Banking on team ethics : a team climate perspective on root causes of misconduct in financial services

Scholten, W.W.

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I gratefully acknowledge the support and sponsorship provided by DNB, which enabled me to carry out this research.

Layout	Bianca Pijl, www.pijlldesign.nl, Groningen, The Netherlands
Cover design	Bianca Pijl
Printed by	Ipskamp Printing Enschede, The Netherlands
ISBN	978-90-828254-0-4 (print) 978-90-828254-1-1 (digital)

Available for purchase at www.wiekescholten.nl

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Proefschrift

ter verkrijging van
de graad van Doctor aan de Universiteit Leiden,
op gezag van Rector Magnificus prof. mr. C.J.J.M. Stolker,
volgens besluit van het College voor Promoties
te verdedigen op donderdag 29 maart 2018
klokke 15.00 uur

door

Wieke Willemijn Scholten
geboren te Alkmaar in 1979

To my father

Promotor
Prof. dr. Naomi Ellemers

Promotiecommissie
Prof. dr. Floor Rink *(Groningen University)*
Prof. dr. Femke de Vries *(Groningen University)*
Prof. dr. Eric van Dijk
Prof. dr. Wilco van Dijk

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Acknowledgements

There are many people who I would like to thank. However, two of them were of essential influence and value: Naomi Ellemers, my supervisor and Frans-Jan van Laer, my husband. They therefore provide the head and tail of my acknowledgements.

It is a great honour to have worked with Naomi. Her clear guidance, paired with her creative thinking, was essential for applying insights to my work practice and innovative usage of data. Her enthusiasm and genuine care for my wellbeing kept me going. I have been very lucky to receive such high quality supervision.

I am grateful to Wijnand Nuijts at DNB for allowing me to do this research. I thank Suzanne Verheij for her help in using supervisory data, along with my DNB colleagues Jildau Piena, Melanie de Waal, Moritz Römer and Sophie Cohen Tervaert, who I hold dear.

Mirea Raaijmakers knows all I am discussing in this thesis without having to read it. The Corrupting Barrels model was born out of one of our great discussions. I cherish her friendship.

I thank Elianne van Steenbergen and Armin Cuyvers for their friendship and advice. I hold Elianne's positive attitude and balanced discipline as all-guiding examples.

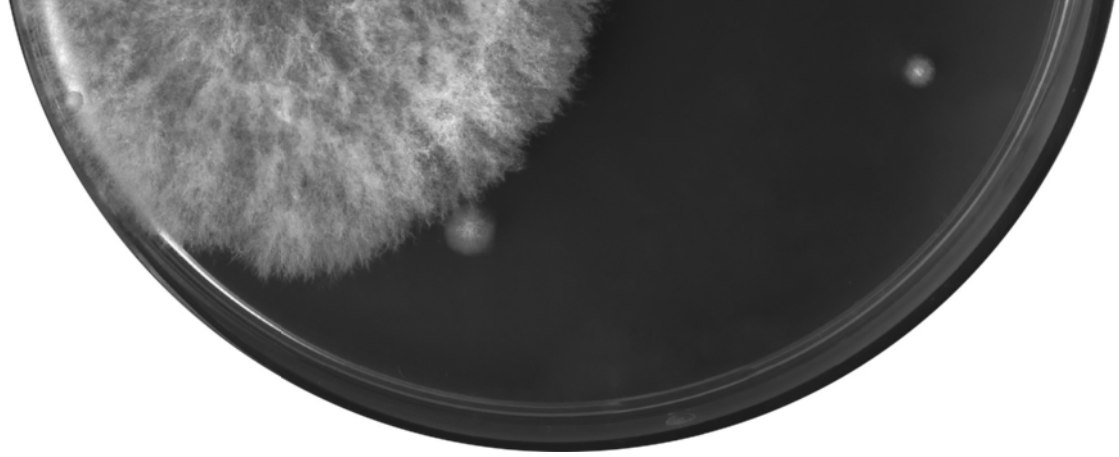
Emma Sluman, Mirjam van den Anker and Wieke Leonhard were always there. I am grateful for their love and support. I thank Debbie Bent and Suzanne Vlek for sharing precious Leiden-memories; Yvonne Span for her interest; Anne and Frans Komen and Paulien and Thijs ten Bokkel Huinink for providing welcome distractions.

A working mother is in true need of others to get anything done. I am grateful to Inez van Laer and Aly Dijk for creating the necessary time and space for me to write.

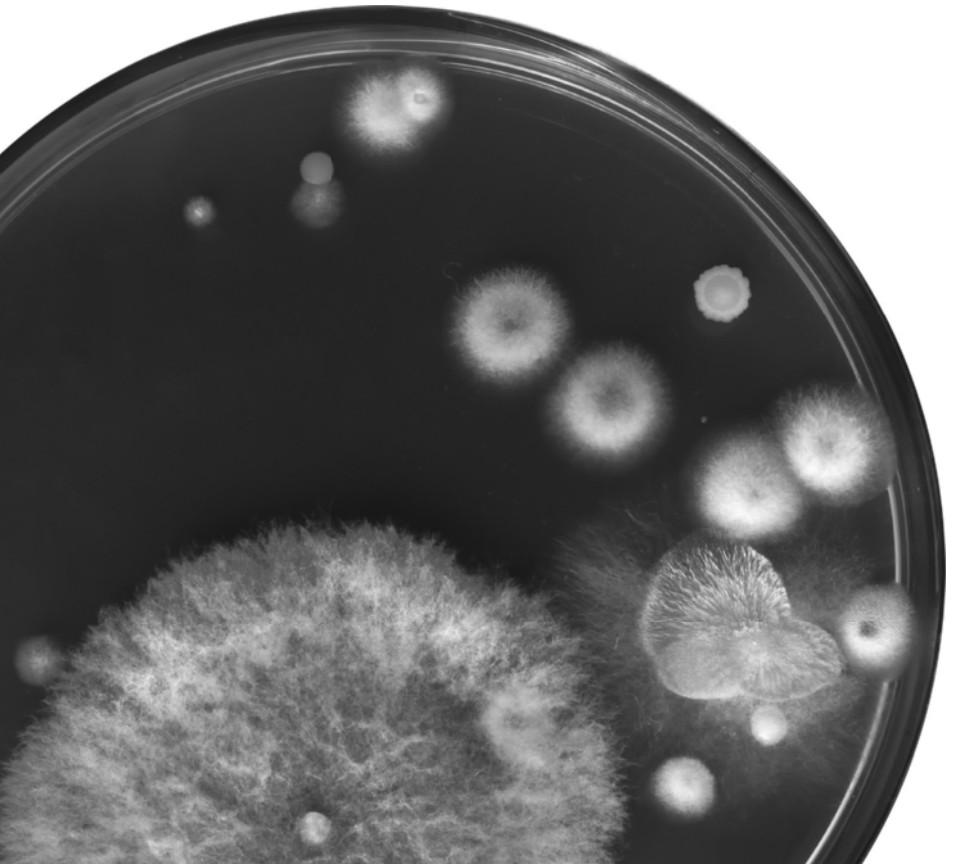
The love and encouragement I received from my parents Arend Scholten and Netteke Schwartz are the pillars on which my life rests. Their interest in and commitment to my personal and professional development have given me fuel; their trust in me has given me courage. They have taught me the joy of learning. I hope I give the same to my marvelous daughters Hedi and Flo.

Finally, I am extremely grateful to Frans-Jan who is at my side in all I do. When I was at a dead end, he thought of new solutions. When I was frustrated, he comforted me. His intelligent suggestions and heartening actions have been of crucial importance to this work and to me.

Wieke
January 2018



Introduction



Introduction

The personal story of Kweku Adoboli, the British trader who was convicted in 2012 for losing $2.3bn of the Swiss bank UBS, was published in the fall of 2015 by the Financial Times[1]. This 'rogue trader's tale' is one of few insider's views gone public of a trader that committed fraud. Adoboli, working in the investment bank's global synthetic equities division, spent nearly four years in prison for exceeding his risk limits and hiding this by booking fictitious hedging trades. He also created a sort of internal fund filled with skimmed profits, that he could use to cover up daily losses. For years, using these methods, he made millions for the bank. In 2010 he was promoted to director and was rewarded by a £250.000 bonus (although Adoboli never received this bonus), on top of his £110.000 salary at that time.

His UBS colleagues, the article says, claim that they had no idea that he was committing fraud. Adoboli maintains that management pushed him to make as much money as he could for the bank and even used him as an example for others when he was doing well. He helped his colleagues when there were problems. A former UBS trader told the author of the FT article that Adoboli was the man to turn to if you had screwed up. He would fix it for you, and "We didn't know how he did it, but we didn't want to know". In line with this statement, Adoboli says that "others did in fact know, and actively encouraged his behaviour for more than two years as long as it was profitable".

Adoboli was convicted when he was 31 years old, and condemned by the public, being the perfect mascot of The City's 'greedy' and misbehaving bankers, when the public trust in banking reached an ultimate low. UBS, his management or his teammates were not held accountable for anything that might have contributed to Adoboli acting like he did. The bank is off the hook. According to Adoboli - as stated in the article - "by holding up himself and Tom Hayes, the former UBS and Citigroup derivatives trader who was jailed ... for manipulating Libor, as rotten apples in otherwise a clean industry, the banks are moving on without considering what happened to allow or even encourage their misconduct".

Now, what caused Adoboli to commit fraud cannot be fully derived from public information released in this FT article alone. What does seem valid, even without having conducted further analysis, is that there is more to his story than merely the individual motivation to make money, or a personal willingness to cross limits and break the rules in doing so. The targets and praise Adoboli received from his management, the calls for aid from his teammates and the fact that others chose not to ask questions, all influenced the way he acted. Adoboli did commit fraud and punishment is justified. Nevertheless, without taking away his individual responsibility and accountability, I argue that punishing Adoboli alone is not enough to prevent future misconduct cases in his or other trading teams within banking. The professional context in which he worked

[1] Financial Times, October 22, 2015. "Kweku Adoboli: a rogue trader's tale". Available at: http://www.ft.com/intl/cms/s/2/0fa0b42a-783a-11e5-a95a-27d368e1ddf7.html

harbours root causes of his misconduct. As long as these contextual root causes are not identified and dealt with, the chance that a misconduct case like this occurs in the future is considerable.

In this book I address contextual root causes of misconduct from a social psychological perspective. My central argument is that shared behavioural patterns reflecting the climate within a trading team can contribute to the (mis-)behaviour of its individual members. Social psychology works from the assumption that our behaviour at work is influenced by our direct social context: our colleagues, our manager and the team we work in. Identifying social psychological root causes of misconduct implies addressing team climate and behavioural patterns as potential contributors to the choices made by individual workers. The bad news of such an analysis is that getting rid of specific individuals who committed fraud (as 'rotten apples') is unlikely to eliminate such contextual root causes of misconduct. The good news is that these root causes represent concrete levers banking divisions can analyse and use to prevent future misconduct cases. Finding contextual root causes, and using social psychological knowledge to prevent future misconduct cases within trading businesses, is the next step that banks and financial supervisors can use to improve the industry. My analysis aims to identify such contextual root causes, invoking current insights from empirical research in psychology, as a way to deliver practical guidelines for banks and financial supervisors that help to prevent future misconduct.

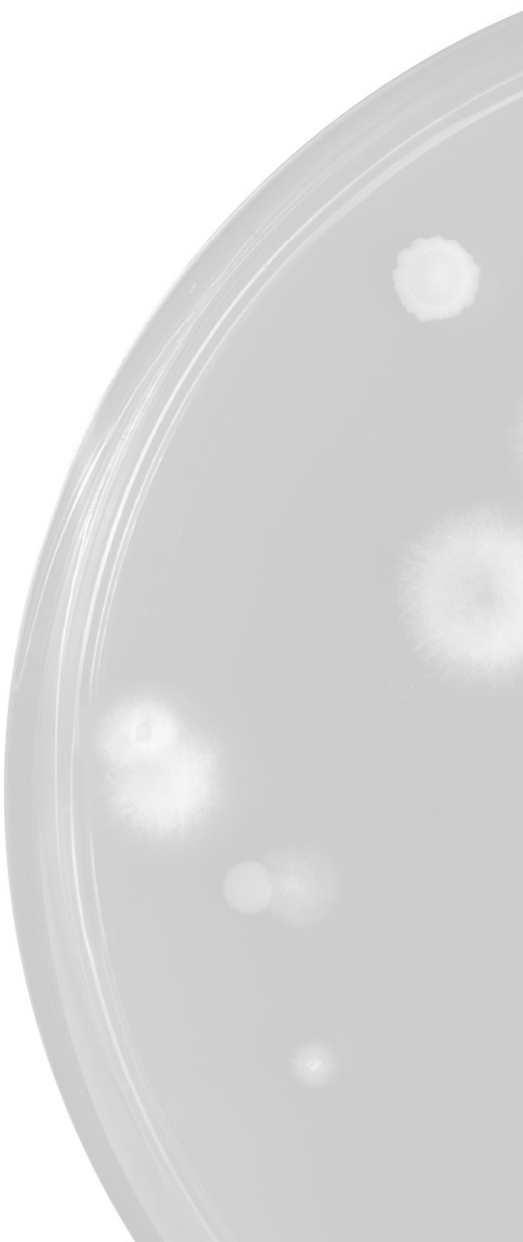
Overview

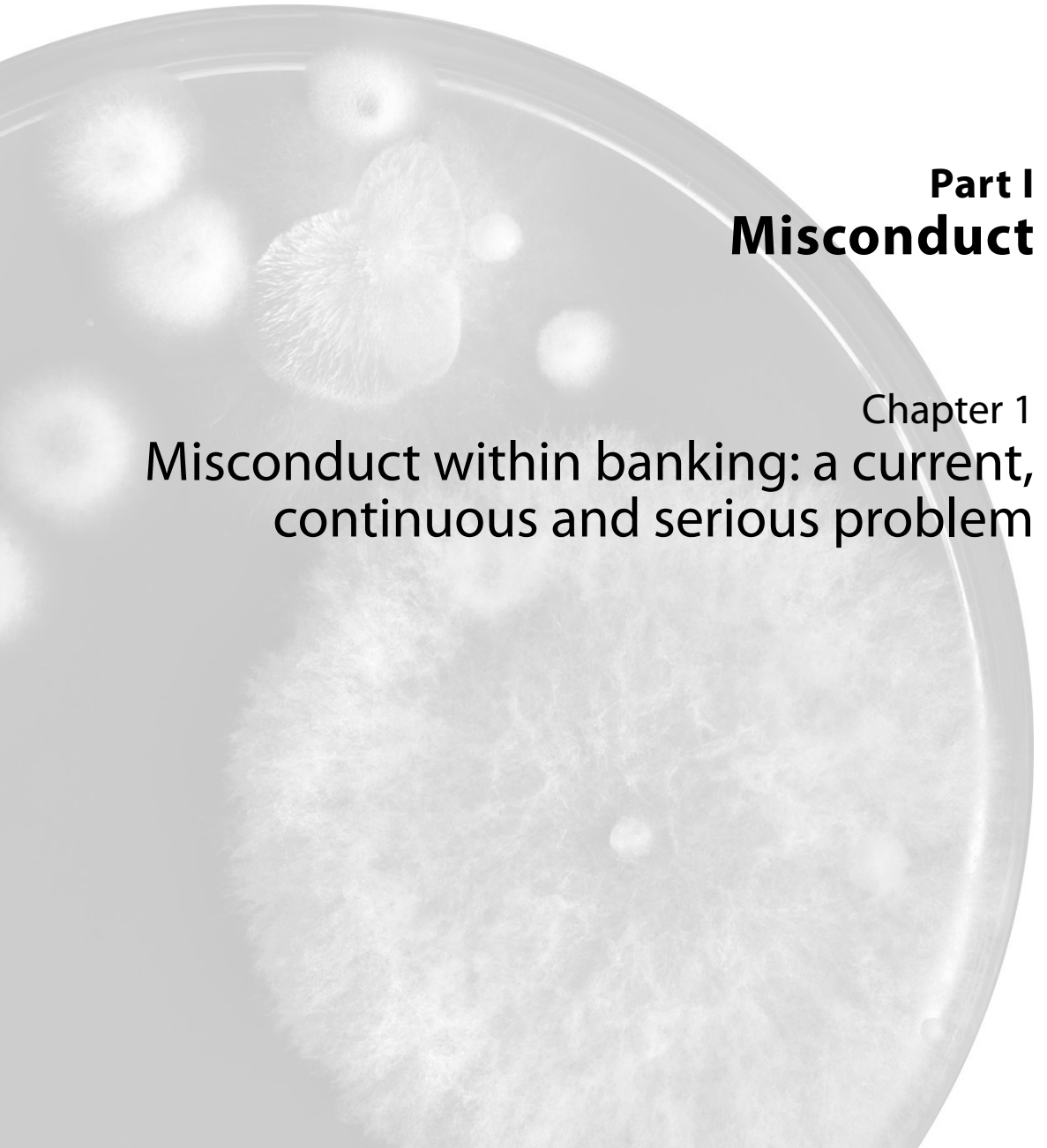
In this book, I present my analysis in four parts. First, Part I introduces the preventive social psychological approach to misconduct within trading teams. It shows that misconduct is a current and continuous problem within banking, and explores its detrimental consequences (Chapter 1). It clarifies my conceptualisation of misconduct, and explains the context of my analysis. When examining relevant contextual variables, I distinguish between (a) the context of financial supervision, that provided the data for this research and (b) the context of trading businesses within banking and three organizational aspects that characterize this professional context (Chapter 2). I elaborate on the central problem presented here: banks and financial supervisors are insufficiently effective in preventing future misconduct. My approach to addressing this central problem is to introduce the Corrupting Barrels model, based on an overview of social psychological root causes of misconduct that offers an approach to effectively prevent future misconduct (Chapter 3).

