



HONG KONG MONETARY AUTHORITY  
香港金融管理局



# Report on Review of Self-assessments on Bank Culture

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# Report on Review of Self-Assessments on Bank Culture

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## Executive Summary

Following the announcement of the supervisory measures for bank culture in December 2018, the Hong Kong Monetary Authority (HKMA) commenced the self-assessment exercise in early 2019 by requiring 30 banks (including all major retail banks and selected foreign bank branches with substantial operations in Hong Kong) to conduct self-assessments on their culture enhancement efforts and benchmark themselves against the findings of major conduct incidents outside Hong Kong. The selected banks were given six months to complete the exercise. The HKMA has reviewed the self-assessment reports from the selected banks to draw insights from the submissions with a view to providing a range of practices as well as identifying common themes for reference by the industry.

### Range of Practices

Overall, the selected banks agree with the need to foster sound bank culture. As there is no one-size-fits-all approach when it comes to culture, the self-assessment exercise is intended to provide an opportunity for the banks to reflect on any insights, lessons learnt and issues encountered on their culture efforts, but not a check-box type compliance exercise. While most banks recognised the self-assessments as an opportunity for the authorized institutions' ("AIs") board and senior management to reflect on their own culture, we noted that there were variations in the quality and depth of the self-assessments.

Based on the self-assessments, the banks covered in the exercise have implemented a range of culture initiatives and made significant progress in promoting sound bank culture over the past two years. We have identified a range of practices under each of the three pillars: (1) governance, (2) incentive systems, and (3) assessment and feedback mechanisms, which can be a handy reference for AIs as they move on and devise further culture enhancement measures.

### Common Themes

AIs are encouraged to pay more attention to some common themes that have been identified from the self-assessments as follows:

- (a) Further work is needed to ensure their incentive systems are designed to promote sound culture and prevent incidents of misconduct;
- (b) Stronger links are required to connect their Hong Kong operations with the culture efforts of their headquarters or upstream entities as well as their downstream operations, as appropriate;
- (c) Deeper analysis is expected to benchmark themselves against the findings from the reviews of the major overseas misconduct incidents;
- (d) More focus is needed to facilitate the undertaking by relevant staff of the continuous professional development under the Enhanced Competency Framework or by other professional bodies to complement the effort of promoting sound culture;
- (e) More effort is needed to tackle the key challenge of culture assessment to identify the gaps between current progress and desired culture;
- (f) More work is needed in promoting an environment which provides “psychological safety” to encourage staff to speak up without fear of adverse consequences; and
- (g) Sustained effort is required in driving cultural changes and banks should be mindful of “culture fatigue”.

## **Next Steps**

While the key observations are identified from the selected banks covered in the first phase of the self-assessment exercise, these key observations will be relevant to all AIs. We thus encourage all AIs to pay attention to the common themes identified, make reference to the range of practices, and consider whether such practices are effective in driving cultural changes based on their desired culture, values and behavioural standards.

We would also like to remind the AIs that were not covered in the first phase of the self-assessment exercise that, they are still expected to reflect on their own culture

enhancement efforts, and take into consideration the key observations shared in this report.

The insights drawn from the self-assessments have informed the HKMA's future work on bank culture supervision. We will, as next steps, conduct focused reviews with an aim to dive deeply into the incentive systems of front offices in the business of distributing banking, investment and insurance products in retail banks. As for culture dialogues, we have already commenced such dialogues with several AIs in 2019 and the engagement with AIs will continue going forward. We will inform AIs selected to take part of the details individually.

# Chapter 1 Background

## 1.1 Bank Culture Reform

- 1 In March 2017, the HKMA initiated a Bank Culture Reform to develop and promote sound corporate culture that supports prudent risk management and contributes towards incentivising proper staff behavior leading to positive customer outcomes and high ethical standards in the banking industry.
- 2 While it is recognised that there is no “one-size-fits-all” approach, the HKMA expects AIs to adopt a holistic and effective framework for fostering sound culture within their institutions through three pillars: (1) governance, (2) incentive systems, and (3) assessment and feedback mechanisms. Practical guidance on these three pillars was also provided to all AIs. Please refer to the circular issued by the HKMA dated 2 March 2017 on “Bank Culture Reform” (“2017 Circular”) for details.

## 1.2 Supervision for Bank Culture

- 3 In December 2018, the HKMA announced several supervisory measures for bank culture following consultation with the industry. One of the supervisory measures was to commence a self-assessment exercise among AIs.
- 4 The HKMA had selected 30 banks (including all major retail banks and selected foreign bank branches with substantial operations in Hong Kong) for inclusion into the first phase of the self-assessment exercise. These 30 banks were required to review and report their governance arrangements as well as policies and procedures in relation to corporate culture and the implementation of enhancement measures in fostering sound bank culture with respect to the 2017 Circular. The HKMA had designed a template to assist the banks in conducting the self-assessments. The template was divided into two parts. The first part “Culture Questions to the Board” comprised a set of high-level questions, aiming to serve as an opportunity for

the board of the banks to reflect on any insights, lessons learnt and issues encountered in the implementation of enhancement measures. The second part consists of specific questions for banks to review and report their governance arrangements as well as policies and procedures in relation to corporate culture and the implementation of enhancement measures in fostering a sound bank culture. Please refer to the circular issued by the HKMA dated 19 December 2018 on “Supervision for Bank Culture” (“2018 Circular”) for details.

### 1.3 Range of Practices

- 5 The review has identified a range of practices across the banks covered in the self-assessment exercise, including examples of how these banks approach their culture reform along the above three pillars that may be relevant to other banks as they undertake initiatives to enhance their own culture.
- 6 We recognise that there is no “one-size-fits-all” approach. Banks are therefore encouraged to make reference to the range of practices and examples to consider whether these or similar practices and examples could apply to their banks. The practices and examples are not exhaustive and banks can explore different culture enhancement initiatives based on the bank’s desired culture, values and behavioural standards as long as the culture initiatives are effective in driving cultural changes within the bank.
- 7 For the avoidance of doubt, while all the 30 AIs selected to participate in the first phase of the self-assessment exercise were licensed banks, and that restricted licence banks (“RLBs”) and deposit-taking companies (“DTCs”) often have simpler business models and operations, are relatively smaller in size, and have smaller number of staff, the expectations on banks are generally applicable to all AIs. Moreover, RLBs and DTCs are also encouraged to make reference to the good practices identified in this report when pursuing their own culture journey as appropriate.

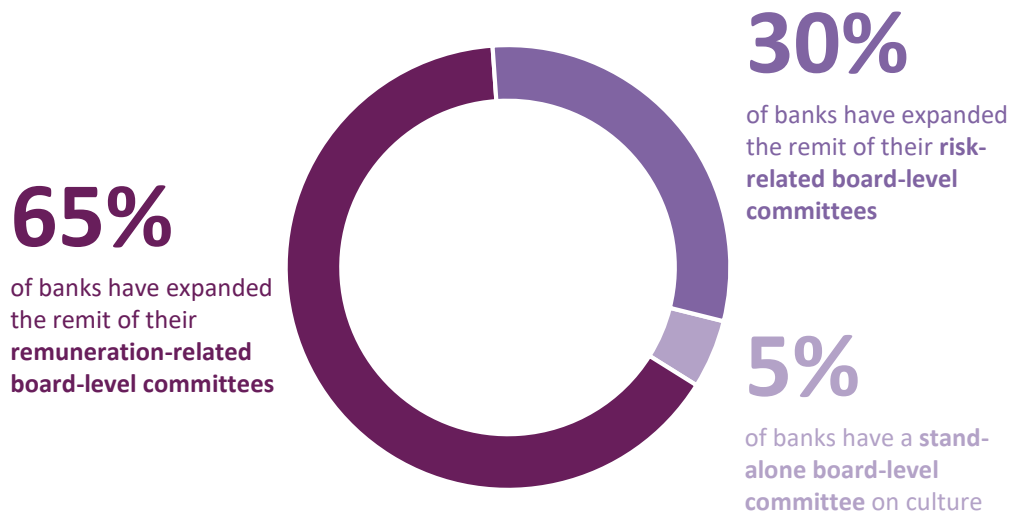
## Chapter 2 Range of Practices – Governance

- 8 Culture defines ethical values and desirable behaviour within the bank that must be set and owned by the board and senior management and supported by sound governance framework. On the first pillar of “Governance”, the board should play a leading role in establishing the bank’s desired culture, values and behavioural standards that promote prudent risk-taking and fair treatment of customers. Senior management is expected to put in place effective mechanisms for ensuring that the bank’s desired culture is understood and shared by all levels of staff.

