http://chrisroebuck.co/files/2014/02/Companies-need-to-be-more-aware-of-risk.pdf

interpretations of what the “right” behavior is in any situation. Here, there are sometimes no common perspective, and what is viewed as acceptable inside the organization may not be viewed as such from the outside. This reputational risk can only be dealt with via culture and leadership and poses one of the greatest threats to organizations going forward. The ability of “reputational bad news” about your organization to spread virally through social media and other channels is something regulation can do nothing to halt and which is becoming more and more powerful.

What is interesting is that this “risk” is often separated from “leadership.” For some reason, risk management is dealt with as a different issue from leadership. This is despite all the evidence, too voluminous to list here, that leadership is the key determinant of risk behavior in terms of its direct and indirect effects. So the analysis of the problem “we have to do something about risk” and indeed “we have to do something about ethics” should lead to “so we have to do something about leadership;” but it rarely does. This is true even in those financial institutions where significant action is being taken on risk and ethics but where it is not being linked with leadership issues in sufficient depth to make sure an effective solution is delivered, which is then embedded into day-to-day behavior.

The change in mindset required to deal with the issues around risk and ethics are unlikely to be solved by a “course” as it requires a coordinated refocusing of the way people think and work. This involves everything from senior management to line managers and systems to policies. It also involves emotion as well as rational argument. Making such a change work is a significant undertaking and its impact is much wider and has much greater potential than just dealing with the current hot topics of “risk” and “ethics.” Inherently, in changing employee mindset you are able to influence their approach to many things, not just risk and ethics.

It impacts on their wider performance, through the degree to which they apply effort or not, the things they apply that effort to, their ability to work with others and how they enable organizational objectives to be achieved. This obviously includes things other than risk and ethics. My view is that, to get the risk and ethics right you have to get the complete picture right or you are delivering a partial solution.

The development of a holistic approach to employee behavior brings about greater potential benefits that are significant. As well as managing risk better and developing ethical behavior your organization could (1) get up to 57% more effort and 20% more performance from your people,[2] (2) improve the performance of new team members by 25% in the first year,[3] (3) deliver better customer service,[4] (4) as an individual leader get within the top 8% of your peers so that you have a 75% chance of being a top performer at the next level – thus increase your chances of promotion,[5] (5) improve organizational operating income by 52%,[6] (6) be significantly more effective financially than competitors,[7] (7) increase total shareholder return by 9.6% over 3 years,[8] (8) reduce the chances of your talent being taken by competitors by 87%,[9] (9) increase the willingness to innovate from 3% of employees to 59%,[10] (10) increase profits by 5.8% year-on-year more than comparable business units,[11] and (11) more than halve sickness absence.[12]

Thus, if you need to change mindsets to deal with the risk and ethics challenges and that change could deliver the sort of benefits outlined above, why wouldn't you do it?

Sadly, even now there is inherently something going wrong in organizations around current leadership generally. Data from Hay Group paints a picture where about 60% of employees

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2 Corporate Leadership Council, 2004, "Employee engagement framework and survey"
3 Corporate Leadership Council, 2004, "Employee engagement framework and survey," p89
4 Hakanen, J. J., R. Perhoniemi, and S. Toppinen-Tanner, 2008, "Positive gain spirals at work: From job resources to work engagement, personal initiative and work-unit innovativeness." Journal of Vocational Behavior 73(1), 78–91; Rucci, A. J., S. P. Kirn, and R. T. Quinn, 1998, "The employee – customer profit chain at Sears," Harvard Business Review (January– February), 82–97; Barber, L., S. Hayday, and S. Bevan, 1999, "From people to profits: the HR link in the service-profit chain," Institute for Employment Studies, Report 355
5 Corporate leadership Council, 2005, "Realizing the full potential of rising talent," p89
6 Towers Perrin, 2006, ISR employee engagement report
7 Fleming, J. H., C. Coffman, and J. K. Harter, 2005, "Manage your human sigma," Harvard Business Review (July–August), 107–114; Harter, J. K., F. L. Schmidt, E. A. Killham, and J. W. Asplund, 2006, "Q12® meta-analysis," Gallup
8 Corporate leadership Council, 2005, "Realizing the full potential of rising talent," p6
9 Corporate Leadership Council, 2004, "Employee engagement framework and survey"
10 Krueger, J., and E. Killham, 2007, "The innovation equation"' Gallup Management Journal
11 Gallup, 2008
12 Harter, J. K., F. L. Schmidt, E. A. Killham, and J. W. Asplund, 2006, "Q12® meta-analysis," Gallup

globally are keen to give their best, but that on average 33%, rising to 42% in Europe and the Middle East, feel that their organizations obstruct them from delivering it.[13] Set against this background, the chances of getting people to think and behave differently about risk and ethics, unless the issues causing this underlying problem are also solved, is nonexistent.