In Part II, I discuss current banking and financial supervisory practices as outcomes of my analysis conducted in the context of my (former) job in financial supervision. Chapter 4 first offers an overview of two studies and their different research questions and data sources. Then, I present a first study that explores to what extent banks currently include team level in their own analysis of misconduct cases when this is initiated by themselves (Chapter 5 on Study 1). Next, in a second study, I explore the effects of initial supervisory requests asking banks to analyse their misconduct cases and to include the team level in their analyses (Chapter 6 on Study 2).

In Part III, I present a supervisory assessment of social psychological root causes of misconduct within trading teams (Study 3), using the Corrupting Barrels model that I developed as a basis. After introducing the research question and data source (Chapter 7), I first elaborate on the theoretical foundation of the Corrupting Barrels model by providing an overview of the scientific research on three social psychological root causes of misconduct (Chapter 8). I summarize research on error management, relating to the task of the team and the way errors relating to that task are dealt with. An ineffective error approach within a team can form a root cause of misconduct (paragraph 8.1.). Next, I review research on outcome inequality, relating this to the relationships within the team. This inequality, and its emotional consequences such as perceived injustice and envy, can form a root cause for misconduct (paragraph 8.2.). I connect to prior research on morality, relating this to the moral climate within a team. A dysfunctional moral climate can form a root cause for misconduct (paragraph 8.3.). Furthermore, I elaborate on leadership impacting team climates Paragraph 8.4). Finally, I describe Study 3: a supervisory assessment of social psychological root causes of misconduct within trading teams (Chapter 9, on Study 3) and present the outcome of this analysis in the form of a framework (including deskresearch guidance, formats for interviews and observations and a survey) that can be used to identify team climates facilitating misconduct.

In Part IV, I present the conclusions of my analyses and explore the practical implications of the preventive approach of misconduct that can be used by banks and by financial supervisors (Chapter 10). I discuss the way banks and supervisors can use the Corrupting Barrels model and framework to *analyse* the root causes of misconduct (paragraph 10.1). Next, I discuss the way team climates facilitating misconduct can be *improved* using the insights as presented (paragraph 10.2). Finally, in Chapter 11, I consider the strengths and limitations of my analysis and offer suggestions for future research.





Part I
Misconduct

Chapter 1
Misconduct within banking: a current, continuous and serious problem

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Misconduct within banking: a current, continuous and serious problem

1. A current and continuous problem

Since the fall of Lehman Brothers in September of 2008, often marked as the start of the economic crisis, multiple misconduct cases in the trading business that involve unethical behaviour have come to the eyes and ears of the public. In 2013 for instance, the manipulation of London Interbank Offered Rate (Libor) was painfully illustrated by explicit emails between traders who manipulated the Libor. The Libor reflects the rates at which banks borrow money from each other each day and influences what these banks charge their customers (Finel- Honigman & Sotelino, 2015). The emails between traders manipulating Libor revealed neglect of the general public's interests (Box 1), since financial products like mortgages and other loans depend on the Libor, and manipulation of the Libor therefore determines how much the public pays for these financial products. These email exchanges clearly show the traders were aware that their behaviour was fraudulous but considered this to be 'normal' in trading (e.g. "*We're dirty-clean .... No one's clean-clean*").

Even though many attempts were made to address and mitigate misconduct in the trading business, partly as a result of the financial crisis, misconduct in trading is not a problem of the past. Also after 2008, multiple frauds by traders have received public attention and even reached court rooms (see Table 1.1). There is reason to believe more cases exist than the ones that are publicly known. Prudential and integrity supervision within the banking sector pay close attention to cases such as these, as they continue to emerge also today.

Box 1. Libor manipulation: emails between traders

Below fragments of emails between traders and submitters of Barclays, one of the banks involved in the Libor manipulation. These emails were published by several media in the summer of 2013.

- *"I have a huge 1m fixing today and it would really help to have a low 1m tx a lot.": "I'll do my best."*
- *"For you ... anything...", "Always happy to help, leave it with me, Sir," , "Done ..for you big boy.. "*
- *"[Senior Trader] owes me!", "Dude. I owe you big time! Come over one day after work and I'm opening a bottle of Bollinger."*
- *"If you know how to keep a secret I'll bring you in on it,", "We're going to push the cash downwards on the imm day..."*
- *"If you breathe a word of this, I'm not telling you anything else..."*
- *"This is the way you pull off deals like this, don't talk about it too much, 2 months of preparation ... the trick is you must not do this alone ..."*
- *We're clean, but we're dirty-clean, rather than clean-clean.", "No one's clean-clean."*

The problems identified in Table 1.1 are not contained within a specific organization, and continue over time despite increased regulatory scrutiny and supervision. This leads to at least two conclusions. The first is that misconduct in this sector is a current and ongoing problem. As a (ex-) financial supervisor I am bound to confidentiality, and not in the position to give recent examples of misconduct cases that have not (yet) been made public. That having been said, my own experiences as a financial supervisor, and the continuous attention financial supervisors have for integrity supervision and misconduct prevention, give rise to the statement that the cases in Table 1.1 cannot be seen as exceptions to the rule, nor do they represent 'tales from the past'.

Table 1.1 *Five publically known large misconduct cases perpetrated by individual traders, before and after the onset of the financial crisis in 2008 (as described in Finel-Honigman & Sotelino, 2015).*

	Trader	Bank	Year*	Summary of misconduct	Consequence for bank	Consequence for trader
1	Nick Leeson	Barings (Singapore desk)	1995	Creating fictitious accounts to cover up losses, resulting from taking excessive risks.	Barings was sold to ING for the symbolic GB£1.-.	Sentenced to 6.4 years in jail – served four.
2	Jérôme Kerviel	Société Generale (Delta desk)	2008	Creating fictitious reports or claiming error has occurred, to cover up losses, resulting from taking excessive risks.	Trading loss: €4.9 billion. Société Générale was accused of lax risk management and poor supervisory controls.	Sentenced to 3 years in jail – served 100 days.
3	Kweku Adoboli	UBS (Exchange traded funds desk)	2011	Placing unauthorized trades, betting on stock markets. Using an 'umbrella account' to hide evidence. Using profit to cover up gambling debts.	Fined GB£29.7 million by the UK FSA.	Sentenced to seven years in jail – served four.
4	Bruno Iksil	JP Morgan (London desk)	2012	'The London Whale': building a synthetic credit portfolio, proprietary position. Manipulating valuations of the portfolio to cover up losses.	Trading loss: US$6.2 billion. JP Morgan incurred fines and penalties of over US$2 billion.	Fined, not sentenced to jail.
5	Tom Hayes	Several banks were involved in LIBOR; Hayes worked at RBS and Citi.	2015	Manipulation of the London Interbank Offered Rate (Libor). Hayes is the first trader involved that is sentenced.	The next paragraph provides an overview of fines to banks involved in LIBOR, under "Business perspective: costs of misconduct".	Sentenced to 14 years in jail, in December 2015 lowered to 11 years.

** Year of court ruling.*

The second conclusion that can be drawn from Table 1.1 is that misconduct cases constitute a continuous problem, and seem to repeat over time. This implies that the problems identified are not contained within a specific banking organization, and suggests that it is not easy for those in practice to learn effectively from prior occurrences of similar problems elsewhere. An example is the lesson that could have been learned from the Leeson case in 1995: it is risky to grant traders access to back office operations, while at the same time taking trading positions. Thus, a more general conclusion could have been that such combined discretions should not be assigned to a single individual. Yet, in 2008 Kerviel and in 2011 Adoboli, both junior traders, had access to back office operations to cover up their questionable investments – just as Nick Leeson had. These cases also involved back office manipulation of accounts and creation of false accounts, but could have been prevented if (junior) traders had not been offered such access to back office operations after the Leeson case had come to light (Finel-Honigman & Sotelino, 2015).

In the next section, I will elaborate on why such misconduct is not only current and continuous, but also a serious problem – by elucidating its detrimental consequences and broader implications for the financial sector and as a factor that may undermine economic stability.

2. Detrimental consequences

Misconduct of traders has detrimental and negative consequences for a bank; from a business perspective, as well as a legal perspective. I will elaborate on each below.

Business perspective: costs of misconduct

From a business perspective, misconduct is costly. There are several reasons for this. First, the trading losses as a direct result of the misconduct are often massive. The Société Generale case of 2008 (see Table 1.1) resulted in a trading loss of €4.9 billion; the London Whale case led to a trading loss of US$6.2 billion.

Second, banks are faced with high fines – imposed by courts and regulators – and settlements - arranged with prosecutors. Illustrative of the height of fines is that these fines in the US exceeded US$25 billion in 2012, which included fines for fraudulent mortgage back securities transactions (JP Morgan, Bank of America, Goldman Sachs and UBS), and the manipulation of Libor (Barclays, Rabobank and RBS) (Finel-Honigman & Sotelino, 2015). For Europe, the same trend is observable. Between 2010 and 2015, fines imposed in Europe have been increasing, reaching a cumulative total of around EUR 200 billion for all banks and EUR 50 billion for EU banks (Finel-Honigman & Sotelino, 2015). Taking the Libor scandal as an example, the settlement between the implicated banks and US and UK regulators, by October 2013, had reached US $1.5 billion for UBS, US$450 million for Barclays and US$615 million for Rabobank. Further, the European Commission fined Deutsche Bank €259 million; RBS €260 million and JM Morgan €80 million for the attempted manipulation of the Libor and Euribor rates (Finel-Honigman & Sotelino, 2015).

Third, misconduct often forces banks to set aside additional capital and cover litigation and redress costs. As a result of the Libor case for instance: Swiss regulators ordered UBS to increase by 50% the amount of capital held against compliance and operational risk, and litigation costs, and Deutsche Bank set aside an additional 1.2 billion to meet litigation costs (Finel-Honigman & Sotelino, 2015). Indeed, misconduct is costly from a business perspective because of high litigation and redress costs. The European Systemic Risk Board (European System of Financial Supervision) elaborates in its 2015 report on misconduct risk in the banking sector, on the costs of misconduct. It reports an increase in costs of expanded legal departments, fees for external consultants and legal advisers. The ESRB report refers to a survey that showed 84% of banks reporting an increase in litigation spending since 2008. Finally, redress costs can be a factor in case of mis-selling of financial products. Between 2010 and 2015, more than EUR 100 billion redress costs are paid to both professional and retail clients around the world (ESRB, 2015).

Now, all the costs summed up here – trading losses, fines and settlements, (forced) capital provisions, litigation costs and redress costs – can build up to enormously high 'costs per case' that can have a detrimental effect on profitability. The ESRB report (2015) states that without past litigation costs and provisioning for future litigation costs, the total accumulated profits of large European banks in the period between 2010 and 2015, would have been a third higher. Furthermore, uncertainty about often long-lasting litigation may have a negative impact on the shareholder value of banks. The performance of shares of a bank with litigation issues is substantially lower than for banks without litigation issues. The ESRB reports that the market capitalization of the banks with litigation issues would have been EUR 54 billion more in December 2014 if their share prices had followed the same trend as those of the banks without any litigation issues. In sum, the costs of misconduct from a business perspective, have a considerable impact on financial performance. The costs of misconduct can lead to serious capital pressure, forming a risk for soundness and stability of banks.

Business perspective: reputational damage and trust decline

A second detrimental consequence of misconduct in banking, from a business perspective, is reputational damage and its negative impact on trust. Although unethical behaviour in trading businesses does not represent behaviour in the banking sector as a whole, it has likely led to a decrease of trust in our financial economy and the banking system in particular. The current trust of the public, consumers, politicians, companies, in banks is at an ultimate low (Cruijsen, van der, *et al.*, 2014; ESRB, 2015). Stereotyping of traders who will do anything to increase their profit, and have lost their heartfelt ambition to serve society, is at an ultimate high. This is alarming because a decrease in trust in the banking sector hurts our real economy. Businesses are more careful to spend and invest. Reputational damage harms future sales and funding conditions, and that is costly. In fact, the ESRB report (2015) states that the "reputational penalty" is estimated to be 7.5 times the total amount of monetary penalties imposed by the U.S. Securities and Exchange Commission on the 585 firms subject to enforcement actions for financial misrepresentation between 1978 and 2002. Reputational damage leads to a decrease in trust, and therefore in a risk for solidity and stability of the banking sector.

Legal perspective

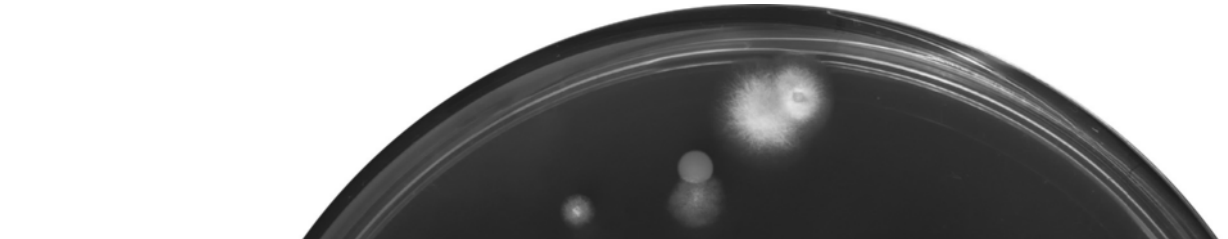
Next to these detrimental consequences of misconduct from a business perspective, negative consequences from a legal perspective are to be considered. Court rulings in misconduct cases increasingly attend to the accountability of the bank involved, and include the senior management overseeing the trader that behaved unethically. Trader misconduct thus implies liability risks for banks and senior management. This was for instance the case for Deutsche Bank, which was ordered in 2013 by a Frankfurt Labour Court to rehire four traders who had previously been fired by the bank, because of their involvement in Libor manipulation[2]. Judge Annika Grey added to her ruling that Deutsche Bank did not have "*adequate internal rules and controls in place and did not ensure that rate submitting and derivatives trading was adequately separated*". Here, Deutsche Bank was held accountable for creating circumstances that allowed these traders to behave unethically. Firing them was therefore considered unlawful. Likewise, in 2015 the Financial Conduct Authority fined a former executive of JP Morgan GB£792.000 for failing to be "open and cooperative" about the 'London Whale' case (see Table 1)[3]. This executive oversaw Bruno Iksil, the trader who was linked to the misconduct. Although the fine is not related to lack of oversight or mismanagement in this case, but on his insufficient communication towards financial supervision, it is an example of senior management being held accountable for its role in a misconduct case. A third example of a court ruling that held the bank or senior management accountable is the 2016 ruling in the Kerviel case. A French tribunal ordered Société Générale to pay €400.000 for unfair dismissal, to Jérôme Kerviel, who was sentenced to jail in 2008 (see Table 1)[4]. Kerviel seemingly never denied the fact that he had covered up losses and created fake trades; misconduct that resulted in a trading loss of €4.9 billion. But he also claimed that his employer was fully aware of his actions. The French court ruled that the bank shared responsibility for what happened. Finally, banks are increasingly holding each other accountable for misconduct. An example is the Foundation for Banking Ethics Enforcement (FBEE). This is an independent disciplinary board for bankers, that can issue fines up to € 25.000,- when a banking employee breaches the code of conduct (see: www.tuchtrechtbanken.nl/about-us).