### **2.1 The board and senior management are responsible for setting and taking ownership of the culture, values and behavioural standards of the banks**

- 9 We recognise that leadership of banks plays a significant role in shaping culture of the bank by setting the appropriate “tone from the top”. Independent non-executive director (“INED”) also plays a pivotal role in instituting or pushing for sound culture at the board level. Our review indicated that all locally incorporated banks covered in this exercise have a board-level committee, chaired by an INED, to advise and assist the board in discharging its responsibilities for the bank’s culture-related matters.
- 10 As illustrated in the chart below, almost all locally incorporated banks covered in this exercise expanded the remit of their existing board-level committees to encompass culture-related responsibilities with the most common one being remuneration-related committees followed by risk-related committees. Such expansions also predominantly occurred after the issuance of the 2017 Circular.

**Figure 1 How locally incorporated banks (major retail banks) use board-level committees to oversee culture-related matters**



- 11 As for overseas incorporated banks covered in this exercise, the culture, values and behavioural standards of these banks are generally set at group level and adopted locally. Culture initiatives of these banks are also predominantly driven at group level with board-level oversight at either global or regional level on culture-related matters. Most of these banks have board-level committees at global or regional level either focusing on culture, ethics, integrity and conduct while some have their culture agenda covered under risk management, remuneration and governance board-level committees.
- 12 We observed that the board of many banks covered in this exercise has also set up working groups or taskforces that focus on culture and provide steer on the implementation of culture initiatives, and in the case of most overseas incorporated banks covered in this exercise, to provide support on the ground at the local level.

## **2.2 The board-level committees need to have a regular process to review the effectiveness of banks' overall culture efforts**

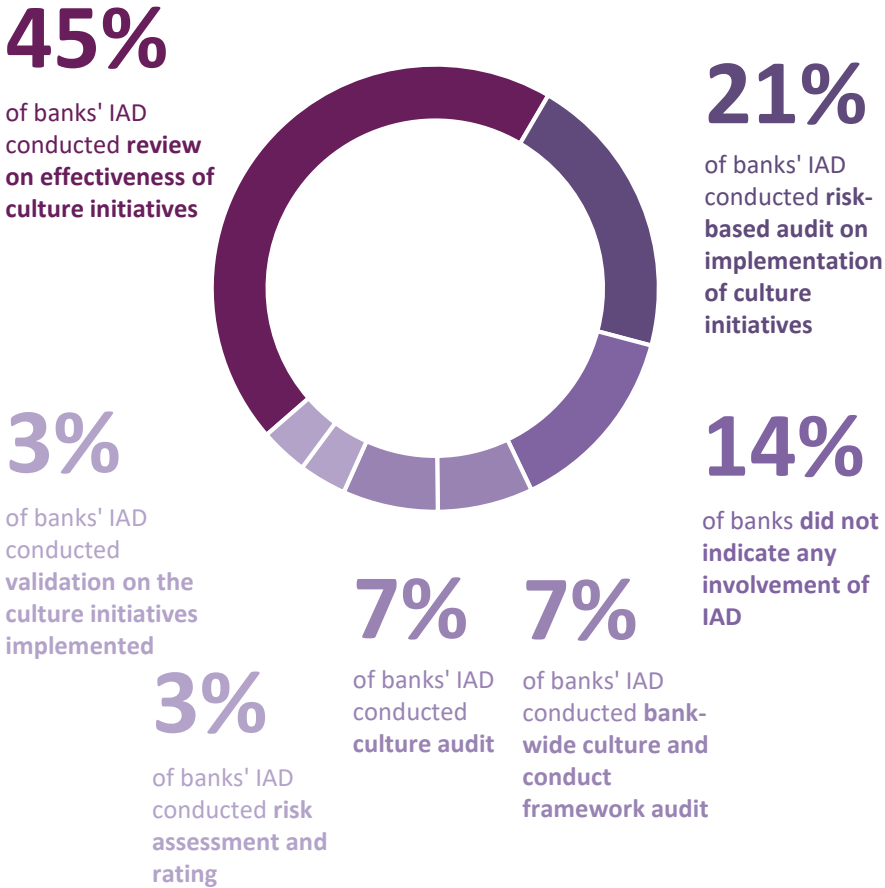
- 13 Regardless of whether banks have a stand-alone committee or expanded the remit of an appropriate board-level committee to encompass culture-related responsibilities, the board-level committee should dedicate appropriate time and attention to culture-related matters, and more importantly, to have a regular process to review the effectiveness of the overall culture efforts of the bank.
- 14 We observed that the board or board-level committees of most banks covered in this exercise review the effectiveness of the overall culture enhancement initiatives at least annually, while some banks review the updates of their culture enhancement initiatives on a quarterly basis. The board-level committee of most banks covered in this exercise also approve and review the relevant statement which sets out the bank's culture, values and behavioural standards annually, and in the case of most overseas incorporated banks covered in this exercise, such statements are generally approved or reviewed by board or board-level committees at global level.
- 15 As illustrated in the chart below, the more common culture-related matters that were brought to discussions at the board or board-level committees include review of the progress of the bank's culture initiatives; development of, and in some banks, also review of, the culture dashboard and discussions on the dashboard updates; review and approval of culture statements and behavioural standards; review of employee survey results; review results on culture conducted by the internal audit function ("IAD"); review of remuneration structure and performance evaluation and discussions on the regulatory and industry updates.

**Figure 2 Culture-related matters that were brought to discussions at the board or board-level committees of the banks**



16 There is also consideration being given to how culture can be incorporated in internal audits of banks to assist the board-level committees to review the effectiveness of the overall culture enhancement initiatives pursued by the banks. As illustrated in the chart below, IADs of some banks are now responsible for conducting regular reviews of the effectiveness of the bank's culture efforts. However, some banks expressed the challenge of the potential lack of behavioural assessment skills when auditing culture of the bank.

