Bank Investor Engagement Project

January 2022

BIEP

VIEWPOINTS

Assessing purpose and culture in banking

The Bank Investor Engagement Project (BIEP) was launched in 2021 by Tapestry Networks and the High Meadows Institute to address communication challenges between large banks and their investors. Its primary focus is to establish key priorities and identify gaps and good practices for effective communication and engagement between institutional investors and banks on environmental, social, and governance (ESG) issues. In the first BIEP discussion on June 9th, 2021, an investor suggested effectively addressing ESG issues in banking required first answering a fundamental question about purpose: *"What is a bank's role in society?"* continuing, *"Until CEOs globally answer that, there will always be something to be fixed from an ESG standpoint."*

Articulating and embedding a meaningful purpose into organizational culture remains a challenge for many large banks, particularly as they seek to incorporate environmental and social risks and objectives into their businesses. While firms talk about purpose and stakeholder governance, few have articulated to their investors' satisfaction how their stated purpose has changed their business or operations, how that purpose is translated into values and behaviors that define the culture, and how they are controlling and monitoring cultural effectiveness.

On December 3rd, BIEP participants—bank executives and directors, executives from institutional investors, and subject matter experts—met virtually to discuss how banks and their boards think about purpose at a time when various stakeholders are demanding that banks avoid value and reputation destroying misconduct and play a key role in addressing issues like climate change and diversity, equity, and inclusion. Participants explored how that purpose is embedded into a firm's culture and monitored on an on-going basis. Investors also provided perspectives on how they try to assess bank culture and how they would like banks to more effectively communicate about their approaches to purpose and culture. This *ViewPoints* synthesizes perspectives emerging from the session and discussions in preparation for the meeting on December 3rd. It is organized around the following sections:

- **Reexamining purpose in banking** *(pages 2-3)***.** A combination of refining business models, addressing past misconduct, and expanding stakeholder expectations are leading many large banks to restate their purpose and better link that purpose to strategy.
- **Embedding a sense of purpose into bank culture** *(pages 3-6)*. To embed purpose into bank operations, leaders are identifying ways to ensure the desired culture is aligned to

their stated purpose. Banks are focusing on ensuring accountability across the organization, aligning incentives, and more actively monitoring behavior to better understand and steer their cultures.

- **Assessing bank communications on purpose and culture** *(pages 6-9)***.** The record of bad behavior in banking has resulted in lost value for investors. They have an interest in understanding and assessing a bank's purpose and culture, but it is extraordinarily challenging as outsiders. Investors, therefore, would like to see banks more effectively demonstrate how they tie purpose to strategy and offer more quantitative and qualitative data points to ensure statements are tied to actions and cultures aligned with desired outcomes.

- **Conclusion and next steps** *(pages 9-10)***.** As we look ahead, we invite investors and banks to provide feedback on purpose and culture in banking and to inform the BIEP agenda on improving ESG communications. The BIEP next plans to focus on communication around banks' climate transition plans.

Reexamining purpose in banking

In the first meeting of the BIEP, several investors indicated that they were keen to understand how banks articulate their purpose and how strategy, governance, and culture flow from that. One stated, *"How does their purpose inform their strategy and how does that strategy create long term value?"* Another said, *"Purpose is the framing of time horizons, risk appetite, and culture that define and direct business strategy."* An investor suggested that a clearly articulated purpose can guide employee behaviors and *"help pick up the crumbs that fall through the cracks"* of traditional risk management.

Bank leaders recognize the importance of purpose. Some refer to it as their bank's "north star," guiding objectives and behaviors. As various stakeholders including regulators, investors, employees, and even customers look to banks to broaden their purpose beyond employee and shareholder gains, and avoid fines and losses driven by poor conduct, banks are being forced to reexamine if their stated purposes remain fit for the times. For many, this process raises fundamental questions. Some feel that they are being pushed in directions which may not be appropriate. According to one banker, *"the last thing we want is that we become the answer to the world's challenges."* Others believe they are being pulled in potentially competing directions: *"I don't think there are enough balanced discussions about this tension between E and S and it's already having an enormous impact on people we care deeply about in our communities,"* through climate policies that increase energy prices for example.