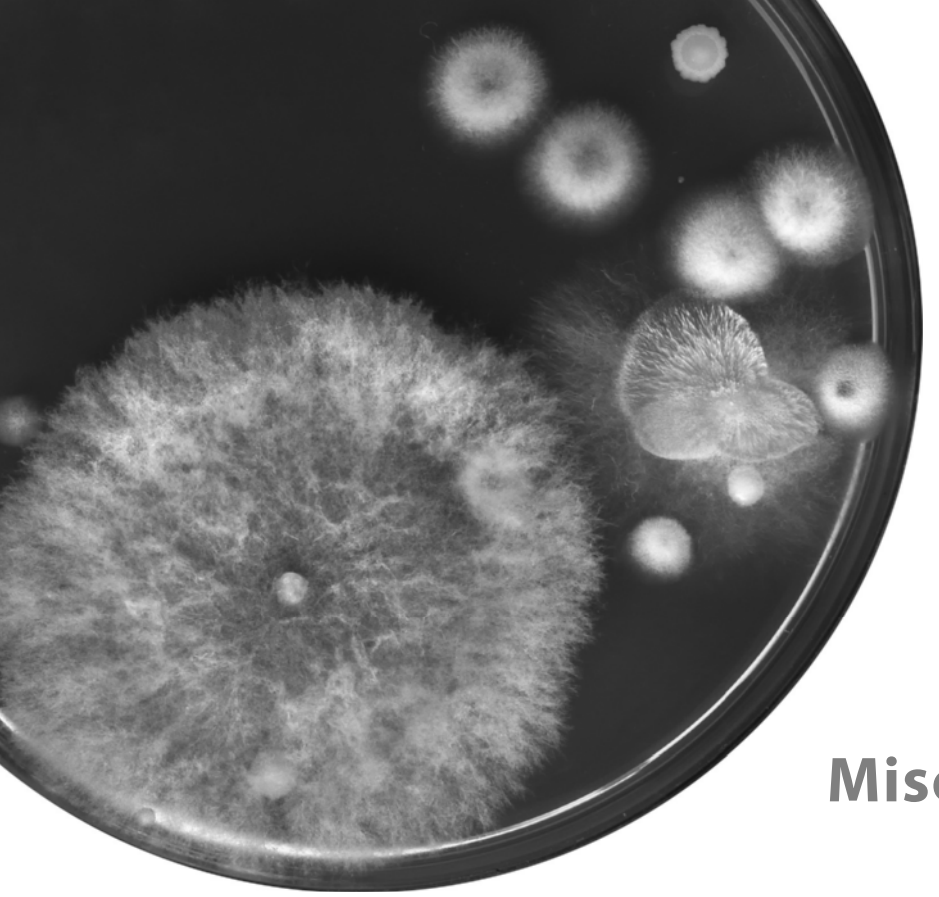
In sum, misconduct has detrimental consequences from a business and legal perspective. Needless to say, taking these consequences in consideration, misconduct by traders within banking needs to be prevented and dealt with effectively. It is not only in the interest of financial supervisors or the general public, but also key to the survival of banks themselves to prevent misconduct from occurring in the future.

[2] The Telegraph: September 11, 2013. "Deutsche Bank ordered to rehire traders unlawfully sacked in Libor probe". Available at: http://www.telegraph.co.uk/finance/newsbysector/banksandfinance/10303136/Deutsche- Bank-ordered-to-rehire-traders-unlawfully-sacked-in-Libor-probe.html

[3] The New York Times: February 9, 2015. "Ex-JP Morgen executive fined 1,1 million in London Whale case". Available at: http://www.nytimes.com/2016/02/10/business/dealbook/ex-jpmorgan-executive-fined-1-1-million- in-london-whale-case.html?_r=0

[4] The Financial Times: June 7, 2016. "Kerviel wins €400,000 from SocGen for unfair dismissal". Available at: http://www.ft.com/intl/cms/s/0/82e3c230-2ca6-11e6-bf8d-26294ad519fc.html#axzz4BrY6cBfS





Part I
Misconduct

Chapter 2
Investigating misconduct: conceptualization and context

Chapter 2
Investigating misconduct: conceptualization and context

1. Conceptualising misconduct

I use the term misconduct to refer to intentional unethical behaviour of traders in banking. Three characteristics are relevant in my conceptualization of misconduct: acts and omissions, intentions and the unethical nature of the behaviour.

Misconduct refers to imputable acts as well as omissions. Acts of traders in this context could be for example sabotage – such as the misrepresentation in financial reports -, bribing others (active corruption) or being bribed (passive corruption) by a third party, theft, the miss-selling of financial products to professional clients or manipulation of financial markets (DNB, 2014). Examples of omissions are: failing to act when action is called for (e.g. warning clients of large financial risks or laying out long term strategy implications) or failing to perform duties or responsibilities (such as reporting information on deals, or specifying transaction costs). In lay terms these acts and omissions are referred to as 'fraud'.

Misconduct refers to intentional behaviour. This means that unintended errors and accidents are excluded from this analysis. Intentional behaviour means that there is an explicit intention, a will, an aim, that motivates the involved trader or sales professional to act or not act (in case of an omission) in ways that imply professional misconduct. The exact intentions for misconduct often cannot be established in retrospect. In fact, they often are not even explicitly addressed in reports on misconduct cases by banks (as a result of internal investigation by audit or legal departments for instance) or by financial supervision. These reports tend to take a legal perspective as they focus on the facts of misconduct, the (financial) impact and causes in terms of opportunity to behave unethically, the lack of oversight and the failure of control mechanisms. The individual intentions that may have led to the misconduct are often not investigated or at least not reported. However, it is often presumed, by public, media and the banking sector itself, that such intentions are obvious. For instance, traders are seen to exceeded risk limits because they wanted to make high revenue to ensure their bonus. Their motivation for (not) acting thus is assumed to consist of the desire for individual monetary gain. The contextual causes of this behaviour – such as the social norms within a team on how to deal with these risk limits - are disregarded. This is in line with the fundamental attribution error (Ross, 1977), explaining people's tendency to infer intentions when observing others behave, whilst disregarding contextual causes that led up to this behaviour. However, when analysing one's own behaviour, these contextual causes or circumstances are weighed heavily.

- *An illustrative example from supervisory practice (Nr. 1, see Table 2.1)*

  "*These guys want to rob my bank*", uttered a CEO of a global significant bank during a discussion of misconduct cases within his investment banking division. With 'these guys' this CEO referred to the traders who were involved in the misconduct cases that were subject of this supervisory meeting with him. He implied that the traders that behaved unethically, were motivated by the desire to gain money and steal this from the bank.

Another inferred intention – also driven by the alleged desire for individual gain - is that a trader wants to increase promotion chances and therefore aims at impressing his or her superiors with his or her trading strategies. Also, the desire to cover up losses as a way to maintain a certain status within his or her team is related to the inferred desire to increase monetary outcomes or organizational prospects. The interview with Adoboli cited at the introduction of this book, suggests this may have played a role in his case. Again, these individual intentions are not studied systematically and could be interlinked or be different expressions of the same motive. Even though misconduct in this analysis is used to refer to intentional behaviour, I do not aim to identify a single explanatory intention – along the lines as mentioned above. Even though I conceptualize misconduct as a form of intentional behaviour, the specific underlying individual motivations of the traders involved are not the focus of my analysis. The focus of my analysis is to assess the drivers in the social context of these traders, as raising intentions that influenced their individual misconduct.

Misconduct refers to unethical behaviour, that is, behaviour that breaches widespread agreement about what is right and wrong. Kish-Gephart, Harrison and Klebe Treviño (2010) define unethical behaviour in a work context, as organizational member actions that violate widely accepted (societal) moral norms. This definition aligns with other research on ethical behaviour in work contexts (Kaptein, 2008; Treviño & Nelson, 2007). According to Kish- Gephart *et al.* employee behaviours that breach generally accepted moral norms of behaviour include lying to customers, theft, sabotage and misrepresentation in financial reports. They exclude other negative workplace behaviours such as lateness from this definition, because these may not be intentional and do not necessarily violate widely accepted societal moral norms (Kish-Gephart *et al.*, 2010).

Misconduct refers to unethical behaviour, that can also be illegal. Illegal behaviour is behaviour that breaches legal regulation or rules. In the trading and sales context, financial and trade sanctions and regulation governing competitiveness (collusion of market prices) are examples of these regulations. Bear in mind that, although unethical and illegal behaviours overlap, there are also unethical behaviours that are not illegal, such as behaviours that are 'only' prohibited by codes of conduct. Trevino and Nelson (2007) use the 'financial meltdown of 2008' to explain the difference between unethical and illegal behaviour. They claim that the implosion of the financial market in 2008 was a result of unethical behaviour, not of behaviour that was illegal at the time. "Government regulators and the legal system often play catch-up after unethical debacle in

business": the activities that brought down the economy were not (yet) illegal. However, they state, many of those activities were seen as unethical and were contrary to ethical principles such as responsibility, transparency and fairness.

In sum, in my analysis I consider misconduct as referring to unethical behaviour, that can be illegal as well. As discussed later on, misconduct cases in the financial context are often handled by legal departments, focusing on a legal approach. In this approach, the misconduct considered is often confined to mere illegal conduct. The present research chooses a broader approach of misconduct that focuses on the unethical nature of behaviour displayed by traders in these cases. It adds to the dominant legal paradigm within banking, when dealing with misconduct, as will be elaborated in Chapter 3. This conception of misconduct also clarifies that regulatory developments, adding rules and restrictions, cannot fully control unethical behaviour by itself – rules alone are not enough to prevent future problems. Next to rules, culture improvements are needed. The aim of my analysis and research is to reveal levers that can help improve team climates and with that, prevent future misconduct.

2. Clarifying the context: supervision of behaviour and culture

I examine the validity of the analysis provided, with a detailed consideration of misconduct cases and anonymous examples derived from information gathered in the context of actual supervisory activities. Although the examples are based on real practices and actual communications, the anonymity of the supervised banks is guaranteed and the supervisory information remains confidential. The materials used for this purpose consist of supervisory information, comments and events that I observed at Dutch and European banks – including significant institutions ('too big to fail' banks), during my work as a senior supervisory officer of behaviour and culture at De Nederlandsche Bank (DNB).

DNB is responsible for prudential supervision of financial institutions, including banks, in the Netherlands. Since 2011, in addition to addressing solvency and liquidity of financial institutions, the DNB supervision also takes into account behavioural patterns and culture aspects of these institutions (Raaijmakers, 2015; Nuijts & De Haan, 2013). Behaviour and culture supervision observes and analyses behavioural patterns in, for instance, leadership, decision making and group dynamics that are essential for sound functioning and enduring performance of a bank. The aim of this type of supervision is to identify and mitigate the risks these behavioural patterns or cultural aspects can have for financial stability and performance of a bank. For example, a trading team handling errors in such a manner that a bank does not learn from what happened, nor is able to prevent the same error from happening again – resulting in ineffective error management – is an example of a behavioural pattern that bears risks for the enduring financial stability of the organization.

DNB was globally the first financial supervisor that explicitly extended supervision to the domain of behaviour and culture (Raaijmakers, 2015; IMF Global Stability Report, 2014). An expert team of supervisors with different professional backgrounds, including organizational psychologists, executes this supervision and is also required to deliver expertise to European banking supervision. More financial supervisors, such as the Dutch Authority for the Financial Markets (AFM) and the Australian Prudential Regulation Authority (APRA) are now working with supervisory expert teams that are explicitly dedicated to behaviour and culture.

The information provided about concrete cases is derived from supervisory assessments at Dutch and European banks, including the 'too big to fail' banks. Every example included in this research is anonymized and stems from interviews conducted in the context of behaviour and culture supervision. The records of these interviews are kept by DNB supervision. Table 2.1 lists the 17 illustrative supervisory examples used throughout this book, and offers information about their sources. These stem from interviews with 14 key players at 4 different banks. The supervisory meetings are conducted primarily with traders within investment banking divisions, executive (management) board members responsible for these businesses, and compliance, audit and risk management officers. By implication, the anonymous examples and cases used here are representative for the Dutch and European banking sector, and reflect real practices within these banks.

Table 2.1. Sources of illustrative supervisory examples in this book

Nr.	Page	Snippet from illustrative example	Interviewee	Role	Bank
1	30 and 44 (used twice)	*"These guys want to rob my bank"*	1	CEO	Bank A
2	35	*"We are risk managers, more than traders".*	2	Senior trader	Bank A
3	37	*"They were hiring us by the dozen"*	2	Trader	Bank A
4	37	*"You do fx, you do fx, and you do fx, And who gets the business set up first, gets to run it."*	3	Senior manager of trading desks	Bank A
5	38	*The only thing that counts is our P&L: profit'*	4	Trader	Bank A
6	44	It was a set up: the trader and the third party arranged this scheme before the trader started to work at this bank.	-- (derived from desk research)	-- Not a quote	Bank A
7	45 and 100 (used twice)	*"That is just the way he is".*	5	CEO	Bank C
8	50	*"I know something happened at the desk two rows away from me on the floor, since someone was suddenly missing and fired"*	6	Trader	Bank A
9	50	"*Tell me their names, and I will fire them all"*,	1	CEO	Bank A
10	51	Instead of their own cases, anonymized cases of other banks were used as illustrative training material.	7	Senior compliance officer	Bank A
11	54	"*Culture or profit: what do they want from me* ?"	8	Trader	Bank A
12	97	*"We assume you have thought this over. Please explain to us your reasoning on these events"*	9	Senior manager (CEO-1)	Bank B
13	98	The colleague confirmed that the reputation of the employee was damaged, although the blame of the failed project on the employee stayed implicit.	10	A project leader and colleague	Bank D
14	101	In strong words – including swearing - he was summoned up to the board floor. The senior manager dreaded these calls and what would come next.	9	Senior manager (CEO-1)	Bank B
15	106	*"Stop preaching to me, with your income you do not need to worry about making more money like I do"*	12	Trading desk head	Bank A
16	107	"*He made us look like we were criminals! I never have been so angry"*	11	Trading desk head	Bank B
17	110	*"It is kind of strange isn't it… I work in oil, but I personally do not think it is good for our climate and environment"* .	13	Middle manager of trading desks	Bank B
18	146	The senior manager calling the desk head of desk A, with the dysfunctional leadership style, "high potential" that needed some coaching to work on his "relationship management".	14	Senior manager of trading desks	Bank B

In Chapter 9, I present an assessment framework that is used by the DNB supervision of behaviour and culture in the Dutch and European context. It is designed to identify and assess social psychological root causes of misconduct within trading teams. This assessment has the aim to mitigate misconduct risk by requiring banks and businesses within banks to change team climates that harbour these root causes. The empirical evidence described in Part III of my analysis is the outcome of the application of this framework by the DNB supervision of behaviour and culture.

3. Clarifying the context: trading

For my analysis, I chose to focus on the context of trading businesses within (investment) banking. In this section I substantiate this choice of context, and elaborate on the organizational aspects that characterize this professional context. Misconduct occurs within the financial sector mostly within banking. De Nederlandsche Bank (DNB) – the Dutch central bank and financial supervisor of the Netherlands – registers supervisory incidents, among which misconduct cases. DNB oversees the Dutch financial sector and distinguishes within this sector between four subsectors: banks, insurance companies, pension funds and trust agencies.