**Figure 3 Degree of involvement of IAD in culture initiatives among banks**

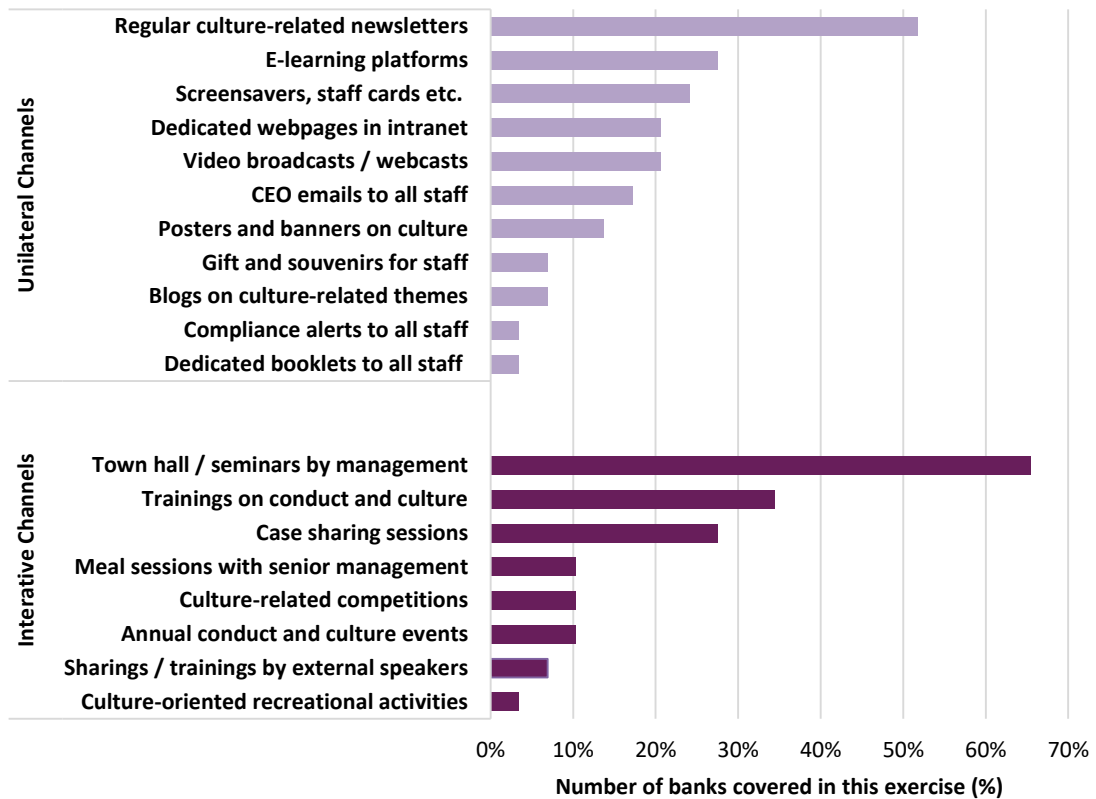


17 On the other hand, banks have increasingly engaged external providers to assist the board or board-level committees with developing overall culture framework including dashboards, to conduct review on the bank’s culture, remuneration structures or performance assessment, or to carry out employee surveys or customer satisfaction surveys. The most common external support that banks have sought from external providers is to solicit staff feedback, through means such as employee surveys and focus groups.

## **2.3 Banks need to cascade “tone from the top” down to ensure desired culture through effective and continual communications and training**

- 18 While the bank’s leadership plays a significant role in changing culture by setting the appropriate “tone from the top” and lead by example, board-level oversight alone would be insufficient if banks want all their staff to understand and live up to the desired culture. Therefore, it is equally important that banks’ leadership cascade the “tone from the top” down to ensure that the bank’s desired culture, values and behavioural standards are understood and shared by different levels of staff, through effective and continual communications and training.
  
- 19 Overall, banks should ensure that a culture of competence and ethical behaviours is embedded within the bank by providing relevant and timely training to staff to maintain and enhance their competencies. Banks are also expected to facilitate the undertaking by relevant staff of the continuous professional development under the Enhanced Competency Framework or by other professional bodies to complement the effort of promoting sound culture.

**Figure 4 Common methods of communications from the top**



20 Many banks have embarked on their “tone-from-the-top” communications and expanded training programs on culture-related topics. As illustrated in the chart above, common methods of communications include conducting town hall meetings or seminars by senior management and/or leaders of individual business units, with topics on bank culture reform; delivering regular newsletters to staff to (1) share management’s views and direction; (2) remind staff on misconduct cases; and/or (3) refresh staff’s understanding on relevant policies and guidance; delivering training through classroom training or e-learning platform on culture-related topics for new hires and/or existing staff (“refresher” training); and conducting case sharing sessions for staff, covering topics such as dealing with “grey areas”.

## 2.4 Banks need to develop an easily understood language around culture

21 Regardless of the communication methods, banks should communicate culture expectations in a language that can be easily understood by their staff, so that their staff can identify themselves as part of the team with the common goal of shaping sound bank culture. For example, providing guidance for staff dealing with “grey areas” can be an effective means of communicating culture and behaviours expectations while in some cases, the use of non-traditional communication method can also be an effective means of raising staff awareness.

**Box 1 – How banks communicate desired culture, values and expected behavioural standards to staff**

**Use of guidance questions and case examples for staff dealing with “grey area” situations**

A bank includes a set of questions that a staff should consider when faced with morally ambiguous situations. The questions are divided into several subsets, such as “policy” and “principles”. For example, in the “principles” subset, under the main question of “Does this decision sit well with our sense of right and wrong?”, there are several questions, such as “What would your friends, family or colleagues say?” and “How would you feel if it was reported in the media?”.

Furthermore, the questions are complemented by email circulars that shared real-life examples of how staff upheld the bank’s values by bearing in mind the considerations outlined in the guideline questions when making decisions in specific situations.

One of the shared real-life examples involved staff members turning down potential revenue opportunities that would arise from a client’s request because they stood firm by their assessment that further buying of an investment product, even though the original purpose of buying the product was “hedging”, would potentially be in excess of the client’s genuine needs and expose the client to substantial risks.

### **Use of creative videos**

Another bank produced a series of videos covering conduct-related themes that creatively intermingled Fung Shui elements after learning that staff would be more effectively engaged if the messages were communicated through videos. The videos, which were broadcasted to all staff in the bank, had a different conduct-related focus every month, and featured a local Fung Shui master or celebrity together with a member of the bank's senior management team. The bank received largely positive feedback among staff under this non-traditional communication method. For the avoidance of doubt, we are not making direct inference that sound bank culture must be related to Fung Shui. Instead, the lesson that can be drawn is that banks should aim to communicate culture expectations in a language that can be easily understood by their staff, so that their staff can identify themselves as part of the team with the common goal of shaping sound bank culture.

## **2.5 Banks need to ensure their desired culture and expected behavioural standards are relevant to different level of staff**

- 22 While most banks covered in this exercise have attempted to design summary sheets, many of them are more of a “summary” of code of conducts on a “bank-wide” basis, we observed that only a few banks covered in this exercise have developed summary sheets that are relevant to the day-to-day responsibilities of their staff and specific to individual business functions. To assist this process, some of these banks have developed templates, together with some real-life examples, to facilitate individual business functions to develop their summary sheets.

**Box 2 – How banks use summary sheets to set out the culture, values and behavioural standards expected of staff in carrying out their day-to-day responsibilities**

A bank has tailored-made the summary sheets of the bank’s culture, values and behavioural standards for various business functions. For example, the summary sheet designed for their retail banking business cited, among others, that “encouraging customers to replace an existing product at the bank or third party products in order to earn new commissions” breaches the bank’s key business standards and code of conduct. In other words, the summary sheet is designed in such a way that makes culture issues resonate with the day-to-day work at the retail banking function.

## **2.6 Banks need to have clear ownership of risk and culture reform**

- 23 Many banks, spanning from locally incorporated banks to overseas incorporated banks covered in this exercise, have appointed senior staff members as “conduct risk champions” which are responsible for cascading messages relating to culture and conduct further down the institutions. It is common to see that the conduct risk champions appointed span across various divisions, and in some cases, are the division heads while a few banks appointed a single senior management staff as conduct risk champion, for example, Chief Risk Officer.
- 24 However, the self-assessments for some banks covered in this exercise contained relatively fewer details on the responsibilities of these conduct risk champions on the ground, and what roles these champions have taken in the culture enhancements. Some other banks have not indicated that they have appointed any conduct risk champions at all.

### **Box 3 – How banks appoint conduct risk champions to take responsibility for cascading messages down the institution**

A bank, nominated the members of their senior management team as the Risk Champions, and they are responsible for driving various culture initiatives with clear deliverables and target delivery dates. Actions and initiatives driven by these Risk Champions are presented to the relevant committee for comments.

Another bank has formulated a “Culture Plan” which sets out the key culture initiatives that help foster a sound culture with target audiences, accountable owners and completion dates, and the broad themes in the Culture Plan also link with the three pillars. For example, under the initiative “tone from the top / lead by example”, the CEO and heads of business function are tasked with the responsibility to embed messages relating to conduct and culture via different means such as “Messages from CEO” and “Town-halls” to enhance the staff’s culture understanding.