And yet, many banks have concluded that a change in purpose is appropriate to respond to a changing business environment. A banker explained, *"This is business. Climate is business.*

How do we bring ecological, as well as social and social justice, together with economics? That's the point." Another described how ESG considerations are increasingly central to winning business: *"People are saying, 'Tell us your ESG rating,' and if it's not at X level, you can't even pitch for that mandate."* For some, the process started several years ago. A banker stated, *"A few years ago, our CEO took a view that we needed to refresh and recommit to a new framework. Under his leadership, we rearticulated a specific purpose for the bank."* For others, the change is more recent. A banker explained, *"Earlier this year we rearticulated our purpose. It is driven by four strategic pillars, focusing on our strengths, energizing for growth, digitizing at scale, and transitioning to net zero. That act in itself was significant."*

Embedding a sense of purpose into bank culture

As banks rearticulate their purposes, they are also working to ensure they embed that sense of purpose into the culture of their organizations so that it drives desired behavior and results. That is no easy task. A participant shared, *"One thing I find again and again is when companies ask themselves if they know the kind of culture they want and if they ask themselves, where are we today in terms of that aspiration, 100% of the time they self-evaluate as very far away. From the board on down, no company is close to the culture it says it wants."* Embedding purpose into culture requires consistent effort from the top of the house, from middle management, and regular communication to the front lines. A participant observed, "*After 20 years of corporate life, I concluded that projects to change culture don't work. The only thing that works is the flywheel that runs the company, the machine, and whether culture is embedded in that. Otherwise, it fades."*

Investors are aware that many banks do not have a strong track record of effectively embedding purpose into *"the flywheel"* of their organizations. Big banks are often perceived to be bastions of bad behavior, often driven by greed and evidenced by actions leading up to the global financial crisis and persistent conduct fines and significant losses since. An investor said, *"The one thing that seems to be missing is culture. That's one thing we're looking at more closely. All the problems relate to culture."* Another stated, *"We're really focused on culture and compliance. Those have the potential to sink a bank really quickly. Culture comes first. We're interested in what are employee incentives? Are the board and management overseeing culture? How are they overseeing culture? What reporting are they seeing?"*

Banks have invested significant time and resources in trying to root out bad behavior and realign their cultures. While the desired culture at each institution may vary, there are some common actions and attributes that management, boards, and investors can adopt to assess whether the desired culture reflects the stated purpose. Participants discussed the various steps banks are taking to demonstrate that purpose is embedded in culture and that management is being held accountable for instilling that culture across these organizations:

- **Establishing accountability at the top.** An investor said, *"Culture needs to be owned by the board as part of their fiduciary duty, linked to incentives and measurable ways to exemplify it."* Bank participants agree. A director stated, *"The board needs to be very dialed-in and focused on, 'Are we living our mission statement and our purpose?' And when there are tough calls that need to be made, do you in fact handle it? When there is bad behavior, what do you do with it? Whatever your purpose is, you have to show that you live it day in and day out. That can be really hard."*
- **Creating an effective oversight structure.** A participant observed, *"On one level, this is really simple: If you want to translate purpose into culture, the starting point has to be a commitment to spend the time, do the work, and think of it the right way from the board down."* Many banks are changing how they oversee culture both at the management and board levels. One bank established a management reputational risk committee that *"takes on review of any credit, any business relationship, any initiative that might rise to the level of a question of alignment with the bank's purpose, brand, reputation, etc."* and regularly engages with the board on such issues. Another noted, *"We changed our corporate responsibility committee to be the culture and responsibility committee. The change in name shows that it needs a lot of effort and that you can't let go of it. It needs constant monitoring, checking, and so on to move it forward."*
- **Aligning incentives and risk practices.** Implementing an effective governance regime across the firm is critical to control behavior. As one investor said, *"It comes down from the board and its risk appetite. What are the KPIs? That does tend to shape culture."* Banks and their boards are working to redefine acceptable behavior and ensure incentives include not just results, but also how those results are generated. A banker explained, *"I think in 2002 or 2003, we had our first code of conduct, it was maybe one page for the SEC. Today it's a totally different beast. Culture was looked at from a conduct perspective particularly in the financial crisis. Then we realized you can't just change a company by purely looking through a conduct lens…As we've gone on this journey for the last 10 years or so, it's become about really embedding purpose, making it part of performance management systems, and just about everything else."* A director agreed, *"There are many subtopics to this. Accountability, diversity and inclusion – we spend a lot of time there and harnessing it for innovation and growth, and integrity, holding ourselves to high standards. This frame of reference is important for thinking through all the elements of our strategy and execution. The board is very involved and it also shows up in how we monitor performance."*
- **Driving business decisions.** Making difficult decisions and aligning strategy to the stated purpose can demonstrate that purpose is embedded into culture. A director shared an example, noting, *"We exited coal six or seven years ago. It was a very difficult decision at the time because it had an impact on communities in which we are very present with our*

branch system. This was non-trivial. It was not an easy decision to make because of the impact." Climate is not the only area where this happening. New product opportunities also present banks with a chance to align purpose with culture. A banker described how a new market opportunity drove *"a vibrant conversation around how that fits into our risk appetite, but more importantly, into how we thought of the brand of the bank and ultimately we determined not to be part of that despite it being profitable for a competitor."*

- **Regularly monitoring behavior.** Banks commonly use employee surveys to gain insight into their cultures. A director explained, *"Every year we do a comprehensive survey of all of our colleagues. Every comment that comes in goes to the CEO and the board. I read every comment good, bad, and different. There are themes that come through."* Monitoring culture means looking not just for broad themes from these surveys but also looking for individual comments that could signal an underlying issue, even in one specific part of the business. A banker said, *"The employee surveys, when you read them, if you don't get any surprises, you don't have a good program. There should be in every survey something that catches you by surprise."*

Improving culture assessments

Assessing culture is a challenge for many institutions and their boards. One participant shared, *"I once met with the general counsel of a major bank 8 or 9 years ago and he made the comment, 'Look, we can't measure culture, monitor it, etc. That's not our job. We're not in the culture management business.' I got up and said I disagree."* Assessing culture is an evolving art, but some good practices are emerging. A banker said, *"This is something that's absolutely measurable and that every organization should be able to operationalize."* BIEP participants discussed how organizations can effectively assess their cultures.

- **Focus on a core set of culture indicators.** Every institution will have its own unique culture. Research suggests, however, that institutions with effective cultures tend to focus on some common traits. A participant observed, *"The things that are most meaningful and hard, but possible, to measure are things like trust, fear, justice, the ability to speak openly about concerns, whether values-based decisions survive business pressure, and whether there is a widespread grassroots belief that leaders model the behavior that they say they want from the rest of us. If you can work hard on those factors, you can move a lot."*
- **Supplement survey results with additional data.** While almost all large companies use some form of an employee survey, these are often insufficient to

Improving culture assessments

gauge culture on a standalone basis. Firms should also use things like exit interviews, focus groups and townhalls, employee disclosures and hotlines, and reviews on social media and websites like Glassdoor.