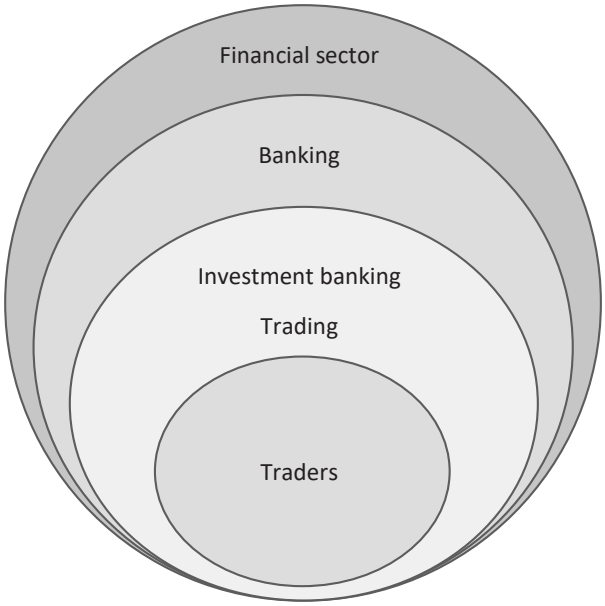
Table 2.2. *DNB Supervisory Incidents – 2013, 2014, 2015*

DNB supervisory incidents				
	Banks	Insurance companies	Pension funds	Trust companies
The total number of misconduct cases (or 'integrity incidents'), added over the three years 2013, 2014 and 2015	30	17	7	6

The DNB data shows (see Table 2.2) that in the Netherlands, most known misconduct cases occur in the banking sector, opposed to the other subsectors. This is not just the case for the Netherlands: also at international level, banks are the financial institutions facing the most significant misconduct issues (ESRB, 2015).

My analysis reported here specifically addresses unethical behaviour of traders, who work in trading business, within investment banking. For simplicity and readability, I refer in this analysis to these professionals as 'traders'. Figure 1.1 shows how banking, relates to investment banking, and to the businesses central in my analysis. Boxes 2 and 3 summarize what investment banking and trading businesses entail.

Figure 2.1. *Zooming in: the context of this research.*



I chose this specific context for misconduct – the trading business - for two main reasons. First, the risk and impact of misconduct occurring in trading is relatively high. Traders often have control of large amounts of funding or credit. A large part of profit of a bank is made here. Traders are highly responsible for decisions they make and often have to make these decisions by themselves, under time pressure (for instance when traders run their own book). Hedging the risks that come forth from trading positions, is one of the most important tasks of a trader. A senior trader remarked during a supervisory interview in 2015: "*We are risk managers, more than traders" (Nr. 2, see Table 2.1)*. In sum, unethical behaviour of traders, can lead to severe financial consequences for the bank (see for instance the trading losses in Table 1.1).

Box 2. Trading business

Trading businesses generally deal with four main asset classes: rates, equity (stocks), cash equivalents (money market instruments) and fixed income (bonds). For example, the markets division within Corporate Banking & Securities of Deutsche Bank AG (Deutsche) was at year-end 2013 responsible for trading of fixed income, equity, equity-linked, foreign exchange and commodity instruments, in addition to structuring and implementation of financial risk management solutions for institutional clients (Finel-Honigman & Sotelino, 2015). The main trading locations in the world are London ('the City'), New York ('Wall street') and Singapore/ Sydney.

Box 3. Investment banking

Investment banking refers to capital markets services of banks to institutional clients. According to Finel-Honigman and Sotelino (2015), 'the primary role of an investment bank is to design and realize financing structures, that satisfy the objectives and constraints of both the issuers and investors'. Investment banking is often combined with corporate banking within a wholesale bank. The main revenue generating activities of an investment bank encompass (Finel-Honigman & Sotelino, 2015) securities underwriting, secondary market-making in these securities for investors, structuring of, and market-making for risk management instruments (derivatives), propriety trading in securities, commodities, foreign exchange and derivatives, credit (typically short-term and secured) to issuers, investors and trading counterparts and mergers & acquisitions advisory services.

A second reason to focus this research on misconduct within trading businesses, is that many examples of misconduct that are known to the public occurred in these businesses. The examples given in Table 1.1 are illustrative of that. Misconduct of traders has received media exposure and therefore has impaired the trust of the public in the soundness and integrity of banking in general.

Even though the context of my analysis is rather specific, as illustrated in Figure 1.1, misconduct can take place at any organizational context or specific business. It can display itself at a level across businesses, a whole bank or across the entire banking sector. In principle, the Corrupting Barrels model that I develop and the supervisory framework that is a result of my analysis can be used in any organizational context.

Organizational aspects

There are three organizational aspects that I will discuss here, since they characterize the professional context of (investment) banking and trading businesses specifically. These are aspects of the organizational context, that are relevant for behavioural patterns and team climate within trading teams. These three organizational aspects are: a history of strong and fast growth of the businesses, a history of revenue as the main organizational goal, and a history of high pay or incentive compensation.

First, investment banking has a history of strong and fast growing business. The 1990's pushed trading businesses to great heights. Due to the lowering of barriers to international capital flows, rapid technological change and the explosive growth of securities markets, many corporate commercial lenders engaged in investment banking in this period of time. Banks would buy investment banking activities, and rapidly set these up themselves (Finel-Honigman & Sotelino, 2015; Brink, R.C.G. van der, 2003).

- *An illustrative example from supervisory practice (Nr. 3, see Table 2.1)*

  During interviews with traders of a global significant bank during a supervisory assessment, a trader looked back on how he was hired in the early 2000's. He stated 'They were hiring us by the dozen', and remembered how he was sitting in a hallway with 'twenty other guys who went for trading positions'. 'They were calling us in two at a time, running different interviews simultaneously'.

This simultaneous hiring of traders and whole trading teams, came hand in hand with a push on growing the business rapidly.

- *An illustrative example from supervisory practice (Nr. 4, see Table 2.1)*

  During a supervisory interview at a global significant bank, a senior manager within investment banking who worked as a trader at that same bank in the early 2000's recalled how the Fx trading business was set up and started. She recalled that many Fx traders were hired at the same time and were instructed as followed: '*You do Fx, you do fx, and you do fx. And who gets the business set up first, gets to run it*'.

There are two risks of this legacy of strong and fast growth in trading businesses and teams. First, the fast acquisition and building of investment bank activities by retail or consumer banks led to a degree of *detachment* of these investment banking activities from the bank. These investment banking activities were often unknown territory for these banks: new products, a new way of making money, new geographical locations and a new kind of people (Van der Brink, 2003). This detachment of the organization as a whole, led to a high autonomy of these trading businesses. It contributed to the creation of an isolated playing field with the possibility to set up own rules and new ways of working.

Second, all banks were acquiring or setting up investment banking activities during the same period (roughly 1989 – 2008: see, Finel-Honigman & Sotelino, 2015; Van der Brink, 2003). This led to a high demand for young traders, and resulted in considerable mobility: being a 25 year old Fx trader, in those days you could find highly paid employment at many banks. If a position did not suit you, there was plenty of opportunity to 'hop' to another Fx team, at another bank (even often in the same financial district, e.g. around the corner). Both aspects, detachment of the organization leading to autonomous playing fields and high employment mobility, would make it easier for young Fx traders to identify and connect with their peer group – Fx colleagues - rather than the particular bank they were working at. The detachment, autonomy and mobility evoked identification with teams, over and above identification with the organization as a whole.

Now, why is this high identification with a team relevant for the contextual root causes of misconduct? The more we identify with our team, the more our team influences our individual behaviour (Postmes & Branscombe, 2010; Ellemers et al, 1999; Tajfel & Turner, 1979). A high

identification with a trading team augments the influence of that team – and its distinctive norms and habits - on the ethical behaviour of an individual trader. Therefore, a legacy of fast growth of the business is a contextual factor that possibly strengthens the relation between root causes at the team level and misconduct.

A second relevant contextual factor for investment banking is the legacy of revenue being the main organizational goal. In my supervisory interviews with traders, increasing profitability was often seen as the main goal of their work, and the main thing management asks of them.

- *An illustrative example from supervisory practice (Nr. 5, see Table 2.1)*

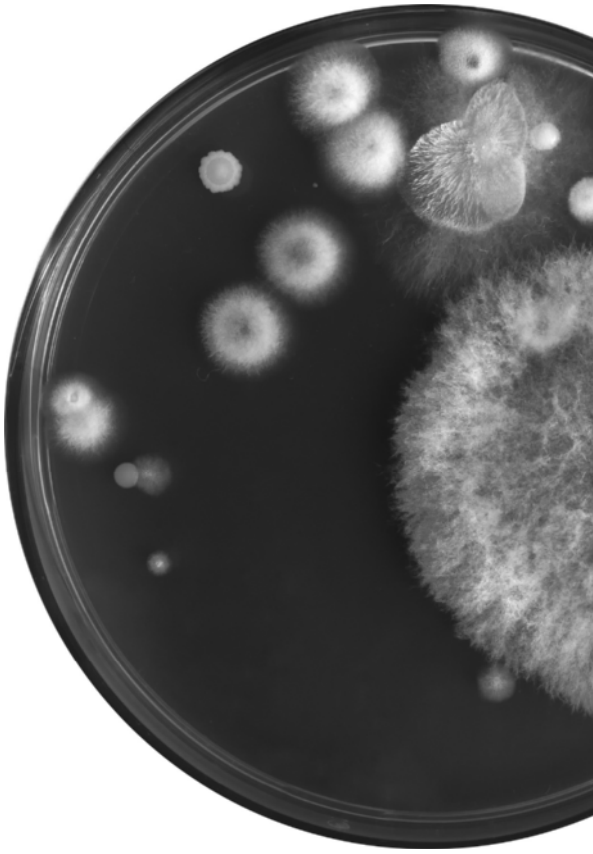
  During interviews with traders of a global significant bank during a supervisory assessment, a trader talked about the messages he got from his management. He stated '*The only thing management communicated were the numbers: how well did we do these months. That was it. The only thing that counts is our P&L: profit*'.

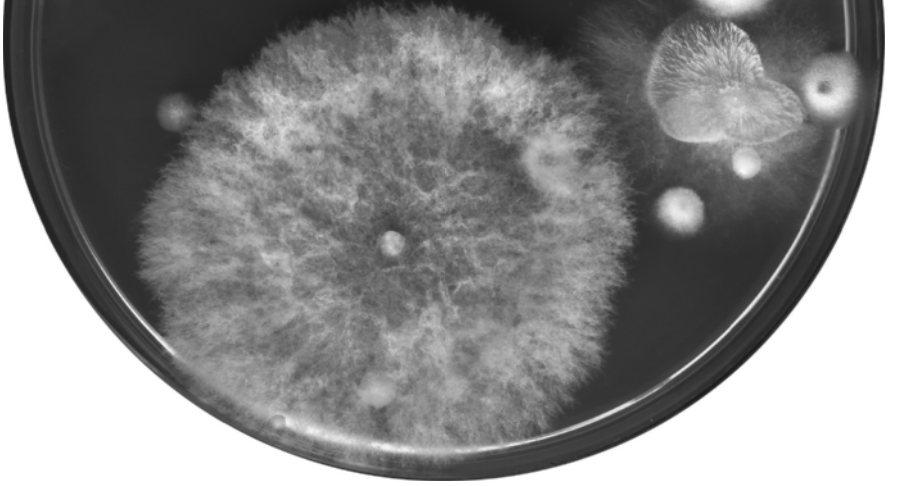
This management push on revenue leads traders to perceive that the goal of making financial profit (the 'what'), is more important than the way to make this profit (the 'how'). In the period of fast expanding businesses, the instruction was to get there quickly ("*And who gets the business set up first, gets to run it", Nr. 4, see Table 2.1*), but there was little leadership on how to get there.

The push on profit was strengthened by the incentive compensation system that was common in these banking divisions. This is a third relevant aspect in the legacy of trading businesses: the high proportion of variable (vs. fixed) pay, that was connected to revenue. The more profit you made as a trader, the more you got paid. It is not hard to see that this single focus on profit has an undermining effect on ethical behaviour. If making as much profit as you can is the only goal of importance, this provokes people to transcend ethical boundaries. In the perception of traders, profit and ethics could be contradictory. An example from supervisory practice of the trader that stated "*Culture or profit: what do they want from me*" (Nr. 11, see Table 2.1), illustrates this. Also, the quote of Adoboli at the start of this book suggests this perception: "*others did in fact know, and actively encouraged his behaviour for more than two years as long as it was profitable*". So, the push on profit evokes unethical behaviour by itself. And, although the banking industry acknowledges that misconduct can relate to a motivation of individual gain, it disregards the link between this motivation to gain individually and the organizational context and culture. The motivation to gain, causing a trader to behave unethically, is seen as an individual motivation and not as a result of a social context that values profit as a measure of success.

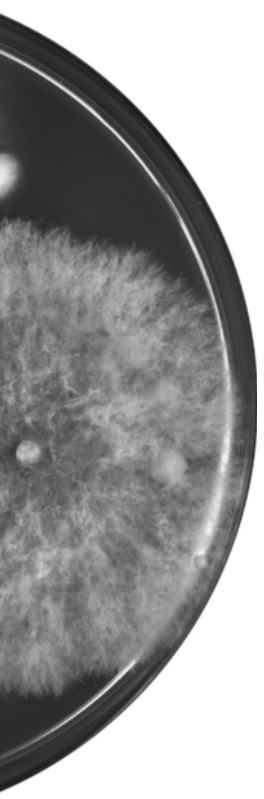
Moreover, since the 'how' to make profit is not addressed in interpersonal communications, neither is part of management instructions nor reflected in the targets that variable compensation is based on, the moral dimension of trading remains implicit. So, next to evoking unethical behaviour by itself, the push on profit results in a blind spot for the 'how' to make profit. This blind spot augments the development of a team climate of moral neglect, that is a contextual root cause for misconduct.

In sum, my choice to analyse contextual root causes of unethical behaviour within trading, is based on an increased risk of misconduct in the trading and markets business. As discussed, the legacy of fast expanding businesses and a push for revenue strengthened by a habit to incentivise financial performance with (high) variable compensation, creates an environment where transactions are likely to be valued over and above ethical considerations. Together with the size of transactions common in investment banking (compared to for instance the retail business of a bank), and the legacy of publically known misconduct cases leading to considerable losses and regulatory fines, I argue that trading within investment banking is a context that requires an effective approach to prevent misconduct. Furthermore, I argue that insight in team climate characteristics that can facilitate unethical behaviour adds value to preventive approaches that can be applied in a broader variety of organizational contexts. I therefore chose to focus my analysis on team climates at trading desks.





Part I
Misconduct



Chapter 3
Preventing misconduct: introducing a social psychological perspective

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Preventing misconduct: introducing a social psychological perspective

The recurring misconduct of traders within banking demonstrates that current responses of banks and financial supervisors are insufficiently effective in preventing future misconduct. Misconduct cases repeat over time at different banks. This implies that the lessons these cases bring forward, are not learned from effectively.

Taking into account the detrimental consequences of this misconduct for enduring financial performance, solidity of and trust in the banking sector, banks ought to do everything that they can to prevent future misconduct. Financial supervisors in their turn, ought to do all in their power to require of banks to effectively mitigate misconduct risk.

Limited causes and reactive response: the problem

The central problem, concerning the way banks and financial supervisors deal with misconduct cases, is twofold:

A. Banks, and financial supervisors alike, have a limited view on what causes misconduct (characterized by 'bad apple'- thinking), and

B. Banks, and financial supervisors alike, have a limited and mainly reactive response to misconduct; aimed at containment, disciplinary measures and decreasing opportunity for misconduct by the increase of controls.

Because of their limited view on causes, and reactive response, banks are insufficiently effective in preventing future misconduct, and financial supervisors are insufficiently effective in their requirement that banks should mitigate misconduct risk.