## Chapter 3 Range of Practices – Incentive Systems

25 The ethical values and behaviour must be underpinned by appropriate incentive system that induces the desired behaviours at all levels. On the pillar of “incentive systems”, we are not just referring to remuneration. It is a much wider concept, as it also includes staff recruitment, performance assessment and promotion systems together with consistent application of rewards and consequences.

### **3.1 Banks need to focus on recruiting individuals who align with the bank’s desired culture, values and behavioural standards**

26 While there is relatively less coverage in the self-assessments on how banks incorporate culture elements in their recruitment processes or assessment of cultural fit, many banks covered in this exercise indicated that their recruitment practices assess the candidate’s alignment with the bank’s desired culture, values and behaviours and culture-related elements such as the candidate’s conduct credentials, ethics, honesty and integrity.

27 Some banks covered in this exercise have cultural fit assessments or assessments on integrity, honesty or values, while some banks include conduct behavioural questions during the interview process and other forms of assessment on aspects such as ethics and customer focus. A small number of banks also indicated that they have provided training to staff on interview skills in relation to the culture components.

#### **Box 4 – How banks recruit for cultural fits**

##### **Use of cultural fit assessment**

A bank, as part of their recruitment process, seeks to determine whether the potential staff demonstrate behaviours which align with the bank's desired values as part of their recruitment process and used an assessment tool developed by an independent expert firm that specialises in cultural fit assessment.

##### **Incorporation of behaviour-related components in interview process**

A bank has incorporated behaviour-related components such as "Customer Focus" and "Professional Ethics" in their interview process to better assess whether the potential candidate has the desired ethical values and behaviours.

### **3.2 Banks need to ensure that remuneration frameworks are designed and implemented to promote sound culture and prevent incidents of misconduct**

- 28 Remuneration is well-recognised as an important driver of behaviour that can affect customer outcomes. Banks should ensure that their remuneration practices are designed to encourage the desired behaviours and focus on not only what the staff do, but also how they do it. We observed there is a greater use of a balanced scorecard approach by banks that would consider "what" (financial factors) and "how" (non-financial factors) when determining variable remuneration for staff. Nevertheless, we observed that self-assessments generally contained fewer details on the design and implementation of the banks' remuneration frameworks, including lack of coverage of the linkages between the performance assessment results and the remuneration of staff.

29 Where banks have provided the weighting of non-financial factors (including behaviour factors) in the design of remuneration, we noted that some banks placed more focus on the ability of their staff to meet financial targets by assigning higher weighting on the financial key performance indicators. Banks should ensure that remuneration frameworks do not overly rely on financial targets in performance measurement, and that non-financial factors (such as staff adherence to the bank's desired culture, values and behaviours, including treatment of customers as well as compliance with policies and procedures) should have real impact on remuneration decisions.

### **3.3 Banks need to make regular reviews including the effectiveness of their remuneration structures and practices**

30 While some banks have indicated in the self-assessments that they have conducted regular reviews of their remuneration frameworks, the self-assessments generally have limited coverage on the adequacy and thoroughness of their reviews including the ongoing effectiveness of their remuneration frameworks. Similar observations exist at frontline staff level, only a small number of banks have taken the initiative to review their remuneration frameworks and practices of front-line staff but such reviews have not covered the effectiveness of the front line remuneration framework as a whole. It is important that banks should make regular reviews of their remuneration framework including assessments of the effectiveness of their remuneration structures and practices to promote sound culture and prevent incidents of misconduct.

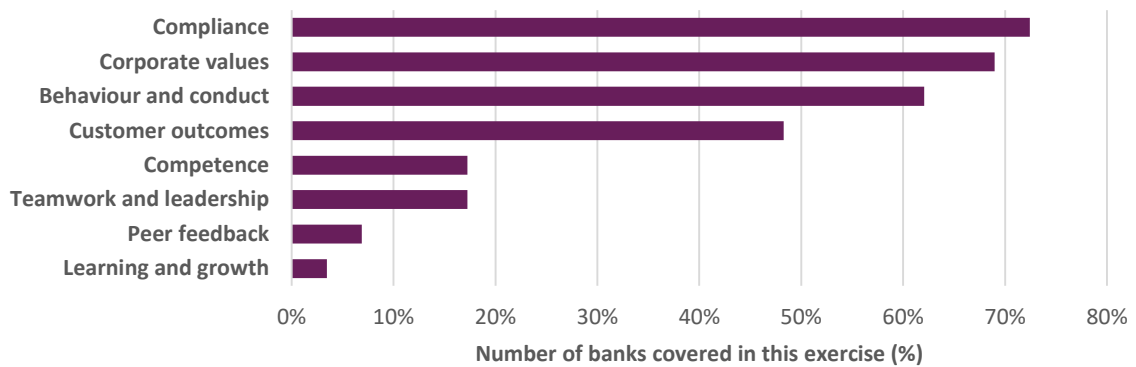
### **Box 5 – How banks review their front line remuneration**

A bank has reviewed their remuneration policies, including the incentive schemes, for their frontline staff. Rather than just solely relying on the key performance indicators, the bank also considers the staff's "conduct-related performance" in their performance assessment, which includes consideration of the staff's alignment with the bank's desired core values. Furthermore, if the staff fails to attain a rating of "acceptable" or above under the "conduct-related performance" component, he/she will not be eligible to receive variable pay for that period, regardless of his/her financial performance. Other than that, the bank has also implemented the use of compensation tools (such as clawback or malus arrangement) to facilitate reduction to staff remuneration for misconduct, where there have been breaches of legal and regulatory requirements.

## **3.4 There should be structured framework to assess staff performance against behavioural indicators**

- 31 All banks covered in this exercise have incorporated certain non-financial indicators (including behavioural indicators) as part of the performance assessment of their staff, apart from their financial performance. As illustrated in the chart below, most banks covered in this exercise have incorporated non-financial indicators which focus on compliance with the bank's policies and procedures, adherence to corporate values, conduct-related behavioural indicators (such as customer satisfaction or focus on "total customer relationship") and customer outcomes. Some banks considered staff competencies and team work while a few banks considered peer feedback on culture as part of the performance assessment.

**Figure 5 How banks use non-financial indicators to assess staff performance**



32 Although most banks covered in this exercise indicated that they have considered both financial and non-financial factors (including behavioural indicators) in the performance assessment, self-assessments generally have limited coverage on how banks consider the behavioural indicators and whether there has been adequate consideration of such indicators in the performance assessment. Banks should establish structured framework to assess staff performance against non-financial factors (including behavioural indicators) as it is important for supervisors to have insights to assess their staff’s conduct and behaviours.

**Box 6 – How banks use structured framework to assess staff performance**

A bank has included the relevant staff data in their staff performance dashboard which is available to managers responsible for preparing annual written evaluations. The results of the review must be (1) documented in the bank’s performance evaluation tool; (2) communicated to the staff; and (3) taken into account when making year-end promotion and remuneration decisions.

Another bank has in place year-end accountability standards to ensure managers consider a staff’s overall performance utilising all available information which includes all disciplinary and non-disciplinary warnings for the full year, and such review would be conducted across the bank to determine the impact on the staff’s performance assessment and incentive. Line managers are also required to affirm that risk management, compliance and conduct-related behaviour (e.g. focus on “total customer relationship”) have been taken into account in the performance assessments of individual staff.

### **3.5 Banks need to strengthen linkage between remuneration outcomes and staff performance on adherence to corporate values regardless of financial performance**

33 While majority of banks covered in this exercise indicated that they have incorporated a separate performance rating for adherence to corporate values (which is separate from “regulatory and compliance” objectives), self-assessments in general contained relatively fewer details on how banks weigh such indicator in the performance assessments and whether there would be any implications for the determination of variable remuneration of staff who receive a poor rating regardless of their financial performance. Only a few banks have illustrated the linkage between the performance rating for adherence to corporate values and the determination of variable remuneration of staff. It is important to have such linkage so that banks can send a strong message to their staff on the importance of adherence to corporate values vis-à-vis financial performance.