Further, the financial crisis made the situation more difficult for those at work as the headcount reductions it drove mean there are now fewer people in organizations to deliver what is required. In most places headcounts have often been reduced more than workloads. As a result, employees are under more and more pressure. Research by the Corporate Executive Board [CEB (2013)][14] and supported by other studies shows that between 2009 and 2012 88% of employees had experienced an increase in workload, 56% had increased hours of work and 78% had experienced an increase in the team workload.

The percentage of employees who said that they did not have sufficient time to complete the work they were expected to do increased from 32% to 55% over the same period, and the proportion of time spent multitasking increased by 15%. Furthermore, everyone is now having to deal with more information, with 76% of employees saying that they are spending more time either finding or dealing with data. This is probably distracting them from higher priorities. All of the above increase the chances of people making mistakes.

In addition, there is still a mindset among senior leaders that "delivery" is more important than anything else. For many, this means focus on only delivery. The problem is that pure delivery focus is counterproductive. While the evidence based on figures alone might suggest that a leader is performing and delivering what is required, this maybe a poison chalice. Delivery "addicted" leaders seems to be having more impact on organizations and it is a negative one. The delivery addicted individual not only wants to deliver for career purposes but also views it as the key internal driver for their self-respect. The problem is that they fail to recognize the impact this has on others. If leaders focus too much on the task and delivery without developing their relationship with people, it will reduce

[13] Hay Group, 2012, "Depressed employee engagement stunts global business performance," July
[14] Corporate Executive Board, 2013, "Driving breakthrough performance in the new work environment"

the performance of the team long term. Further, there is a danger that too much pressure on the team from an excessive drive to deliver and achieve ends up causing short cuts, poor communications, increased risk and poor collaboration and reduces trust and morale.

Research has been done on the effects of failing to balance the desire to achieve with bringing the team with you through collaboration rather than dragging them by coercion.[15] Spreier et al. (2006) show that those leaders seen as high-achieving fell into two groups — those that just pushed the team hard by pace setting, which led to demotivation in the team, and those leaders who delivered results by creating a high performance environment using collaboration, vision, coaching and participation as well as pushing the pace. Thus, even the seemingly "high performing" line manager could, in reality, be creating both damage and risk for the organization.

So, set against this background, the pressure to deliver improved performance from fewer people is, potentially, more likely to be encouraging people to take risk and forget ethics rather than focus more on them. Contradictory messages are being sent down through organizations yet again. "Deliver the financials but also manage risk and be ethical." Something has to give, and it is probably going to be the ethics and risk. Many organizations seem to have a problem managing the ambiguity of doing both.

From a practical perspective, having 55% of employees saying they don't have enough time to deliver what they have been asked to deliver poses very significant questions about the quality of existing leadership. How can you be a competent leader if you give people more work than they can do in the time you have allowed?

Further, the new slimmed-down structures mean that people not only have more to do but have to work together better and the traditional more siloed approach is no longer effective. Partnership working and collaboration is key for the future. According to the CEB (2013), between 2002 and 2012 the relative importance to business unit profitability of

[15] Spreier, S. W., M. H. Fontaine, and R. L. Malloy, 2006, "Leadership run amok, the destructive power of potential overachievers," Harvard Business Review June, 1–10

individuals collaborating across the organization as opposed to working on their own tasks changed dramatically. The importance of individual task working fell from 78% to 51% and the importance of collaboration increased from 22% to 49%. This represents a doubling of the importance of collaboration in these slimmed-down organizations, which makes collaboration with others as important to profitability as working on your own tasks. Getting 50% of employees to contribute organizationally through collaboration could add 4% to profitability, and if all of your staff reaches that collaborative level you could add 12%. It is good news if you can make that happen. But there is little evidence that it is, and ineffective collaboration increases risk.

But it gets worse. Despite all the current challenges about workloads, complexity, demanding customers and limited resources discussed above, organizations, CEOs and investors are expecting better and better performance. The annual objectives set by many organizations demand constant improvements year-on-year. CEB (2013) study shows that in general terms, most CEOs and senior executives say they need a 20% increase in performance to achieve their targets. Set that against the current environment where people are already close to, or at their limits, then something has to change to make this possible, or things will "go wrong" again.

Is there a solution? The answer is "yes", and one that will deal with all the associated issues of concern at the same time — risk, ethics, performance, customer service, innovation and more — by taking a holistic approach to employee behavior, not one that focuses on ad hoc initiatives that cover only a small element of what is needed.

Taking a simple approach is what works. The basics must be in place before adding the more complex elements. Only two steps are needed:

1. Maximize the discretionary effort of your staff by motivating and inspiring them – Mach 1 leadership
2. Deliver maximum return by focusing that effort onto what optimizes personal and organizational benefit – Mach 2 leadership

The impact of both of these components on organizational performance is significant. But the power of the combination is that it also impacts all the critical elements that the organization needs to get right, from risk and ethics to cost efficiency and brand building. This is because the change in mindset enables the creation of an aligned community of effort and collaboration that breaks through the barriers of the traditional silo structures that restrict collaboration. It enables staff to fully understand and operate within the required risk or ethics frameworks more easily. The evidence this works is clear. Both strategic leaders and operational leaders have a role to play.