Root causes and preventive response: the answer to this problem

My analysis offers an answer to this central problem, that is again twofold:

A. I reveal social psychological root causes of misconduct (characterized by 'corrupting barrel'- thinking), and,

B. I offer a preventive response to misconduct, aimed at (1) defining team climate and identifying behavioural patterns that increase the risk of misconduct, and (2) improving these social psychological root causes accordingly to prevent future misconduct.

The central message my analysis conveys is that - by adopting this preventive response to misconduct - banks will be more effective in preventing future misconduct, and financial supervisors will be more effective in their requirement of banks to mitigate misconduct risk. In section 3.1 and 3.2 of this chapter, I will clarify the central problem and the answer proposed.

1. Causes of misconduct: bad apples versus corrupting barrels

Banks, and financial supervisors alike, have a limited view on what causes misconduct (characterized by 'bad apple'- thinking). First, I clarify this banking perspective. Second, I introduce the social psychological root causes of misconduct (characterising 'corrupting barrel'-thinking). Finally, I conclude this section by identifying the reasons for adopting the social psychological perspective on root causes of misconduct, and the reasons for questioning the current banking perspective.

A. Bad apples: a banking perspective

In the banking sector, the conviction that misconduct cases are a result of individual misbehaviour prevails. This thinking, where the individual is solely to blame for his or her misconduct, is referred to as the 'bad apple theory' (Treviño & Nelson, 2007; Kish-Gephart et al, 2010). A trader behaving unethically is a bad apple, that needs to be punished and removed from the barrel of healthy apples before it spoils the bunch. Now, some misconduct cases seem to support this bad apple theory. The next examples fit the bad apple explanation of what causes misconduct.

- *An illustrative example from supervisory practice (Nr. 6, see Table 2.1)*

  A trader at a large systemic bank, was caught making huge deals with a single third party, increasing his P&L extensively. It was a pre-conceived set-up: the trader and the third party arranged this scheme before the trader started to work at this bank. The third party rewarded the trader for getting these great deals. Within a year after he was hired, the fraud was discovered by the bank and the trader was fired.

- *An illustrative example from supervisory practice (Nr. 1, see Table 2.1)*

  "*These guys want to rob my bank*", uttered a CEO of a global significant bank during a discussion of misconduct cases within his investment banking division. With 'these guys' this CEO referred to the traders who were involved in the misconduct cases that were subject of this supervisory meeting with him. He implied that the traders that behaved unethically, were motivated by the aim of gaining money and 'stealing' from the bank.

The executive board member of this systemic bank commented: "*There will always be bad apples*". In the executives' view misconduct cases like these will happen inevitably, because investment banking attracts people who are willing to behave unethically and illegally just to make money. In line with his remark, in supervisory interviews with executives and traders we hear statements such as "*It is an industry problem*", "*There will always be bad apples*" and "*This industry attracts this kind of people*". Attributing the cause of misconduct even to a whole industry, is also a way of not dealing with this misconduct. If this is truly an industry problem, it will be a reality for trading businesses anyway. This attitude calls into question whether preventing misconduct from traders is even feasible.

This reasoning also assumes that stable dispositions drive people's behaviours, impervious to any feedback they get from others. Personality is considered as a stable constitution and often seen as the only explanation and driver of behaviour in a professional context. Some even hypothesize that successful bankers move up to senior management positions when they are extremely aggressive and completely lack empathy – associated with psychopathic or deviant personalities[5].

- *An illustrative example from supervisory practice (Nr. 7, see Table 2.1)*

  During a supervisory interview with a CEO on the group dynamics within his management board, he discussed the ineffective behaviour of one of his executives. This behaviour included for instance the withdrawal from group discussions, and hostile communication. We asked the CEO why he did not address this detrimental behaviour, as the chair of the management board meetings. He stated: "*That is just the way he is*". He considered individual behaviour as reflecting stable differences in personality. 'One acts as one is'. In this line of thinking, talking about this behaviour, or giving feedback to someone who behaves inappropriately, has no use.

The 'bad apple' theory is also reinforced by media reports, targeting individual traders as principal wrongdoers. Mr. Iksil, the trader involved in the London Whale case (see Table 1) opposed the 'bad apple' thinking of the media in his public letter to the press[6]. "*Publicity surrounding the losses sustained by the CIO of JP Morgan typically refers to 'the London Whale' in terms that imply that one person was responsible for the trades at issue*," wrote Mr Iksil. "*In fact the losses suffered by the CIO were not the actions of one person acting in an unauthorized manner. My role was to execute a trading strategy that had been initiated, approved, mandated and monitored by the CIO's senior management*".

Investment banking and financial supervision are – logically so – sourced with employees with economic backgrounds. Professionals with these backgrounds often consider human behaviour from an economical perspective; assuming all behaviour to be a result of conscious thoughts and explicit decisions. How a person acts, or what he chooses, is sees as an outcome of a 'calculation' of information and experiences. In this perspective, individual behaviour is the outcome of an explicit cost-benefit analysis, resulting in a rational choice to act. The benefits are the rewards (like money) every individual wants to maximize: the key assumption is that human nature is to primarily serve one's self-interest. The cost of misbehaviour is determined by for instance the chance of getting caught and the severity of the (financial) sanctions. This perspective on human

[5] The Guardian: September 20, 2015. 'How psychopaths can save your life'. Available at: http://www.theguardian.com/lifeandstyle/2015/sep/20/how-psychopaths-can-save-your-life

[6] The Telegraph: February 23, 2016. 'JP Morgan's 'London Whale' trader breaks his silence'. Available at: http://www.telegraph.co.uk/business/2016/02/23/jp-morgans-london-whale-trader-breaks-his-silence/

behaviour is often referred to by the term 'homo economicus', introduced by Adam Smith in the 19th century (Coase, 1976). In essence, the homo economicus perspective relies on an understanding of rational processes at individual level, that leads to behaviour or decisions. This perspective does not acknowledge that rationality is bounded by limits in information, time and the capacity to process and weigh this information cognitively (Simon, 1982). It also tends to neglect effects of multiple other influences on decision making such as contextual or social influences. The homo economicus perspective therefore aligns with the bad apple theory regarding misconduct, and is a possible explanation for the fact that bad apple thinking prevails in investment banking and financial supervision.

B. Corrupting barrels: a social psychological perspective

The social psychological perspective on misconduct opposes the banking perspective and its bad apple thinking. This 'corrupting barrels' - perspective on misconduct of a trader, is that the professional context the trader is part of, harbours social psychological root causes of his or her misconduct. The traders that behave unethically, are socialised and work in a professional context that evokes or drives their misconduct. Rogue traders are not just bad apples spoiling the barrel. According to the social psychological perspective, it is likely that the barrel has contributed to corrupting these apples.

I propose to assess these root causes of unethical behaviour at team level. The characteristics of trading team climates can elicit problems and form root causes for misconduct of its members (Scholten & Ellemers, 2016). Before we focus on *which* social psychological root causes within teams are relevant for analysing and preventing misconduct, we first briefly touch upon the empirical evidence of groups and group norms influencing the individual behaviour of their members.

Our individual behaviour at work is influenced by our direct social context: the team we work in. This is in line with the general concept that groups and the norms within these groups influence the behavioural choices of their members. "*Although people often tend to consider themselves and others as unique individuals, there are many situations in which they think, feel, and act primarily as group members*" (Ellemers, 2012). This insight is at the core of social psychology, and the body of research that supports this insight has accumulated over decades (see for a review Ellemers, 2012; Haslam, Reicher & Platow, 2013). The group we belong to also affects our *ethical* behaviour (see for reviews on antecedents of ethical behaviour: O'Fallon and Butterfield, 2005; Tenbrunsel and Smith-Crowe, 2008). That is, the people in our direct social context in our professional environment – the team we are part of, our colleagues and manager – influence the norms we set for our ethical behaviour at work. Our direct social context affects our moral compass and our moral decisions (Moore and Gino, 2013; Tomasello and Vaish, 2013; Kish-Gephart *et al.*, 2010). For instance, our group members help to establish a standard for ethical behaviour through their actions and omissions. These actions and omissions provide information on the relevant social norm within a group. This social norm tells its members what (ethical) behaviour is expected in a certain context and is considered appropriate of inappropriate (Moore and

Gino, 2013). So, when analysing the root causes of unethical behaviour of traders from a social psychological perspective, the trading team should constitute the appropriate level of analysis and is an important source of information.

Complement the 'bad apples' perspective with the 'corrupting barrels' perspective

I propose to complement the bad apple perspective by addressing social psychological root causes of misconduct that may be contained at the team level (Scholten & Ellemers, 2016). As indicated above, an extensive body of research shows evidence for the 'corrupting barrels' or social psychological perspective. The scientific foundations of this perspective will be explored in the theoretical part of my analysis (part II: social psychological root causes of misconduct). For now, there are at least four drawbacks of the 'bad apple' perspective, that I will list below.

First, the bad apple hypothesis does not seem to be supported by the misconduct cases within banking, that are known to financial supervision. Clear 'bad apple' cases, such as cases where it is evident that a trader entered a team with malevolent intent and single-handedly committed fraud within a short period of time after entering the bank, are the exception. In most misconduct cases, like that of Adoboli, Kerviel or Iksil, it is not at all evident that a trader behaved unethically because of a faulty individual moral compass, a bad character or because he was lacking norms of right and wrong. However, the social psychological root causes of misconduct are up to now rarely analysed. The 'corrupting barrels' perspective, with a focus on detrimental influences of team climate and the direct work context, has the potential to contribute to the clarification of what aspects led up to the unethical behaviour.

Second, the 'bad apple' theory does not explain why, within the same investment banking division, certain trading teams have a history of misconduct while other teams do not. Some trading desks within a bank have repeatedly seen misconduct of its traders, while other trading teams stay out of trouble. Organizational factors, like the focus on short term gains or the absence of ethical codes, that have been cited as potential system-level causes of misconduct are unable to account for these differences at team level. The 'corrupting barrel' perspective has the potential to explain this variation. The fact that there are 'hot pockets' in terms of misconduct risk within investment banks, imply root causes at team level and failing team leadership.

Third, the bad apple perspective suggests that individual level behavioural change is unlikely. Individual traders can simply be classified as 'good' or 'bad apples'. Further, the notion that a bad apple has to be removed before it can spoil other apples that were good, does not take into account that an apple that was once bad can 'turn good' again. This suggests that the primary way to prevent misconduct is to keep bad apples from entering the organization, for instance by introducing integrity assessments in personnel recruitment procedures or to get rid of them after they are exposed. In contrast, the corrupting barrels perspective offers concrete levers at team level, that can be used to prevent future misconduct of currently employed traders.

Fourth, the bad apple perspective is misaligned with information that is available about toxic leadership and unethical work climates that affect individual workers. These come to the fore very clearly in the observations of a Dutch journalist who spent a number of years in the London City, interviewing professionals in finance (Luyendijk, 2015). His reports in The Guardian revealed the significant impact of group dynamics and work climates on decision making in banking. Similar observations, calling for the need to address and reform aspects of organizational culture, have been made by financial supervisors (European Banking Authority, 2016), and are even acknowledged by the banks themselves (Banking Standards Board, 2016; Group of 30, 2015; Financial Stability Board, 2014). The 'bad apple' perspective leaves organizational culture out of scope. This misalignment between the 'bad apple' banking perspective, and the societal notion of culture as a cause for misconduct, creates a sense of detachment and incomprehension that is detrimental for the trust of private and corporate clients, the general public and society as a whole in banking.

In sum: defining individual misbehaviour as the sole cause of misconduct is insufficiently effective. Even though a trader who covered up a loss or manipulated an interest rate is to be punished, there may be root causes in his direct social context at work that have caused this trader to misbehave. These causes have to be examined and taken into account in order to effectively prevent future misconduct.

2. Responding to misconduct: reactive versus preventive

The persistence of trader misconduct in investment banking suggests that current responses of banks and financial supervisors to known incidents are insufficiently effective in preventing future misconduct. First, we identify three standard responses that contribute to this state of affairs: containment attempts, disciplinary measures, and increasing controls.

Then, this section touches upon some preventive measures the banking industry is taking, next to its reactive responses. These preventive measures relate to changes in incentive compensation structure, introduction of integrity tests and banking oaths, all aimed at encouraging ethical behaviour and integrity. Why these preventive measures, while well- intended, are insufficiently effective in preventing future misconduct is explained below.

Subsequently, I will introduce the preventive response to misconduct based on social psychological theory. To be effective, this preventive response should consist of a two-step approach, aimed (a) at analyzing social psychological root causes of misconduct within a team, and (b) at targeting these root causes to prevent future misconduct. This section concludes with the argument for investment banks and financial supervisors to adopt a social psychological approach to help prevent future misconduct.

A. Reacting to misconduct: a banking perspective

The currently observed limited and mainly reactive response of investment banks and financial supervisors alike to misconduct, can be categorized into three main reactions:

a. Containment of the misconduct and a focus on damage control;

b. Taking disciplinary measures against the 'bad apples', i.e. specific traders involved;

c. Increasing controls aimed at mitigating opportunities for 'bad apples' to cross the line.

Below, these three reactive responses are explained in more detail.

Containment attempts

Attempts to control the damage of misconduct revelations often try to make the misconduct seem small and inconsequential. The severity of the misconduct is downplayed, so that public concern for its implications seems out of proportion. For instance, even though Jamie Dimon (CEO of JP Morgan) was praised for taking accountability later on, one of the first of Dimon's reactions to the 'London Whale' case (see Table 1) was to dismiss the stories as a 'complete tempest in a teapot'[7]. In this way, the serious and alarming nature of a misconduct case is downplayed.

The implications of misconduct are also mitigated by presenting these as isolated incidents, resulting from individual misbehaviour. The legal implications of organizational accountability form an obvious incentive to blame the individual trader or wrongdoer. As a senior lawyer of a global significant bank – with misconduct cases to deal with – indicated in a supervisory meeting: "*We cannot take any blame: that will not hold up in court if we want to get some of the money back*". However, this legal containment strategy precludes the examination of possible causes in the organizational context that may have led to or facilitated the individual misconduct.

Illustrative of framing misconduct as the result of individual misbehaviour, is an interview with Dutch lawyer Peter Wakkie[8]. Wakkie is a well-known and seasoned lawyer, who specialized in advising corporate firms on how to deal with fraud. He is often consulted as an expert fraud cases, also by the banking sector. In fact, he is also a supervisory board member of ABN/AMRO Bank, one of the globally significant banks based in the Netherlands. In an interview in a leading national newspaper, headlined: "Discovery of fraud? Do not say anything and make sure there is cash", Wakkie lists five explicit points of advice for firms on how to deal with fraud. One of his five recommendations is to 'not take any blame' for what happened. He takes the 2015 Volkswagen emission scandal as an example. Wakkie expresses his relief when he read a press release of Volkswagen, stating that is was just individual misbehaviour that caused all the turmoil. He said: "*That is really good, encapsulate the event. This put me at ease right away*"[9]. Accordingly, banks tend

[7] Financial Times, May 16, 2012. "How JPMorgan's storm in a teapot grew". Available at: http://www.ft.com/intl/cms/s/2/6197eb2a-9f64-11e1-8b84-00144feabdc0.html#axzz43NiUNHNN

[8] NRC Handelsblad, December 19, 2015. "'Fraude ontdekt? Zeg niks en zorg voor cash". Available at: http://www.nrc.nl/handelsblad/2015/12/19/fraude-ontdekt-zeg-niks-en-zorg-voor-cash-1569537

to share as little information as they can about misconduct cases as a damage containment strategy. A misconduct case is primarily seen as a legal liability, and for that reason, information tends to be shared on a 'need to know basis' only. It is understandable that banks prefer not to publicize misconduct cases to outside parties like financial supervisors or the media. However, withholding relevant information about past misconduct from others within the organization, prevents them from drawing important lessons.