**Box 7 – Linkage between performance rating and variable remuneration**

A bank has a policy in place that for staff with a poor rating on adherence to corporate values, their variable remuneration would be reduced by a certain percentage as an alert for the staff. On the other hand, the bank also rewarded staff with good rating on this indicator where their variable remuneration would be increased by a certain percentage as an extra reward for the staff to promote the bank’s desired culture and value.

### **3.6 Banks need to ensure their consequence management frameworks promote culture of accountability**

- 34 To promote culture of accountability, there should be clear and appropriate consequences established, articulated and applied for individuals engaging in any undesired behaviours. Most banks covered in this exercise have consequence management mechanisms in place that set out the consequences of undesired behaviour, but the self-assessments in general contained fewer details on whether the consequences are clearly articulated and consistently applied at different levels of staffs.
- 35 Most banks covered in this exercise have mechanisms in place which set out the consequences for individuals engaging in any undesired behaviours. Disciplinary outcomes range from reminder, counselling, verbal and written warnings to dismissal, subject to the nature and severity of the undesired behaviours. Many of these banks also indicated the use of additional remuneration adjustment tools such as clawback, malus and forfeiture of variable remuneration for more severe cases.
- 36 Some banks have in place more comprehensive consequence management framework that determines the level of severity of undesired behaviours and the corresponding recommended outcome. This is particularly important for banks to ensure that the consequences are appropriately and consistently applied at different levels of staff within the bank.

### **Box 8 – More comprehensive consequence management frameworks**

A bank has in place a “red flag” mechanism, which is a core part of the bank’s consequence management framework. The bank has set out the various types of breaches such as “data confidentiality”, “internal fraud”, “overdue mandatory training” and “inappropriate communications”, and their corresponding “red flag score”. When a Red Flag criterion is breached, the staff receives a Red Flag with specific risk-weighted score. For staff with a Red Flag score of a certain level or more, their performance assessment, promotion, compensation will be impacted. The bank has taken a step further in having on-going reviews and enhancements to the scoring, and taking regular analysis based on the trends and types of the red-flag scores in the bank as a whole.

Another bank has established consequence management process to handle staff conduct breaches where the bank would first determine the severity level of breaches and then the assessed misconduct level taking into account the contextual factors including any mitigating (e.g. breach was unintentional) or aggravating factors (e.g. individual is a management staff). The assessed misconduct level would inform the corresponding disciplinary outcomes, including performance and reward related outcomes. For example, for an assessed misconduct level of “high”, in addition to the recommended disciplinary action of a written warning letter, a minimum percentage of downward adjustments can be applied by the bank to the staff’s current year variable pay.

- 37 It is also important for banks to consider the consequences for poor management oversight as part of the bank’s consequence management framework to promote a culture of accountability. We noted that a few banks covered in this exercise have formal mechanisms in place to consider the accountability of supervisors for the undesired behaviours of their staff.

### **Box 9 – Consideration of accountability of supervisors as part of consequence management**

A bank has set out in their disciplinary policy that the immediate supervisor of the staff who is subject to disciplinary action will also be reprimanded if there is no evidence that the immediate supervisor has made the best effort and fully discharged his/her responsibilities to prevent the occurrence of the incident.

Another bank has specified in their disciplinary policy that the supervisor of a unit in which many staff have compromised customer or company data will be liable for disciplinary actions, and has listed examples of such scenarios in the policy. For example, the supervisor will be penalised if many of his/her staff use personal email for business purpose, send sensitive data to follow up from home or send data for back up purpose.

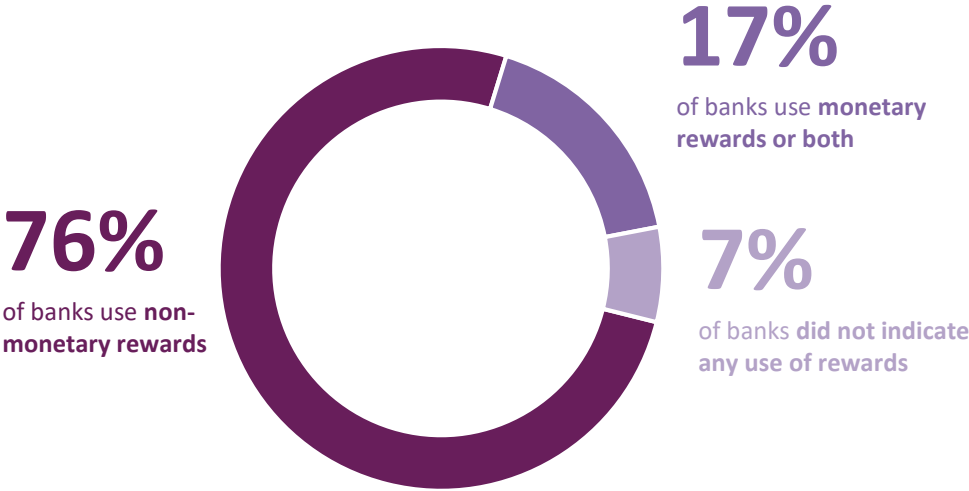
Furthermore, another bank has taken into account the supervisor's accountability in the clawback mechanism of variable remuneration. In addition to poor individual behaviour and performance, a supervisor who displays poor management and has thus led to negative impacts on the department or the entire bank would have his/her variable remuneration reduced or cancelled.

## **3.7 Banks need to promote positive behaviours through proper incentive systems**

- 38 The incentive systems of a bank should not only focus on the use of disincentives to discourage undesired behaviours, but should also take into account that positive recognition of desired behaviours can be equally effective in driving behavioural changes among bank staff. We observed that most banks covered in this exercise have implemented employee recognition schemes in promoting positive behaviours, such as through both monetary and non-monetary rewards for staff who demonstrate exemplary behaviours.

39 As illustrated in the chart below, most banks covered in this exercise used non-monetary rewards in their employee recognition schemes to promote positive behaviours. Such rewards range from a simple thank-you card, recognition emails, certificate, achievement award, praise from senior management, breakfast with CEO to staff appreciation events. A few banks gave out prizes range from small gifts to vacation packages for their staff. While some of these prizes may correlate to monetary rewards, this type of rewards is a one-time recognition with a special value which is not the same as adjustments in variable remuneration.

**Figure 6 Use of rewards to promote positive behaviours**



40 While only a few banks covered in this exercise promote positive behaviours through monetary rewards, the more common type of monetary rewards is to provide positive adjustments to staff remuneration. We noted that some banks have interesting peer-to-peer recognition schemes to promote positive behaviour through the use of monetary rewards in which their staff can nominate, be nominated, recognise and reward each other.

## **Box 10 – Use of monetary rewards to promote positive behaviours**

### **Peer-to-peer recognition scheme using a point-based system**

A bank promotes positive behaviours through their employee recognition scheme which is a dedicated online platform where staff can provide peer recognition by giving out points to other colleagues based on their actions, with different types of choices for recognition under a set of criteria of positive behaviour, such as “Do the right thing” and “Speak Up”, and monetary rewards will be given to staff that have accumulated a certain number of recognition points.

The bank also proactively shared the examples of these behaviours with their staff. A real-life example (classified as “Treating Customers Fairly”) is that a staff noted that an operational error caused a delay in processing a customer’s proceeds which resulted in the customer’s interest income loss. While the customer naturally demanded a refund, the staff verified and discovered that the customer was actually entitled more than requested. The staff has taken the initiative to refund an accurate amount and such fair treatment was well appreciated by the customer.

### **Peer-to-peer recognition scheme using a real-time platform**

Another bank introduced an employee reward program to reward their staff who demonstrated positive behaviour. The bank provides a real-time platform for staff to recognise other colleagues who are living up to leadership standards, and track and manage recognition activities using dashboards. There are different levels of rewards, based on contributions, which can be converted to monetary rewards.