- **Identify ways to gain insight into "microcultures" and encourage employees to speak up.** Across large organizations, microcultures often exist within teams, business units, or geographies. Firms need to work to identify and assess those microcultures to determine if any corrective action is required. A participant explained, *"At any given time, one half of 1% of employees will notice something bad is going on. And the real question is, do they say anything?"* Delving into details of a properly structured survey for key cultural indicators and reviewing whistleblower hotline feedback can be key. Surveys and hotlines, however, are only effective in highlighting potentially dangerous microcultures if the *"one half of 1%"* feel it is safe to provide feedback. An investor observed, *"If firms are struggling because there's a micro piece to this inside the organization and employees themselves don't feel free enough to make that phone call, then there's a larger problem that needs to be addressed."*
- **Actively engage the board.** Boards have a clear role to play in overseeing culture. And yet, a participant lamented, *"In general, board oversight of ethics and compliance is terrible."* For many boards, assigning direct responsibility for culture is key. A director said, *"Responsibility for culture and conduct was dispersed across all the committees…So one thing we've done is asked management a few years back to get us an omnibus look from every theme, source, and division and put it all in one place so we can see if something is trending in internal audit, if it is actually impacting on something else, etc. And we embedded that in the governance committee…We think this is helping us."* Ultimately, the board needs to commit the time and effort as one participant stated, *"Culture is not a half hour discussion at the board level once a year. If culture is the sum total of human behavior in a complex organization, it's a profound question that takes a lot of work, and unfortunately, at most companies, it's not treated with the depth it needs."*

Assessing bank communications on purpose and culture

Gaining a meaningful understanding of how high-level purpose statements are driving behaviors and assessing a large bank's culture is challenging from the outside. Investors are looking for explicit links between purpose and strategy along with a useful set of data points and indicators that can provide a sense for culture over time. For some investors, the task is *"a very nuanced and complex assessment to make."* For others, it is *"admittedly the hardest part to what I try to evaluate as an outsider."* Virtually all investors agree that banks could improve the way they communicate about purpose and culture.

Investors seek clearer ties between purpose statements and actions

Some investors remain skeptical about banks' lofty, yet often generic purpose statements. An investor remarked, *"All these purpose statements, maybe they help a little, but they become meaningless. Sometimes they are the opposite of what people are actually doing."* Another commented, *"Banks don't need to redefine purpose. They need to expand on it and provide further disclosure to make it useful to investors."* Several investors expressed candidly that they don't spend time reviewing bank purpose statements at all.

To make purpose statements meaningful to investors, banks need to better articulate the relationship between purpose and strategy. In some industries this is relatively straight-forward. *"Utilities can be a good example for purpose,"* according to one investor, *"In the past, the purpose of a utility was very clear: provide energy in a safe and affordable way. The transition for them and the purpose they will serve going forward is also very clear. One thing we look for as investors is how does your purpose translate to strategy. For a utility, it's simple; for strategy, enter a capex plan and we can see it."*

Where banks are allocating capital is certainly a useful signal, but absent further narrative or direct communication, investors struggle with their assessment of how purpose is driving culture and behaviors. This is especially true for the larger banks that endeavor to serve multiple client segments across various businesses and continents. Some investors suggest smaller banks have a distinct advantage relative to larger banks. An investor commented, *"As a regional bank, your statement defines your goals and your business model more. From our conversations with management, regional banks are passionate about serving underserved populations. It comes through clearly with discussions with management and other people in the bank."* Another investor agreed stating, *"When you think about a bank in say Ohio, they know who their constituents are. They can target more effectively."*

Investors want banks to tell their culture story more effectively

Assessing bank culture from the outside is complicated for investors. Ideally, they would like to see a common set of forward-looking metrics that would allow them to understand a bank's culture, how that supports its stated purpose, and identify any potential concerns before bad behavior results in negative news and a decline in share price. Most recognize that *"there is no magic bullet metric for culture,"* however, so they rely on the *"old fashioned way of meeting with management, getting to know them and getting a feel that way,"* according to one investor. As they engage, investors want banks to go *"beyond the annual surveys and KPIs* *and discuss how are they communicating to the shop floor,"* said another. For large investors, especially passive managers with thousands of companies in their portfolios, this deeper engagement is rare, however, often limited to companies with recent issues that could be attributed to culture.