- *An illustrative example from supervisory practice (Nr. 8, see Table 2.1)*
  A trader within a global investment banking division, explained in a supervisory meeting: "*I know something happened at the desk two rows away from me on the floor, since someone was suddenly missing and fired. I got 'you do not need to know' as an answer to my questions. Soon after we got a training from Compliance reminding us of some legislation and procedures, I could derive somewhat what might have happened*".

Disciplinary measures

Next to containment, a second reactive response of investment banks to misconduct, is to take disciplinary measures against the traders involved. The misconducting traders in the cases summed up in Table 1 were all fired from the banks that employed them, at the time of the misconduct. Firing the individuals involved in case of unethical behaviour is common. Senior management are prone to firing traders who were involved in misconduct cases.

- *An illustrative example from supervisory practice (Nr. 9, see Table 2.1)*
  "*Tell me their names, and I will fire them all*", uttered a CEO of a global significant bank during a discussion of misconduct cases within his investment banking division.

Another disciplinary measure that a bank can undertake, is to sue the traders involved in misconduct cases. With law suits, banks aim to hold the trader who behaved unethically accountable for the trading loss and the breach of regulation. Again, all traders involved in the cases listed in Table 1 were sued and sentenced to jail – except for Mr Iksil (the 'London whale') who was fined.

Finally, clawback and malus clauses are used by banks to control damage of misconduct. Clawback refers to recovering bonuses that were already paid out to the trader. Malus or holdback refers to revising or refusing payment that was agreed upon before, due to misconduct of the trader. The Prudential Regulation Authority (the UK's financial supervisory authority) is planning to ensure that malus and clawback can occur even after a trader has moved to another bank[10].

Increase of control

[9] In Dutch he stated: "Dat is heel goed, lekker inkapselen. Ik kreeg er gelijk een rustig gevoel van." See: http://www.nrc.nl/handelsblad/2015/12/19/fraude-ontdekt-zeg-niks-en-zorg-voor-cash-1569537

[10] The Financial Times, January 13, 2016. "Bank of England tightens bonus rules". http://www.ft.com/cms/s/0/709cab9e-b9e4-11e5-bf7e-8a339b6f2164.html#ixzz43TWExjEi

A third reactive response to misconduct by investment banks, is to increase controls. Control functions as risk management, compliance and audit are expanded with resources. Limits and control frameworks are tightened; risk appetite statements are made explicit. The political and regulatory context of banks encourage this response. Politicians and regulators are creating more rules, more laws, more guidelines and codes banks have to comply with. The assumption is: by rules and regulation – we can control how banks act, and therefore decrease misconduct cases that hurt our economy and our society. Regulatory push is on increase of controls, assuming the lack of controls create opportunity for a trader to behave unethically, and so an increase of controls decreases this opportunity. Of course, an increase of controls can also be a signal to traders on the extent to which banks take misconduct cases seriously, and on what behaviour is ethical or allowed for.

Why standard responses are insufficiently effective

Focusing on containment, disciplinary measures and increase of controls is not sufficient to prevent future misconduct. Considering cases as isolated incidents caused by specific individuals leaves organizational causes of these cases unexplored. Containing information as a form of damage control impairs the possibility to learn from past misconduct. This contributes to the repetition of known problems, and the accumulation of misconduct cases.

- *An illustrative example from supervisory practice (Nr. 10, see Table 2.1)*

  A senior compliance officer, at an investment banking division of a significant bank with multiple misconduct cases, indicated that none of these cases were used as 'learning materials' in Compliance training sessions for traders. Instead of their own cases, anonymized cases of other banks were used as illustrative training material.

Disciplinary measures too may not provide the optimal way to improve future behaviour. Legal and financial sanctions have a strong signaling function, as they clearly indicate that misconduct is not accepted. However, there also is a downside to such communications. For instance, the prospect of invoking severe disciplinary measures can prevent traders from voicing concerns about questionable business practices or makes them hide instead of reporting (beginning) misconduct of their teammates. Further, the imposition of (deterrence) sanctions generally undermines employee trust and reduces rule compliance (Mooijman *et al.*, 2015; Tenbrunsel & Messick, 1999).

Even though the increase of controls might have some preventive effects – in terms of decreasing opportunity for traders to behave unethically, and sending out a signal on what behaviour is risky – increasing controls alone is not enough. The same accounts for limiting geographical distance. Whilst geographical distance provides a challenge for effective oversight and controls of behaviours, it does not predict misconduct (i.e. there are also teams geographically distant from a Bank's head office that show excellent ethical conduct). Unethical behaviour is not solely determined by opportunity to behave poorly. Opportunity is about circumstance, not

about what actually drives unethical behaviour. However, the increase in controls by banks is in line with the regulatory increase and demands of financial supervision. The political environment pushes this development as well. All these rules, regulations and controls might contribute to a (short-term) decrease of misconduct, but are insufficiently effective by themselves to sustainably prevent unethical behaviour.

In sum, current responses to misconduct tend to be suboptimal, and can even be counterproductive. Yet containment, disciplinary and control strategies characterize the way banks deal with misconduct, and reflect the demands of regulators, supervisors, and politicians.

First attempts to prevent future misconduct

Next to the three-way reactive response to misconduct outlined above, banks do undertake some preventive measures with the aim to prevent future misconduct. First, many banks alter their incentive compensation (often the balance between fixed and variable income) and performance management systems, related to promotion and talent development. Next to qualitative targets and KPI's, qualitative and behavioural targets are added to performance assessments. These changes, some of which are enforced by regulators, aim to lower the motivation for taking excessive risks and relating success in these businesses solely to revenue.

A second preventive measure is the addition of integrity tests to recruitment and selection processes, to try and filter out 'bad apples' coming in. Additionally, in the Netherlands the banking employees are required to take a Bankers' oath[11]. The objective of this oath, that is binding in the Netherlands for all banking employees, is to affirm ethical standards that provide guidance for integrity and individual behaviour and is a legal basis for later measures against breaches of these guidelines. Finally, as a preventive measure many banks embark on a trajectory for culture change that amongst other things emphasises professional integrity. An example is the Culture change program of Deutsche Bank AG[12] or the code of conduct of JP Morgan Chase[13]. Pushing integrity as a corporate value, and promoting an organizational culture that fosters ethical behaviour, is often one or the aim of culture change programs like these.

Even if well-intended, these preventive measures are insufficiently effective in actually preventing misconduct. There are two main reasons why this is the case. First, the measures generally do not target team level mechanisms. As a result, the direct social context of employees is in these preventive measures often not addressed.

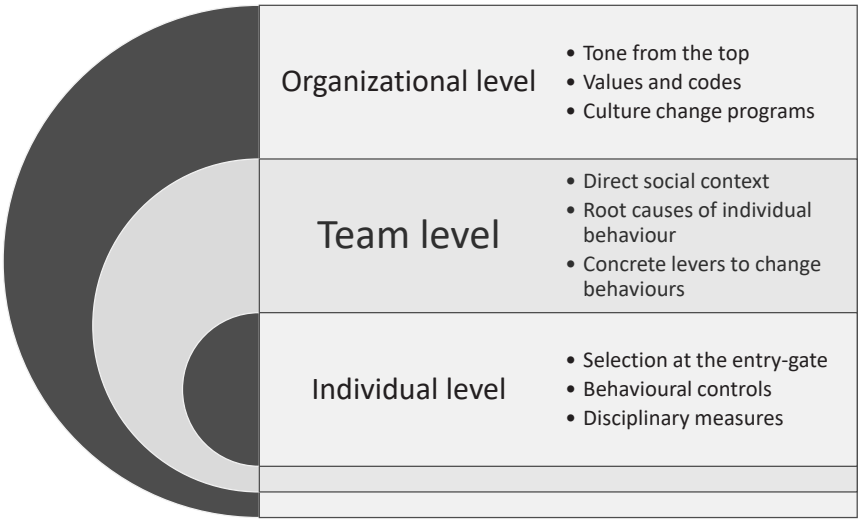
[11] See for the Dutch Bankers' oath, that all banking employees are obligated to since January 2016: www.bankierseed.nl or www.nvb.nl. For the Banking and Finance oath, see: www.thebfo.org.

[12] https://annualreport.deutsche-bank.com/2012/ar/deutschebankgroup/culture.html

[13] https://www.jpmorganchase.com/corporate/About-JPMC/document/FINAL-2014CodeofConduct.pdf

Changes in incentive compensation (such as a bonus cap) and performance management systems, integrity tests and a Banker's oath, all aim to impact the individual processes that underlie behaviour. Take for instance an integrity test: this instrument aims to test individual integrity outside the work context, and is not applied to groups of employees.
The teams these individuals work in are not sufficiently taken into account in these preventive measures. This is also the case for the culture change programs. These programs are often designed to change culture at organizational level. The explicit example given of the Deutsche Bank program, is a global program designed to change the culture of the whole bank (with its 98.000 employees, present in about 60 countries). Even if this is successful at an organizational level, it remains a challenge for banks of this size to translate their corporate values and culture change ambitions to their varied working floor contexts. This translation to working floor or team level is essential for achieving actual behavioural change on the working floor, and hence for the success of a culture change.

Figure 3.1. *Individual, team and organizational levels, ant their role in preventing misconduct by impacting behaviour and culture.*



The second reason for the insufficient effectiveness of the preventive measures banks take, is that these measures are often detached from the core business. For example, culture change programs often stay at a generic level (with a focus on corporate values), and are insufficiently translated to the business of for instance a trading desk, or the performance targets individual workers are supposed to meet. For instance, employees are introduced to the corporate values and expected to be aware of the culture the bank wants to see. If these values are not translated to concrete guidelines that relate to team level realities, it may be unclear for a trader what day to day behaviour within his task is expected. The objective of the culture change, the culture the change program aims for, usually is not explicitly connected to the strategy of the bank nor is

it clear how the pursuit of culture change relates to the core business of each team. A generic integrity test or Banker's oath are also not connected to the task of an individual employee after he or she is employed. These instruments are context-free, and often convey very generic and unified guidelines even though their implications can be very different for traders, retail bankers, secretaries and other employees.

- *An illustrative example from supervisory practice (Nr. 11, see Table 2.1).*

  A trader at a global significant bank uttered his confusion about the aim of the culture change program this bank was running. He wondered what was expected of him: "*Culture or profit*". In his perception, the behaviour that the culture program was promoting (like 'integrity') would also imply that he would make less profit. He thought 'good behaviour' also implies making less money. It was not clear to him how this culture change would profit the business goals. "*What do they want from me?*".

I argue for a preventive approach that does address culture at team level, and takes the business itself, the work task, into account. The next section presents this preventive approach, based on social psychological insights.

B. Preventing future misconduct: a social psychological perspective

Taking into account the contextual root causes of unethical behaviour will enhance the effectiveness of attempts to mitigate misconduct risk. Preventing future misconduct in this way requires that financial organizations and supervisors:

1. *Define* team climate: identify to what extent social psychological root causes may drive future misconduct within teams.
2. *Improve* team climate: target these social psychological root causes within teams.

This section gives a compressed introduction of the two-step approach that this social psychological research promotes. I will elaborate on this approach in further chapters: I will explore the scientific research that supports it, and report and discuss experiences and outcomes of the use of this two-step approach in financial supervision.

Step I. Define team climates

The first step of the preventive approach is to define team climates to identify to what extent social psychological root causes may drive future misconduct. These root causes of misconduct occur at team level, harboured in team climate. Let's say a Fx trading desk in the City of a certain investment bank consists of 7 traders, including a desk manager. Behavioural patterns of this team, of these 7 traders, and the climate within this team, influence ethical behaviour of the individual traders who are part of this team. This approach explicitly addresses team level of analysis, since a trading team is the most relevant day-to-day social context for a trader. As stated above, research clearly shows that our professional ethical behaviour and the moral decisions we

make at work are strongly influenced by the work teams in which we function: our colleagues and managers (Kish-Gephart *et al.*, 2010). For instance, other group members establish a concrete standard for ethical behaviour through their actions and omissions. These provide information on social norms of acceptable behaviour, and indicate what is considered ethical and appropriate in this group context (Moore and Gino, 2013). This is why I propose to analyse team level concerns and behaviours as root causes of unethical behaviour of traders. Although this first step of the preventive approach is an analysis at team level, there are contextual organizational factors that this model proposes to take into account while identifying root causes of misconduct. These contextual factors refer to the three organizational aspects discussed in Chapter 2: a history of strong and fast growth of the businesses, a history of revenue as the main organizational goal, and a history of high pay or incentive compensation. These contextual factors should be taken into account when assessing climate and social psychological mechanisms within trading teams.

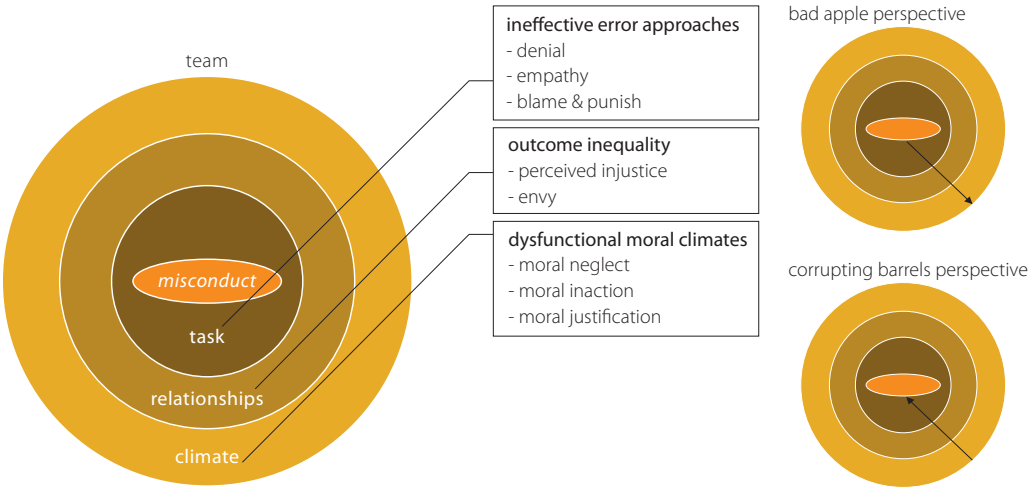
I present the 'Corrupting Barrels Model' to capture social psychological mechanisms that facilitate misconduct at team level (Scholten & Ellemers, 2016; see Figure 3.2). The title of the model – Corrupting barrels – refers to the teams that can harbour these root causes. As stated above, it is too simplistic to think of rogue traders only as bad apples spoiling the barrel. Applying a social psychological perspective clarifies that the barrel may also have corrupted these apples – and may do so again in the future. The model targets three core team characteristics that can contribute to misconduct addressing the way the team deals with its *task* (ineffective error approaches), interpersonal *relationships* within the team (outcome inequality), and the functionality of the team *climate* (dysfunctional moral climate):

1. *Ineffective error approaches (dealing with task)*
   The first category addresses the way errors are managed within the trading team. Errors refer to all kinds of unintended failure. Error management addresses patterns in how a team deals with failure that is related to the task its performing. Three ineffective error approaches are taken into account: denial, empathy and blame-and- punish. These ineffective error approaches within a team can contribute to unethical behaviour of its members. It therefore harbours possible social psychological root causes of misconduct. Chapter 8, paragraph 8.1., elaborates on ineffective error approaches and their contribution to the occurrence and persistence of unethical behaviour at work.

2. *Outcome inequality (interpersonal relationships)*
   The second category addresses the unequal relationships within a team. This inequality can be present in relationships between team members or co-workers, and in relationships with management. It can lead to emotional consequences, such as perceived injustice and envy. These emotional consequences of unequal relationships within a team can contribute to unethical behaviour of its members. It therefore harbours possible social psychological root causes of misconduct. Chapter 8, paragraph 8.2., elaborates on outcome inequality, and its contribution to the occurrence and persistence of unethical behaviour at work.

3. *Dysfunctional moral climate (team climate)*
   The third category addresses the moral climate within a team. Moral climate refers to the way the team deals with the moral dimension of its work. I address three aspects of moral climate: moral neglect, moral inaction and moral justification. The moral climate within a team can contribute to unethical behaviour of its members. It therefore harbours possible social psychological root causes of misconduct. Chapter 8, paragraph 8.3., elaborates on dysfunctional moral climates, and their contribution to the occurrence and persistence of unethical behaviour at work.