An example provided by the bank is that individual teams including frontline and the Anti-Money Laundering Team were rewarded for assisting in the opening of an account for a customer from a financial inclusion perspective. Another example is for a frontline staff who has properly escalated to his supervisor a case of being offered a reward from a prospective customer to open an account.

- 41 Regardless of which type of rewards banks use to promote positive behaviours, banks should also focus on sharing the positive behaviours that were demonstrated in each case with their staff to ensure effective positive reinforcement. Some banks covered in this exercise have shared the positive behaviours through internal channels, such as intranets, internal emails or newsletters, town hall meetings, or posters in prominent areas.

## Chapter 4 Range of Practices – Assessment and Feedback mechanisms

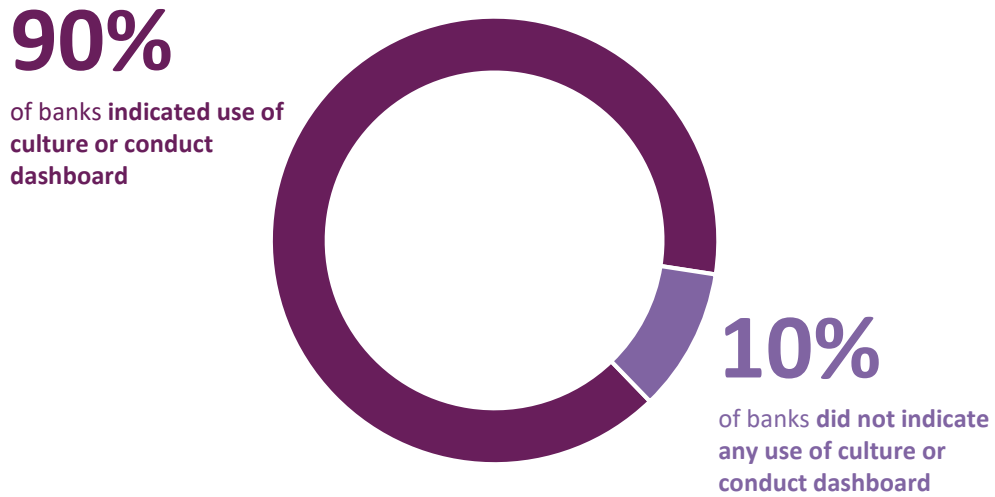
42 An effective feedback loop on actual outcomes should be put in place by banks to inform the culture journey. On the third pillar of “assessment and feedback mechanisms”, we are looking for “echo from the bottom” besides “tone from the top”. We ask banks to put in place an effective feedback loop to solicit response from their staff and customers, as well as an effective escalation policy (including “whistle-blowing” mechanism) to allow staff to timely report any illegal, unethical or questionable practices in a confidential setting so that there is no fear of reprisals.

### 4.1 Banks need to assess culture including the effectiveness of their culture efforts

43 While banks covered in this exercise have implemented a series of culture initiatives, it is important to assess whether these initiatives are effective in driving behavioural changes among bank staff. The board and senior management of banks need to receive meaningful culture insights to inform them whether their “tone from the top” is reflected in a consistent “echo from the bottom”, and how close are the banks to achieving the desired culture. To facilitate oversight by the board and senior management, monitoring culture would involve regular analysis and interpretation of granular data and information gathered from a range of sources.

44 As illustrated in the chart below, many banks covered in the exercise have set up a dashboard of indicators to assess culture or conduct of the bank.

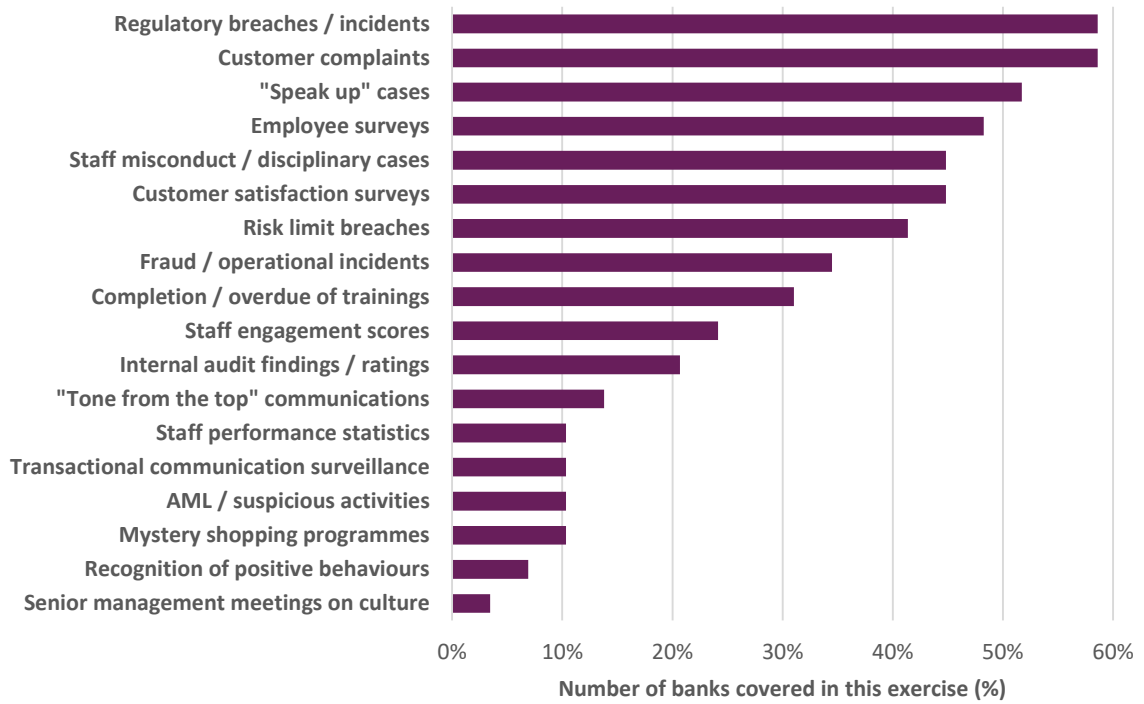
**Figure 7 Use of dashboard of indicators to assess culture or conduct**



45 However, we observed that dashboards of the banks primarily leverage existing data from the banks’ management information and most banks are still in the early stages of determining what the appropriate indicators are and how to use the dashboards to inform their culture journey.

46 We recognise that there is no uniform set of indicators when it comes to assessing culture. As illustrated in the chart below, the range of indicators that are adopted by banks in their dashboards is wide. The most common types of dashboard indicators which we have seen include number or type of customer complaints, regulatory breaches or incidents, “speak up” cases and staff feedback.

**Figure 8 Common types of indicators adopted by banks covered in this exercise in their dashboard**



47 There are also other tools which can be useful for banks in collecting data to assess culture. Most banks covered in this exercise have conducted employee surveys which may be carried out by internal resources or external service providers.

48 We have seen different employee survey approaches that are used among banks covered in this exercise. There is a greater use of culture specific surveys while some banks have drawn qualitative data from staff engagement surveys to provide culture insights. While employee surveys are usually supplemented with focus groups and interviews which are designed to explore identified issues in greater detail and depth, only a few banks covered in this exercise have used these tools as a means of assessing culture.

- 49 The key is that banks need to be able to assess behaviour through a set of indicators that are meaningful to the value and desired culture of the banks, so that useful and actionable insights can be provided to the board and senior management of the banks to consider whether any culture enhancements are necessary. The more sophisticated approach is not to look at individual indicators in isolation, but to allow for the multiple data sources to be triangulated.

#### **Box 11 – A more sophisticated dashboard**

A bank has demonstrated a higher level of maturity in assessing and understanding culture by developing a dashboard which has incorporated multiple data sources. The bank’s culture dashboard seeks to measure culture through several lenses including the feedback from their employee survey in which the staff would rate perceptions of themselves as well as their colleagues, and together with other quantitative data (e.g. complaints, whistleblowing cases, staff conduct cases, etc.) which allows for the multiple data sources to be triangulated. Based on the results under these indicators within the culture dashboard, the bank was able to identify the areas where enhancements are necessary and come up with recommended actions. The dashboard itself is also reviewed and revised from time to time to enhance its readability and reliability.