Given no *"magic bullet,"* investors described what they would like to see from banks on culture and how they currently go about trying to get that information:

- **The story behind the numbers.** Investors want to engage directly with a variety of people within a bank to form a view on culture and how it is evolving over time. An investor explained, *"I find it much more interesting and helpful to ask management and the board, 'What do you attribute the trends in the surveys or programs to? Is engagement getting better or worse?' It is more telling to see people are aware of what's behind that. It's the qualitative info behind the data that is helpful."* Another shared a similar perspective: *"Disclosure has increased over the years, but there are some laggards. There are some that provide statistics: Ok, but what are the programs to promote that? I'd much prefer to hear someone say, 'We have a problem with gender diversity, we have more males than females and this is what we are doing to promote,' than to point to statistics that make things seem rosy."*

- **A range of perspectives from across the bank.** Hearing from senior leaders is important, but some investors want to gather a range of perspectives from across different levels of the organization. One said, *"As an investor, you really should be talking to the chair, the CEO, and the line management. If you went to some banks and spoke to the chair, you'd get a completely different idea versus if you spoke to the line managers."* Another investor reported, *"The things I find to be most helpful are going to an office or going to a branch. Sometimes, but not always, we'll tie it to an official visit. IR will say come downstairs and see how we interact with customers and get free cookies."* Another investor described speaking with friends and former colleagues at banks to get a *"general feel"* about the place.

- **Multiple data points to support the narrative.** Investors also value quantitative metrics. Some review engagement survey results, but often don't believe what they read: *"Many surveys don't look too honest to me. They say, 'We have 105% satisfaction.' It's not credible. I know the HR people don't want to go negative for recruiting purposes, but it ends up saying something like, 'All of our employees have oxygen in the office.' It is so ludicrous that it makes you question other disclosures."* They would therefore like to see other data points to corroborate survey results. An investor said, *"Fines are an easy metric. How can you say you have a great culture when you are the all-time leader in fines?"* Another participant commented, *"One way to measure it is to look at attrition, not at the overall form* *but at different levels; middle management versus tellers versus executives. Then the other is the ability to promote from within."*

- **A clear articulation of risk appetite.** Every bank has its own unique risk appetite. Investors are keen to glean insight into how banks integrate purpose into how they assess risk. An investor explained, *"Look at Buy Now, Pay Later. Some banks say the rules are not set, there is a risk of doing the wrong thing for the client, etc. Others will say this is an amazing opportunity. You are going to have a great investment with the ones who see the great opportunity in the short term, but as an investor, you are taking a risk there."* Another said, *"Whenever you talk about culture, people talk about 'good' and 'bad' cultures. But you can be at different ends of a spectrum and be successful. So, the question is, what is the culture and what does that mean for risk-taking and are we comfortable with that?"*
- **An explanation of the role of the board in providing oversight.** Investors expect boards to be involved in the alignment of culture with strategic objectives and want to see evidence of that. An investor asserted, *"It's not enough for the board to say, 'We didn't know.' We would want to understand the information flows, the interaction among the lines of defense. We would want to understand how the board and the risk committee are organized, the power of the CRO, the relationship with the people in the businesses. How robust are the controls? How low is the risk tolerance for breaches? How vigilant are they about monitoring and responding to breaches?"*

Conclusion and next steps

As the ESG agenda continues to accelerate and stakeholder expectations expand, and if cultural issues continue to create losses for investors, purpose and culture will remain essential areas for boards and investors to penetrate. With no commonly agreed set of metrics to rely on, some nuance and ambiguity in assessing purpose and culture is inevitable. Banks and their investors will have to devote time to get that assessment right. A participant noted, *"This is about creating muscle memory about purpose and culture the same way companies have it about profitability, competition, and innovation. There are frameworks and techniques for all of this, but that presupposes the desire to do the work and maintain staying power."* The end goal is not to get a "perfect" purpose statement or the "right" culture, but rather to align purpose and culture to drive long-term value. As one investor stated, *"I would not necessarily say I'd prefer a bank that has worse outcomes but 'better' culture; our fiduciary duty goes against that."*

We invite investor and bank feedback on purpose and culture in banking and on bank ESG communications more broadly. The next session of the BIEP will take place in late spring of 2022 and focus on climate change and the articulation and implementation of strategies to transition to a less carbon-intensive economy.