Figure 3.2. *The Corrupting Barrels model: social psychological root causes of misconduct at team level (Scholten & Ellemers, 2016).*



Step II. Improve team climates

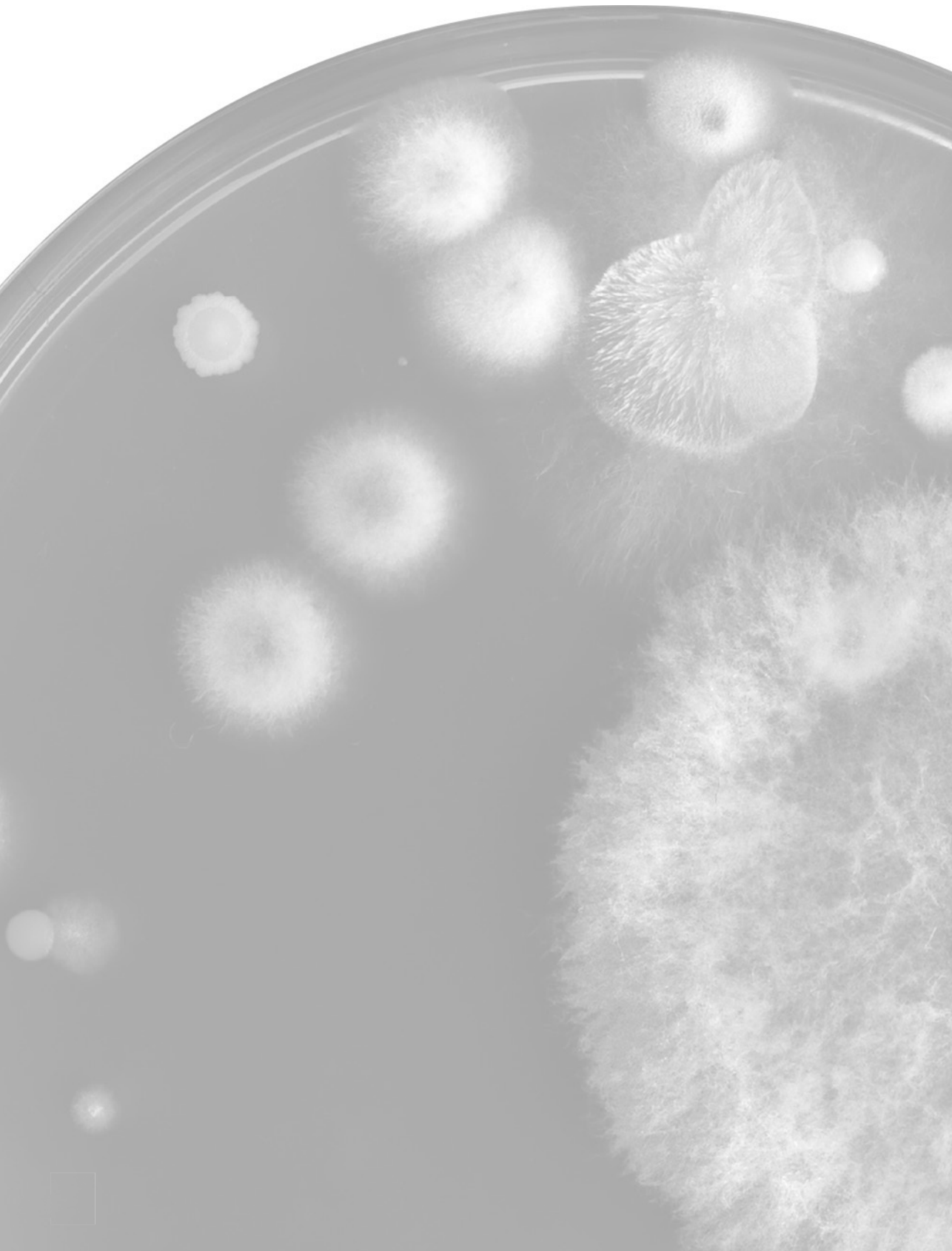
The second step of the preventive approach of misconduct, that this social psychological research promotes, is to target these social psychological root causes by improving team climate. Specific improvements to team climates that facilitate unethical behaviour are to adopt a more effective error approach to task performance, to adapt treatment of individual workers and improving the moral climate. Based on the outcome of the identification in the first step of the preventive approach, team climate and detrimental behavioural patterns can be improved, and consequently prevent misconduct happening in the future.

This second step of the preventive approach presented here implies a great opportunity that has as yet not been seized: targeting and changing the social psychological root causes of misconduct that lie within team climates. The Corrupting Barrels model can be used to identify team level root causes of misconduct. The good news is that these root causes can be targeted by business areas within the bank. Financial supervision can require of banks to do so. This research aims to reveal the adjustments banks can make within team climates, in order to prevent future misconduct.

Embark on preventing misconduct, in addition to reacting to misconduct cases

Banks ought to embark on the preventive approach of misconduct, in addition to the reactive measures they take to deal with misconduct cases. It is fair to say that the preventive approach that I promote here has downsides, compared to the reactive banking approach. There are valid reasons why this approach has been neglected so far. First, the preventive approach is not aligned with the professional background of the people within this sector. The analysis of social psychological root causes within trading teams requires social psychological expertise, that is underrepresented among professionals in the banking context. Second, the preventive response to misconduct is less visible to the public and to society. It does not entail a law suit that a bank can win, with media attention to show as a bank how strongly it opposes misconduct. The preventive approach requires a thorough analysis – although this analysis is not more time consuming than a law suit - and then a change of team climate and social psychological patterns that requires continuous attention and a long-term perspective. It does not offer a quick fix.

However, there is much to win in embarking on the preventive approach presented here. It is a simple truth that to truly prevent misconduct, deeper insight in what caused prior misconduct is needed. This preventive approach reveals what root causes of misconduct are present in the direct social context of traders, their trading team. Behaviour is rooted in team practices and climate. When we are able to pinpoint these practices, investment banks can use them to influence the behaviour of the traders part of these teams. By making adjustments in team procedures and other aspects of the teams these traders work in, their individual behaviour can be influenced and guided where necessary. This research aims to reveal these insights and hand investment banking useful leverage points to make cultural and behavioural changes in trading and sales business teams, in order to prevent future misconduct. The application of social psychological insights regarding unethical behaviour to trading teams, to this specific professional context, has not been made before and is therefore unexplored. Social and organizational psychology and the banking sector have been worlds apart. The current times ask for these worlds to meet.



Part II
Banking and supervisory practices

Chapter 4
Introduction Studies 1 and 2: research questions and data sources

Chapter 4
Introduction Studies 1 and 2: research questions and data sources

In this chapter I introduce two studies that I have conducted with the aim to examine current banking and supervisory practices. Below I introduce the research questions central to these two studies and the data sources that I have used to answer them.

1. Team climates add a valuable perspective

As I elaborated in Chapter 3, current banking and supervisory approaches to prevent misconduct seem to approach behaviour and culture mainly at individual and at organizational levels. Examples of the individual level approach to prevent misconduct are to increase controls of individuals when entering an organization (such as additional checks of antecedents during on-boarding procedures); to increase scrutiny of individual behaviours during their employment (such as controls of communications through email or chat); and to discipline individuals after inappropriate behaviours have occurred (such as to end their employment, fire them, apply clawbacks or other disciplinary measures), also as a deterrence to communicate to other employees that unethical behaviour does not stay without negative consequences. Some organizations 'select individuals at the entry gate' and invest in additional personality and trait assessments, e.g. integrity tests, during recruitment and selection procedure to prevent "rotten apples" to enter their organizations (Laurijssen & Sanders, 2016; Vries, de, 2016; Wisse *et al*., 2016). Examples of the organizational level approach to prevent misconduct are specifying corporate values, communicating ethical behavioural codes, modifying the tone at the top - using for instance fit and proper tests for exco and board members including integrity as an important aspect, introducing culture change and leadership programs, adapting performance management systems and expanding targets to include ethical behaviours. Attempts to change organizational culture, with integrity often as one of the key values, are made by adapting communications, rules and incentives.

These individual and organizational level approaches are valid. Some misconduct cases are clearly 'bad apple' cases, where there is for instance an intentional preconceived plan of a trader who seeks employment to commit fraud by dealing with a known third party that is in on this criminal plan. In these 'bad apple' cases discipline is needed and selection processes to prevent such occurrences are clearly useful. Indeed, to mitigate the risk of misconduct by bad apples, measures at individual level could be effective. Examples are the improvement of HR recruitment including personality and ethics testing, incentive systems and disciplinary measures. Also, recent contributions of organizational sciences show that measures at organizational level can be effective in changing organizational culture. Examples are extensive research on ethical culture (Treviño, *et al.*, 2014; Kaptein, 2008), and research how to analyse risk culture at organizational level effectively (Sheedy e*t al., in press*).

However, there are two main reasons why assessment of the team climate represents a perspective that can add substantially in the prevention of misconduct, next to individual and organizational level approaches. First, as elaborated in Part I, individual behaviour is strongly

influenced by the direct social context an individual feels part of or identifies with: the team(s) he or she belongs to (more so than the organization he or she belongs to). Collective norms in the team can overrule individual moral compasses. To understand why an individual behaved unethically, analysis of the team climate that formed the direct social and professional context of this individual is essential. Second, since team climate can facilitate unethical behaviour it is a value-adding perspective in preventing future unethical behaviour to impact and alter team climate. Who are the people that an individual wants to be included with and valued by? Who are the people that an individual depends on for day-to-day work activities and social relations? What are their norms and practices that can impact, reinforce, change, condone or correct individual behavioural preferences? Analyses at team level could identify underlying day to day processes on different levels of the organization: resulting in concrete levers to impact team climate and thereby mitigate misconduct risk.

My main message is that team level approach offers an additional valuable but often neglected perspective that can help prevent unethical behaviour. In Studies 1 and 2, reported in Chapters 5 and 6, I will examine to what extent analyses of behaviour or root causes of misconduct at team level are currently included in banking and supervisory practices. Besides individual and organizational level approaches in preventing misconduct, I argue that approaches at team level should be part of these practices to prevent misconduct effectively.

2. Research questions Studies 1 and 2

Because I focus on team climate as a value-adding perspective in preventing misconduct, Studies 1 and 2 focus on four research questions that assess the extent to which team climates are included in current banking and supervisory practices in preventing misconduct.

The first two research questions, addressed in Study 1, refer to the way banks deal with their own misconduct: are banks conducting and reporting team level analyses when exploring their own misconduct cases? Do they demonstrate in their own analyses that they are aware of root causes within teams of the unethical behaviours that their employees have shown? These research questions are addressed in Study 1, reported in Chapter 5.

Research questions Study 1, Chapter 5

1. *To what extent do banks consider team climate in their own reporting of misconduct cases?*
2. *To what extent do banks consider team climate in their analysis of a misconduct case?*

As a next step, external supervision can specifically ask of a bank to report on team level behaviours and culture patterns that led up to, explain or potentially caused their misconduct cases. Study 2 examines the way banks assess their own team climates, when explicitly requested to do so by financial supervision. These research questions are addressed in Chapter 6.

Research questions Study 2, Chapter 6

3. *To what extent are banks able to (re-)produce behavioural data, as indicators of team climate of teams with high misconduct risk, when requested to do so by supervision?*
4. *To what extent are banks able to conduct a root cause analysis of own misconduct cases with a team climate perspective, when requested to do so by supervision?*

3. Data sources Studies 1 and 2.

To examine the research questions in Study 1 and 2, four sources of supervisory data are used, see Table 4.1. These data sources have been gathered within the context of DNB's behaviour and culture supervision. The data presented reflect real practices that have been documented in the context of this supervision. The identity of the individuals and organizations involved remain anonymous and irretraceable in line with the confidential nature of supervisory information, and in accordance with DNB compliance regulations.

Table 4.1. *Studies 1 and 2: four research questions, and used data sources*

		Data sources			
		Study 1		Study 2	
Research questions		1. An annual litigation report	2. An internal investigation of a misconduct case	3. Behavioural data, delivered upon request	4. A root cause analysis, delivered upon request
1	To what extent do banks consider team climate in their own reporting of misconduct cases?	Ch. 5, § 5.1			
2	To what extent do banks consider team climate in their analysis of a misconduct case?		Ch. 5, § 5.2		
3	To what extent are banks able to (re-)produce behavioural data, as an indicator of team climate of teams with high misconduct risk, when requested to do so by supervision?			Ch. 6, § 6.1	
4	To what extent are banks able to conduct a root cause analysis of own misconduct cases with a team climate perspective, when requested to do so by supervision?				Ch. 6, § 6.2

The fact that the data is gathered in a supervisory context, and therefore are to remain anonymous and irretraceable, brings forth two main challenges. The first challenge is to show that the two banks from where the supervisory data was gathered are relevant and representative for the banking sector, without revealing their identity. The supervisory data presented in Studies 1 and 2 were gathered at two large banks: here referred to as banks A and B (the same banks A and B as referred to in Table 2.1, next to banks C and D). Both these banks are large significant, or 'too-big-too-fail' banks, with a total equity of more than 15 billion USD and more than 50.000 employees worldwide. Failure of a too-big-too-fail bank brings forth collateral damage to the financial system and the economy (Finel-Honigman & Sotelino, 2015). Governments therefore bail them out when necessary. They receive the highest supervisory intensity in European banking supervision. Both banks offer retail and wholesale services i.e. investment banking and trading

businesses. They serve international markets and have a global spread. Table 4.2 shows for each supervisory data source the bank it relates to.

Table 4.2. *Data sources for Studies 1 and 2, gathered in the context of DNB's supervision of behaviour and culture*

		Data sources			
		Study 1		Study 2	
Research questions		1. An annual litigation report	2. An internal investigation of a misconduct case	3. Behavioural data, delivered upon request	4. A root cause analysis, delivered upon request
1	Bank A	Ch. 5, § 5.1	Ch. 5, § 5.2		Ch. 6, § 6.2
2	Bank B			Ch. 6, § 6.1	

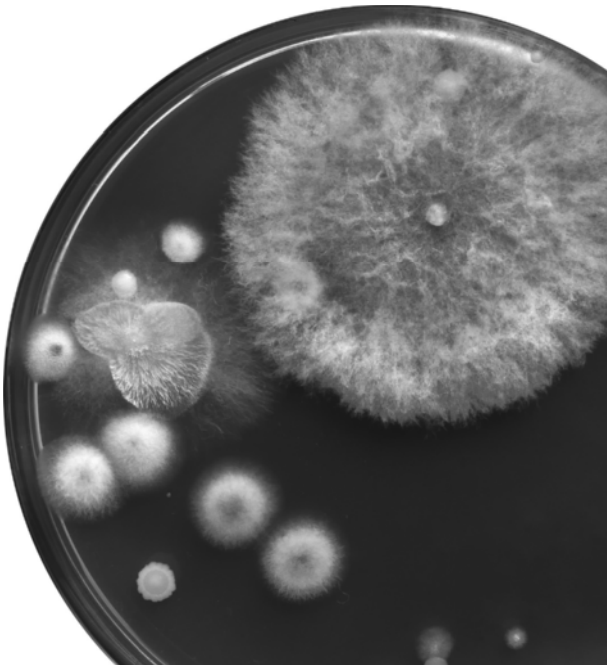
The second challenge of working with supervisory and therefore confidential data, is to archive the original data in a way that is accessible to the author and others who need to access the original data for verification purposes. While writing up this analysis, I left my role as a supervisor of behaviour and culture at the DNB and took up the role of Head of Audit Behavioural Risk within Group Internal Audit of RBS (United Kingdom, London based). Before leaving DNB at the first of November 2016, the original – non-anonymised – data were stored on the server of DNB in a separate protected folder. These data are not publicly accessible, although I and others who need to access the data for valid (scientific) reasons can do so after signing a confidentiality agreement.