## **4.2 Banks need to foster “speak up” culture that encourage staff to speak up without fear of adverse consequences**

- 50 While all banks covered in this exercise have certain “speak up” mechanisms in place, the efforts banks made in fostering a “speak up” culture that encourages their staff to speak up or escalate issues varies. It is important to provide staff with multiple channels to turn to when they choose to speak up. We noted many banks have offered multiple channels for their staff to speak up.

- 51 As there are different factors which may create a fear of speaking up, some banks have considered the potential of an independent advice channel and engaged external parties in managing the whistle-blowing reporting from staff which allows their staff to speak up safely without fear of adverse consequences.
- 52 While banks should ensure effective operation of the different internal and external channels or hotlines, there is also a need for banks to ensure that their “speak up” mechanisms including the benefits of speaking up are well understood by their staff.

**Box 12 – Facilitating the use of “speak up” mechanism with examples**

A bank operates a 24/7 hotline with live operators who can connect to translators in multiple languages, so that their staff can raise concerns promptly.

Another bank, in their whistleblowing policy, has provided to their staff a list of possible types of concerns that can be raised (e.g. possible fraud, misuse of confidential client information, staff misconduct, etc.).

The bank has also developed quizzes with case studies for staff to better understand their whistleblowing policy e.g. Colleague A is concerned about the behaviour of Colleague B, respondents have to choose in the following scenarios that give rise to treatment under the bank’s Whistleblowing Policy: (1) Colleague B discusses on his personal mobile phones with individuals outside the firm about clients of the firm; (2) Colleague B is regularly failing to set up meetings when asked; and (3) Colleague B is loud on the phone. The correct answer is (1) as Colleague B may be misusing confidential client information.

Where a reported concern helps the bank to identify failings, the bank would deliver positive stories to their staff through their “speak up” campaign, illustrating the benefits of speaking up.

53 A small number of banks covered in the exercise have make it an obligation for their staff to speak up by stating in their “speak up” policies that it is a responsibility of their staff to speak up. Specifically, if a staff is aware of any misconduct or misbehaviours but does not speak up, the staff may be subject to disciplinary actions by the banks. Another bank has taken a different approach by encouraging their staff to speak up through the use of monetary or non-monetary awards.

**Box 13 – Encourage “speak up” through the use of awards for proven cases**

We noted an interesting policy at a bank which grant awards to encourage staff for speaking up with known identity, after the cases are investigated and proven. The policy is in place with a view to, among others, supporting staff to proactively report misbehaviours. The awards are in the form of recognition and/or monetary awards.

Recognition may include but not limited to letters of appreciation and/or give positive consideration during performance appraisal and career advancement. For monetary award, if the risk amount (i.e. the reduction in potential losses by the bank) can be determined, a certain percentage of this risk amount will be awarded to the staff concerned with a maximum cap.

54 Finding ways to encourage “speak up” is not enough, and effective “speak up” mechanisms must put a great focus on protecting those staff who choose to speak up as they may face bullying or even retaliation. Some banks covered in this exercise have incorporated measures in their “speak up” mechanisms that seek to protect their staff who choose to speak up.

## **Box 14 – Fostering protection for staff who choose to speak up**

### **Prohibition of retaliation**

A bank is explicit in their whistleblowing policy with regard to the prohibition of retaliation (in any form, including among others, demotion, dismissal/discharge, suspension or harassment) against any other staff who has raised concerns through whistleblowing channel. Staff who believes they have been subject to retaliation can report a possible violation to the Human Resources or Employee Relations representative. The policy is also explicit in stating that individuals who engage in retaliation towards a staff may be subject to disciplinary action up to and including termination of employment.

### **Option to report anonymously**

Another bank has also clearly stated that their staff engaging in retaliation can be subject to disciplinary action up to termination of employment or other relationships with the bank. Also, the bank offers option for their staff to report to the responsible office anonymously if the staff feels more secure raising concerns anonymously and understands the possible difficulties of following up on anonymous reports.

- 55 Effective “speak up” mechanisms should also recognise the importance of responsiveness. For example, a bank has set out in their whistle-blowing policy that, for whistle-blowers who provided identity, the department who is responsible for handling the whistle-blowing case need to provide the whistle-blower a preliminary timeline for investigation, and should offer the investigation results once the case is completed. If the whistle-blower is dissatisfied with the investigation results, he/she may provide supplementary information, which the responsible department will follow up further.

### **Box 15 – A more comprehensive “speak up” mechanism**

A bank has a whistleblowing policy that has various complementary features to enhance the utilisation and effectiveness of whistleblowing mechanisms within the firm. First, the bank offers both internal and external whistleblowing channels. Internally, staff can contact four designated whistle-blower protection officers directly or via email. The bank also has an external reporting service operated by an external consultancy, which can be reached by email, post or phone. Second, the bank has trained their staff members and tasked them as advocates to guide them to use the right channels to raise concerns. Third, the bank also has a mechanism in place to ensure the senior management’s knowledge of whistleblowing cases. Specific cases are reported on an ad-hoc basis and reports are circulated to the senior management every month. Furthermore, the bank reviews its whistleblowing policy annually, and the revised version is made available to all staff through the bank’s intranet.

## Chapter 5 Common themes

- 56 Based on the self-assessments, the banks covered in the exercise have made significant progress in promoting sound bank culture over the past two years. Nonetheless, we have identified from the self-assessments the following common themes across the banks. Banks are encouraged to pay more attention to these common themes as they continue their culture journey.
- 57 For the avoidance of doubt, while the exercise has covered 30 licensed banks and that RLBs and DTCs are often simpler in their business models and operations, RLBs and DTCs are also encouraged to make reference to these common themes as they continue their culture journey.

### **5.1 Further work is needed to ensure incentive systems are designed to promote sound culture and prevent incidents of misconduct**

- 58 Incentive systems play a crucial role in driving sound behaviours and affecting customer outcomes. It is therefore important that incentive systems are designed and implemented by banks to promote sound culture and prevent incidents of misconduct. While we are observing an increasing trend away from reward being based solely on financial factors to a greater use of balanced scorecards, there remains questions on whether there is an appropriate balance of “what” (financial factors) and “how” (non-financial factors) or there is still a stronger focus on the “what”; whether there are the right non-financial factors (including behaviour factors) embedded with a greater focus on customer outcomes; whether there is consistent application of consequences regardless of staff financial performance. It is also important for banks to incorporate assessment of culture and ethical fits of potential staff in their external recruitment decisions.

59 However, in most of the self-assessments conducted by banks covered in this exercise, coverage of incentive systems (including staff recruitment, performance management, remuneration structures and practices) is, in general, relatively limited, as compared to the coverage of initiatives related to the other two pillars. As such, banks' culture efforts in the area of incentive systems remain a "work-in-progress" and further work is needed to ensure appropriate incentive systems across the entire bank at all levels to induce proper behaviour and promote accountability, which helps align the interest between banks and their customers.

60 We expect to see more initiatives with greater level of details in respect of incentive systems which are designed to promote sound culture and prevent incidents of misconduct. In particular, banks need to:

- focus on hiring individuals who align with the bank's desired culture, values and behavioural standards;
- ensure that the design and implementation of their remuneration structures and practices focus on not only what staff do, but also how they do it;
- ensure that performance assessment have adequate consideration of behavioural indicators, and that there is a structured framework to assess staff performance against behavioural indicators;
- strengthen linkage between remuneration outcomes and staff performance on adherence to corporate values regardless of their financial performance;
- ensure there is clear consequence management frameworks in place to promote culture of accountability; and
- make regular reviews including the effectiveness of the remuneration structures and practices.