To learn more about the BIEP and future discussions, please contact Dennis Andrade (dandrade@tapestrynetworks.com) or Tucker Nielsen (tnielsen@tapestrynetworks.com) from Tapestry Networks.

About the Bank Investor Engagement Project (BIEP)

The Bank Investor Engagement Project addresses communication challenges between complex banks and their investors. Its primary focus is to establish key priorities and identify gaps and good practices for effective communication and engagement between institutional investors and banks, especially around matters not covered in existing financial communications. The BIEP is organized and led by Tapestry Networks, in partnership with High Meadows Institute. *ViewPoints* is produced by Tapestry Networks and aims to capture the essence of the BIEP discussions and associated research. Those who receive *ViewPoints* are encouraged to share it with others in their own networks. The more board members, members of senior management, advisers, and stakeholders who become engaged in this leading-edge dialogue, the more value will be created for all.

About Tapestry Networks

Tapestry Networks is a privately held professional services firm. Our mission is to help the leaders of the most important institutions in the world do their work more effectively and with greater confidence. We create an environment where directors, executives, regulators, and policymakers learn from one another, explore new ideas, and collaborate to solve problems, working across the public and private sectors. Our work creates value for those who participate, for those who sponsor it, and for society. Since 2003 we have helped groups of leaders deal with difficult problems, all material to the success of their organizations.

About High Meadows Institute

High Meadows Institute is a think tank and policy institute focused on the role of business leadership in creating a sustainable society. High Meadows Institute conducts research, leads programs, and develops frameworks to increase private sector contribution in addressing the challenges of the 21st century. High Meadows Institute sponsors the BIEP as part of its continuing commitment to drive positive change.

About LRN

LRN is a global firm committed to fostering principled performance and inspiring, rather than requiring, people to do the right thing.

Appendix

The following individuals participated in these discussions:

Participants

- Charlotte Apps, Sustainable Investing (ESG) Associate, Fidelity International
- Mike Ashley, Audit Committee Chair, Barclays
- Jeffrey Barbieri, Vice President, Corporate Governance/ESG Research, Wellington Management
- Laura Barlow, Group Head of Sustainability, Barclays
- Celeste Clark, Corporate Responsibility Committee Chair, Wells Fargo
- Hervé Duteil, Chief Sustainability Officer, Americas, BNP Paribas
- Benjamin Friedrich, Director, BlackRock Investment Stewardship
- Drew Hambly, Executive Director, Global Stewardship, Morgan Stanley Investment Management
- Carolyn Hewitt, Senior Investment Strategist, Responsible Investment, Newton Investment Management
- Frederick Isleib, Director of ESG Research and Integration, Manulife Investment Management
- Christian Leitz, Managing Director, Head Corporate Responsibility, UBS
- Andrew Mason, ESG Investment Director, Abrdn
- Marty Pfinsgraff, Risk Committee Chair, PNC Financial
- Matthew Roberts, Stewardship Analyst, Fidelity International
- Sabahat Salahuddin, Director, BlackRock Investment Stewardship
- Alan Smith, Senior Advisor, ESG and Climate Risk, HSBC
- Katie Taylor, Chair of the Board, RBC
- Federico Wynne, Senior Cross Asset Analyst, Fidelity International
- Tim Youmans, EOS North America Engagement Leader, Hermes
- Maria Zhivitskaya, Investment Stewardship Lead, Vanguard

High Meadows Institute

- Allison Kosta, Communications and Operations Manager
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