As well at getting risk and ethics right overall this could deliver up to 30% more effort from 60% of staff in the same time for the same money. Line managers could get significant improvements in effort from individuals. This is by simple day-to-day actions, such as:[16]

- Explaining to an individual or team how what they do fits into the bigger picture (+30.3%)
- Making sure that they give fair and accurate day-to-day feedback on performance (+39%)
- Making sure that every team member has a plan to develop them and their performance that the line manager helps them implement (+38%)
- Showing they respect their people as people can increase performance by +26.1%

But senior leaders must contribute as well via personal example and by creating the right environment through culture and systems. They must create a new more collaborative world of work. CEO and senior managers can improve how much discretionary effort their staff make if they show that they:[17]

- Are open to new ideas (+22.9%)
- Care deeply about employees (+20.7%)
- Make employee development a priority (+19.7%)
- Are strong in leading and managing people (+15.6%)
- Are strong in strategy selection and implementation (+15.6%).

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[16] Corporate Leadership Council, 2004, "Driving employee performance and retention through engagement"
[17] Corporate Leadership Council, 2005, "Driving employee performance and retention through engagement," p 67

As was hinted before, it is not all about rational analysis. Emotion is absolutely key. We know that an employee's decision to give high performance is 57% rational and 43% emotional. Furthermore, 80% of the emotional element is under the control of the individual's line manager. Giving a rational business case to do something is sufficient to get base level performance, but providing an emotional driver will get the best from people. But, it is also about building loyalty. It is even more powerful if the organization can create a strong emotional link with the employee — it can increase their effort by up to 43.2%[18] and a line manager who achieves this can reduce the chance of talent loss to competitors by up to 87%.

So this is not just about being nice to your staff, it is about delivering the best performance possible but within your risk and ethics framework.

On the capacity issue raised earlier, the fact that 55% of employees say they don't have enough time to do the work they are given, does not mean, in my perception, there is no spare capacity. It is likely that some of this is caused by ineffective prioritization, with work that is not critical to the organization's success taking up too much time. Employees who are not delivering maximum effort will not be effectively prioritizing. Bureaucracy also compounds the problem by removing focus from key priorities. So, it is probably wrong to assume that these figures mean that people have no capability to add more value to the organization.

Thus, while there are significant challenges to organizations in developing performance and delivery while managing risk effectively and maintaining ethics, it is a possibility if a more holistic approach through Mach 1 and Mach 2 leadership is taken. The practical evidence for this exists in a number of environments that I have practical experience in from the Harvard case study: "UBS towards the integrated firm" to application of Mach 1 and 2 to the UK National Health Service and other organizations globally. The undoubted reason for the success of the process is that by using a holistic approach you make sure that everyone in your organization: a) is aware of your strategy b) knows how they

[18] Corporate Leadership Council, 2005, "Driving employee performance and retention through engagement," p 37

contribute to it, c) understands what they need to do to achieve that and d) wants to do so. It is impossible to envisage a scenario where any organization could maximize its effectiveness without all of these in place.

This ensures that effort is maximized and that the only effort that is applied in the organization is that which delivers the organization's strategy. There are no wasted resources, no wasted time, no confusion, and full clarity to allow maximum return on investment. Risk and ethics are dealt with as employees understand the "moral compass" and genuinely want to protect their organization. Furthermore, if things ever do go wrong, armed with the knowledge of the organization's desired destination, those involved can quickly adapt plans to enable a change of operational action, but one which still meets the strategic objective. Just as important, they can do so without having to wait a long time for clarification on what they should do from those higher up as they already have the knowledge they need.

In the final analysis, this is based on thinking about the risk and ethics issues not from the perspective of senior management but from the perspective of those members of the senior management who want to implement the process. Too often, we forget that "beauty is in the eye of the receiver, not the giver," so if what we tell people to do has no relevance or benefit from their perspective they won't fully engage with it, and therefore don't do it properly and to the best of their ability.

If we get this right we will get the holy grail, effective operational and strategic risk management and ethical behavior. You also get an aligned community of effort and collaboration that delivers world class performance as well. Just through two simple steps. As a finance director said, "This is a 'no brainer,' we should have been doing this years ago." But it seems that many organizations just cannot understand that risk and ethics are part of a much wider picture.

Conclusion

The challenge for strategic leaders is to move from silo thinking to holistic thinking if this is not something they have been gradually developed to do as they become more senior. It is a simple fact that organizations work more effectively when they operate as one organization rather than a collection of associated functional units that seek their own slightly unaligned objectives and do not see the value in collaboration for the common good. Creating this holistic mindset in both self and others is the first step on the road to success. When followed by clear communication of what is needed, why and how it benefits everyone, the vision and operational delivery combine into aligned action.

In the end, the more senior leaders can create "an aligned community of effort and collaboration," the better the organization is likely to do in all areas from risk management to customer service, innovation, cost efficiency and everything else that drive success. The evidence for this is now indisputable; the road map to implement is clear, so there is no further excuse for inaction.

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