## **5.2 Stronger links are required to connect their Hong Kong operations with the culture efforts of their headquarters or upstream entities as well as their downstream operations, as appropriate**

- 61 We observed that the culture enhancements are often driven by the headquarters of banks which are part of the larger banking group incorporated outside Hong Kong. However, the links of these banks to the culture efforts of their headquarters (including the global headquarters or regional headquarters, if applicable) or upstream entities vary, with some of these links being weak. There is, in general, limited coverage in the self-assessments on how the formulation of the global culture initiatives have taken into account feedback from regional operations and different contexts across geographies including that of Hong Kong; how adjustments have been or will be made by these banks when implementing their global culture initiatives here in Hong Kong with regard to local circumstances, especially how to ensure the buy-in of local staff for the culture promoted at the regional or global level; and how any implementation issues would be escalated to the headquarters for consideration and resolution. It is also unclear how the headquarters are providing support to their operations in Hong Kong in implementing culture enhancement initiatives.
- 62 Similarly, the links to downstream overseas operations from the regional headquarters here in Hong Kong seem generally weak or non-existent. This phenomenon is not only happening in small satellite operations in faraway places, but is also happening in larger operations which make substantial contributions of the firm's business covered by Hong Kong. For example, a bank acknowledged that ensuring an on-going and effective implementation of their cultural initiatives across all geographies and at all levels of the organisation is a key challenge. However, the bank has not provided any concrete plan to address such a challenge. We expect banks to cascade down their desired culture to their downstream operations outside Hong Kong, taking into account the local circumstances. This is particularly important for larger banks that span numerous geographies and business lines, and can have a large number of different sub-cultures developed over time.

### 5.3 Deeper analysis is expected to benchmark themselves against the findings from the reviews of the major overseas misconduct incidents

- 63 Another common theme is the inadequate effort that banks have put in to benchmark themselves against the findings of the review of the major misconduct incidents outside Hong Kong. As set out in the 2018 Circular, recent examples include the *Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry* in Australia and the *Prudential Inquiry into the Commonwealth Bank of Australia* by the Australian Prudential Regulation Authority. We see from the self-assessments that while banks had somehow made reference to the findings of these major misconduct incidents outside Hong Kong, most banks covered in this exercise did not go beyond simple sharing of the factual happenings of those overseas misconduct cases with their staff while a few banks did not recognise the need to benchmark themselves against the review of these major overseas misconduct incidents.
- 64 Other than this, some banks have conducted reviews but focused more on the direct application of the recommendations in the overseas cases to their own situation. We would expect banks to understand the underlying root causes of the misconduct incidents and try to identify whether similar incidents could actually arise in their own institutions, even if they were not operating in exactly the same way, selling exactly the same product or offering exactly the same service as those misconduct incidents, and taking appropriate actions within their own institutions to prevent similar issues that they may face.
- 65 It is important for banks to keep an eye on any major conduct incidents outside Hong Kong and consider the relevance of the findings in the context of Hong Kong as there are bound to be lessons that we can all learn. While we do not require all banks to monitor each and every misconduct incident in all jurisdictions, banks are encouraged to keep track of key international developments and put in efforts to draw lessons from major overseas misconduct incidents as far as possible. For the avoidance of doubt, we do not plan to carry out supervisory action if a bank has missed some overseas

misconduct incidents and has not benchmarked themselves against the findings of these incidents. We also aim to share with the industry the relevant overseas development including any overseas misconduct incidents that we would like to draw the attention of banks to from time to time through channels such as circulars and Regulator's Dialogue.

#### **5.4 More focus is needed to facilitate the undertaking by relevant staff of the continuous professional development under the Enhanced Competency Framework or by other professional bodies to complement the effort of promoting sound culture**

- 66 Many professional qualifications comprise an element of conduct and ethics, and hence encouraging and facilitating the staff to pursue professional qualifications would not only enhance the capacity and capability of staff in the technical sense, but can also complement the efforts of banks in driving higher ethical standards of staff and, as a result, promoting sound bank culture.
- 67 Nonetheless, it appears that none of the banks covered in this exercise had mentioned the use of continuous professional development as a tool in promoting sound bank culture. In this connection, banks are encouraged to set out goals and concrete targets in respect of the continuous professional development, including those under the Enhanced Competency Framework (or those offered by other professional bodies), with a view to supporting the strategy of promoting sound culture within the bank.

## 5.5 More effort is needed to tackle the key challenge of culture assessment to identify the gaps between current progress and desired culture

- 68 Assessing culture remains a key challenge for many banks. Many banks in the self-assessments acknowledged challenges in assessing culture or have indicated that developing tools to assess culture or determining appropriate indicators in their dashboards are key priorities in their culture reform agenda. We also observed that banks have further work ahead to identify the gaps between their current progress and the realisation of desired culture within the bank. While we note that banks face challenges in assessing culture, only by assessing the culture will banks be in a better position to understand the cultural drivers and the enhancements that need to be implemented to have an effective cultural change and assess how close they are to achieving the desired culture.
- 69 As there is no “one size fits all” approach to culture, we recognise that there is also no single way or no set of uniform indicators for banks when assessing culture. We observed that most banks covered in this exercise have incorporated “backward-looking indicators” (i.e. what had happened in the past) in their culture dashboards. However, it is equally if not more important to incorporate “forward-looking indicators” which would help banks to identify what may happen in future. A few banks also tended to rely solely on a single source of data, for example, results from employee survey, when assessing their culture. A more sophisticated approach would be combining both quantitative and qualitative data from multiple sources to allow for the different culture indicators to be triangulated.

## 5.6 More work is needed in promoting an environment which provides “psychological safety” to encourage staff to speak up without fear of adverse consequences

- 70 As there are different factors which may create a fear of speaking up, it is important for banks to foster an environment with “psychological safety” that encourages their staff to speak up without fear of adverse consequences. According to Professor Amy Edmondson of the Harvard Business School, the term “psychological safety” is defined as *“a shared belief held by members of a team that the team is safe for interpersonal risk-taking”* and *“a belief that one will not be punished or humiliated for speaking up with ideas, questions, concerns or mistakes”*. In other words, the purpose of psychological safety is to reduce fear so that people can feel safe to express themselves.
- 71 While most banks have certain “speak up” mechanisms in place, not many banks have identified the need to address the fear of speaking up. There is also, in general, limited coverage in the self-assessments on the effectiveness of the banks’ “speak up” mechanisms.
- 72 Effective “speak up” mechanisms must put a great focus on protecting those staff who choose to speak up. Nevertheless, we observed that only some banks covered in this exercise have incorporated measures into their “speak up” mechanisms to protect staff who choose to speak up against bullying or even retaliation. While most banks have in place formal “speak up” arrangements and escalation channels, this needs to be complemented by continuous communications to reinforce the message. Effective “speak up” mechanisms should also recognise the importance of responsiveness as staff will only feel safe to speak up if their voices will be heard.

## **5.7 Sustained effort is required in driving cultural changes and banks should be mindful of “culture fatigue”**

- 73 Banks should be mindful of “culture fatigue” as staff can experience “culture fatigue” over time if banks implement a large variety of culture initiatives in a “form over substance” approach that overwhelms their staff. As a bank noted, “culture fatigue” can subsequently undermine the efforts that banks have put into implementing the various initiatives that aim at promoting sound culture, and thus, perseverance and constant improvement are key to enabling the culture initiatives to effectively promote the desired culture.
- 74 Some banks covered in the exercise acknowledged the key challenge to ensure culture remains at the forefront of staff’s mindset at all times. For culture initiatives to be effective, banks need to ensure that culture is understood by the staff at all levels. As some banks pointed out, continuous reinforcement through effective communication and promotion at all levels is important to have a lasting impact. Hence, banks need to recognise that culture initiatives are not something that can be set aside once implemented. Instead, it is important for banks to sustain their current efforts, by embedding sound culture awareness at all levels over time as they go forward in their continuous journey of Bank Culture Reform.