Part II

Banking and supervisory practices

Chapter 5

Study 1. Current banking practices: teams are the blind spot



Chapter 5
Study 1. Current banking practices: teams are the blind spot

1. A banks' litigation report

Bank A produced a litigation report in the year 2015, that summarizes all misconduct cases that were known to the bank and defined as legal matters at that point in time. The litigation report was written by the bank's legal and control unit, and was meant to inform senior management on all current litigation cases and their status update. As part of a behaviour and culture supervisory assessment, the report was studied as desk research material.

1.1. Research question

The following research question was central to the analysis of the litigation report.

Research question

1. *To what extent do banks consider team climate in their own reporting of misconduct cases?*

1.2. Approach

To answer this research question, I read the litigation report thoroughly and analysed the quantitative and qualitative data the report offers. I focused on:
a. The root causes reported in analyzing the misconduct cases;
b. The response to the misconduct cases of bank A.

1.3. Results

General results

The litigation report states over 5000 legal matters known in 2015 within bank A – as explained in Chapter 4, a bank with more than 50.000 employees worldwide. Of those more than 5000 matters, 18 misconduct cases make up most of the legal risk bank A is facing at that point in time. The litigation report focuses for that reason on these 18 misconduct cases, of which 78% occurred within the investment banking division of the bank. The fact that most of the highest risk matters are concentrated within investment banking, is in line with the rationale underlying the focus of my analysis on trading businesses as elaborated on in Chapter 2.

Root causes

The litigation report lists 14 outcomes of the incident analysis bank A had conducted on its 18 misconduct cases. The list of 14 outcomes is provided in Table 5, in the exact order as reported by bank A in the litigation report.

A root cause analysis of misconduct cases generally aims to answer the question what caused the misconduct, or unethical behaviour that occurred. Study 1 aims to identify whether or how team level factors are taken into account by the bank itself as potential root causes of misbehaviour. Here I distinguish two levels of root causes of misconduct, illustrated in Figure 5.1:

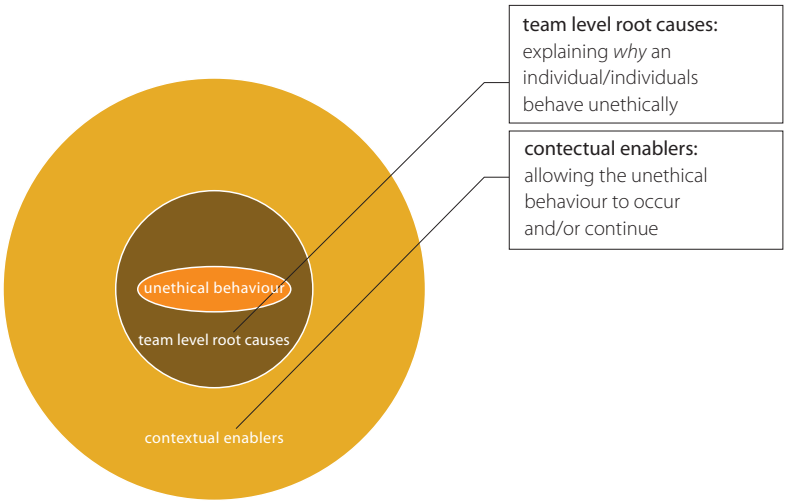
1. Level 1: why did an individual or multiple individuals behave unethically?

   This level of root causes explains what caused the individuals involved to behave unethically by considering a social psychological perspective. From this perspective team climate is a relevant context that may contribute to answering this question. Any root cause that refers to error climate indicators, indicators of negative emotional consequences of outcome inequality, or moral climate indicators thus may indicate that team climate may have influenced individual behaviour.

2. Level 2: what allowed the unethical behaviour to occur and/or to continue?

   This level of root causes refers to circumstances or context variables that gave the opportunity to behave unethically, and/or that allowed the unethical behaviour to continue. Contextual enablers at this level could relate to culture elements, such as a culture of not speaking up or a lack of clear guidance or oversight by local management. Other examples could be enablers that refer to failing controls, such as ineffective processes, systems or structures that are too complex to detect unethical behaviour in time or at all. These contextual enablers cannot explain what caused the misconduct, but can explain why the misconduct emerged and/or was not quickly addressed. Also, the presence of controls can be a guidance for employees, showing them what aspects of their work they should attend to or prioritize. Likewise, when breaching a norm leads to consequences, these consequences could be a deterrent to misconduct. Failure of controls could therefore be, next to an enabler, an indirect cause of misconduct.

Figure 5.1. *Two levels of root causes of misconduct*



When considering the 14 outcomes of the incident analysis listed in the report, three categories emerge. The first and largest category of outcomes (first green column of Table 5.1, corresponding with the red heart of Figure 5.1) do not consider root causes of misconduct in the sense as indicated above. This category contains 9 outcomes that only describe the actual misconduct itself. This majority of the outcomes of the incident analysis conducted by bank A thus describe what happened, detail the behaviour that was shown in the cases, but make no attempt to explain why this behaviour occurred (in the sense of the 'team level root causes' indicated in the middle ring of Figure 5.1) or *what allowed* the unethical behaviour to occur and/or continue (represented as 'contextual enablers' in the outer ring of Figure 5.1). Examples of outcomes or mere descriptions of unethical behaviour, are 'unprofessional communications in chat rooms and mail', 'misselling' and 'violations of embargoes'.

Table 5.1. *Outcomes of the analysis of relevant misconduct incidents, as reported in the litigation report of bank A*

Outcomes of the incident analysis in reported order	Classification		
	Unethical behaviour: description of the actual misconduct itself	**Contextual enablers**: allowing the unethical behaviour to occur and/or continue	**Team level root causes**: explaining why an individual / individuals behave unethically
	9 of 14 reported outcomes	*4 of 14 reported outcomes*	*1 of 14 reported outcomes*
1. Unprofessional communications in chatrooms and mail	X		
2. Improper benchmark submissions	X		
3. Improper inducements to obtain business	X		
4. Violations of embargoes	X		
5. Market manipulation	X		
6. Misselling	X		
7. Valuation issues	X		
8. Transaction lacking economic substance	X		
9. Tax driven transactions	X		
10. Conflict of interest			X
11. Insufficient risk disclosure		X	
12. Inadequate systems and controls		X	
13. Complex structure and insufficient controls		X	
14. Other: KnowYourClient issues, criminal conduct, antitrust violation...	(X)	X	

Next, the second largest category of outcomes of the incident analysis (second green column of Table 5.1, outer ring of Figure 5.1) indicate root causes at the contextual level. This category contains four contextual enablers that relate to the question of what allowed the misconduct to occur and/or continue. Examples in this category are 'inadequate systems and controls' and 'complex structure and insufficient controls'. 'Insufficient risk disclosure' refers to the extent to which the business where the misconduct occurred was reporting the risks the business was facing, and /or the extent to which the risk management, compliance and audit functions assessed the relevant risks. This risk assessment often determines the level and intensity of controls.

For outcome number 14 'Other', is an accumulation of analytical outcomes. Three relevant aspects of the incident are explicitly mentioned under 'other', namely: 'Know Your Client (KYC) issues', 'criminal conduct' and 'antitrust violations'. The last two– 'criminal conduct' and 'antitrust violations' - actually describe the misconduct itself - not what caused it. These can be classified in the first category of outcomes: descriptions of unethical behaviour. 'KYC issues' refer to issues related to the Know Your Client regulation banks have to consider when getting into business with new clients. The KYC regulations ask of a bank to know its clients and to know the origin of its capital. This prevents the bank from doing business with corrupt parties for instance. Failing to comply with 'KYC' regulation issues' can make way for clients and bank employees to behave unethically, this refers to a contextual enabler, and hence is classified in the third column of Table 5.1 (corresponding to the, outer ring of Figure 5.1).

Finally, and most importantly considering the research question: the third green column of Table 5.1 indicates mention of actual root causes at team level (indicated in the middle ring of Figure 5.1). Only 1 of the 14 outcomes of bank A's incident analysis, actually addresses such a root cause as a potential reason why an individual / individuals behaved unethically. The 'Conflict of interest' that is mentioned here could explain *why* an individual or individuals commit fraud. When an individual serves in different roles with conflicting stakes and interests, this can induce conflicting motives, lack of transparency and opportunistic decision making. This is the only incident analysis that can be classified as referring to a team level root cause.

In sum, the internal litigation report offers an account of different instances of fraudulent behaviour (9 out of 14 incident analyses), some ideas on what *allowed* this behaviour to occur and/or continue (4 out of 14 incident analyses), and very few ideas on what *actually caused* the unethical behaviour (1 out of 14 incident analyses). These numbers indicate that bank A does not systematically address the team climate, or culture at working floor level, in analysing potential causes of key misconduct cases.

While I categorized the 14 outcomes of the incident analysis into these three categories, the report does not refer to such a classification. The report does not distinguish between outcomes that explain why an individual behaved unethically, outcomes that explain what allowed the misconduct to occur or continue, and outcomes that merely offer a more concrete description of the unethical behaviour that was shown. In just listing 14 different analysis outcomes for the 18 incidents examined, the report shows little understanding of and exemplifies little need to understand what actually caused the unethical behaviour.

Finally, to learn why the misconduct occurred more insight is required about relevant day-to-day realities on the working floor where the misconduct took place. Any information on this working floor reality, the climate in the teams involved, during the period before the misconduct occurred is essential to determine the circumstances that led up to the incident that occurred. However such pre-incident information is completely missing from this report.

Response

The litigation report also lists five categories of responses to misconduct. These five response categories, or post-incident actions as the report titled them, are reproduced in Table 5.2. Unfortunately, it is not indicated in the report how many actions were taken per category.

Table 5.2. *Categories of post-incident actions*

	Categories of post-incident actions
1	Internal investigation
2	Remediation efforts (e.g. suspending business, systems and controls)
3	Disciplinary / employment measures (firing, suspending)
4	Regulatory interactions / antitrust and/or criminal investigations
5	Civil litigation

Only the first category of post-incident actions, internal investigations (category 1), is potentially (partly) aimed at revealing root causes within team climates. These internal investigations in principle have the potential to reveal social psychological mechanisms at team level, that facilitated unethical behaviour. Again, the post-incident action category of internal investigations is first in line in the reported list of post-incident action categories. This order as chosen by bank A suggests that internal investigation is a frequent response to misconduct and of the highest priority. The litigation report does not show how many of the 18 cases have been investigated internally. It therefore is possible that all cases have been investigated internally. However, bank A has disclosed the results of an internal investigation of only one of the 18 cases, next to the litigation report. This in-depth investigation aimed to identify the circumstances that led up to the misconduct happening. This specific internal investigation, of a single misconduct case, is further analysed in paragraph 2 of this Chapter. Bank A only disclosed one internal investigation to the supervisory team of behaviour and culture, which was offered as the best example of an internal investigation that explores the root causes for the misconduct broadly, including culture related aspects.

Four out of five categories of post-incident actions, are in line with the three-way common banking response to misconduct as described in Chapter 3:

a. Containment of the misconduct and a focus on damage control: categories 4 and 5.

b. Taking disciplinary measures against the 'bad apples', the traders involved: category 3.

c. Increasing controls aimed at decreasing the opportunity for 'bad apples' to cross the line: category 2.

These actions reveal that bank A aims at *containment* of the misconduct and its financial, legal or reputational consequences. Examples are the post-incident actions relating to civil litigation (category 5), interaction with the regulator and criminal investigations (category 4). Containment of misconduct cases is aimed at damage control and closing cases. Second, disciplinary or employment measures as a response to misconduct (category 3) are listed by the litigation report. Clearly, these measures are often just and called for. When an employee behaves unethically and breaks the law doing so, a bank often inevitably ends his or her employment. However, when these disciplinary or employment measures are not combined with investigations into team climate and social psychological root causes of the unethical behaviour shown, this signifies a '*bad apple*' perspective and '*blame and punish' approach* of the bank. Third, the remediation efforts (category 2) of suspending the business after misconduct occurred in a particular business, and *increasing controls*, is aimed at decreasing the opportunity for individuals to behave unethically again.

Responses to misconduct focused on containment efforts, disciplinary measures and remediation efforts inhibit bank A's ability to learn from prior misconduct cases by analysing broader circumstances such as team climate. These post-incident actions do not reveal a concern for team level root causes of unethical behaviour shown in these cases. Even the supervisory team that was responsible for the root cause investigation of bank A's misconduct cases showed signs of containment. This is illustrated by their reluctance to be transparent about the litigation report as I will explain below. For me as a senior supervisor of behaviour and culture, with the explicit temporary assignment to assess culture and misconduct related issues at bank A, it was hard to get access to the relevant information. My supervisory colleagues at the bank were hesitant about sharing information because of its 'sensitive' nature. I could only access information on a 'need to know basis', resulting in a need for me to make a strong case for analysing the litigation report and related information. After making this strong case, I was allowed by the supervisory team to study the report one day, at their premises. I was not allowed to receive a softcopy of the report through a secured email line, nor was I allowed to make a hard copy of the report. So, I made extensive notes and copied relevant information while I was there. One of the supervisors even got irritated and said: "*What kind of analysis would you like to see of bank A? How much would that analysis cost them?*". With his intonation, he made perfectly clear that he thought it was unrealistic to ask of a bank to do a root cause analysis at team climate level of their misconduct cases. Even if these misconduct cases were numerous and had potentially severe consequences.

1.4. Conclusions

Bank A does not consider the team climate perspective in its own analysis of misconduct cases. Hardly any incident analyses of and responses to misconduct as reported by bank A refer to actual root causes of misconduct at all. Team climate, although it can harbour social psychological root causes of unethical behaviour, is a blind spot for bank A.

The post-incident actions, or responses, of bank A to its misconduct might further explain this blind spot for team climate aspects facilitating misconduct. Bank A's responses to misconduct are mainly focused on *containment* efforts, *disciplinary measures* and *remediation* efforts. These responses inhibit bank A's ability to learn from its misconduct cases by analysing team climate and do not reveal team climate root causes of unethical behaviour shown in these cases. Even the supervisory team dedicated to supervise bank A showed signs of containment by making the report and related data nearly inaccessible to supervisory experts of behaviour and culture who were involved in supervising bank A's culture issues. This containment response impedes the potential of analysing the root causes of the misconduct cases in depth, and has therefore a detrimental impact on preventing future misconduct within investment banking of bank A.

To prevent misconduct is it essential that banks, and supervisors alike, analyse misconduct that has occurred in depth to see what *caused* the misconduct to occur (and adopt a team level perspective in doing so). Due to bank A's disclosure of an internal investigation of only one of the 18 cases included in the litigation report I cannot exclude the possibility that only 1 case of 18 highest risk matters that were addressed was investigated in depth by bank A. The next paragraph, 2, analyzes the minutes made during this investigation of a single case, to reveal whether and to what extent bank A did include the team climate perspective in this single case investigation.

2. A bank's internal investigation

Within its investment banking and trading activities, bank A discovered a misconduct case involving a fraudulent trading scheme with money laundering characteristics. Bank A investigated this misconduct case within its own investment banking division, by conducting an internal audit examination that included interviewing individuals involved. As part of a supervisory assessment of behaviour and culture, the interview minutes were analysed as the output of the bank's internal investigation.

2.1. Research question

The following research question was central to the analysis of the internal investigation report.

Research question

2. *To what extent do banks consider team climate in their analysis of a misconduct case?*

2.2. Approach

To answer this research question, the approach chosen is a careful analysis of bank A's internal investigation aimed at exploring the root causes of the misconduct case, conducted using 27 semi-structured interviews. To identify to what extent team climate was considered as a relevant root cause during the internal investigation of the misconduct case, the number of words used referring to or relating to team climate during the interviews was counted.

Specifically, for all 27 interview minutes, all words used by the interviewee or the interviewer in the following category were identified as relating to team climate:

a. All words related to the constructs identified in the 'Corrupting barrels' model, that is, anything related to *error management, outcome inequality and moral climate* at working floor level within the area where the misconduct had taken place, such as blame experiences leading to fear of repercussions, unequal treatment leading to perceived unfairness or envy and signs of moral neglect.

As the 'Corrupting barrels' model was not yet available at the time, it cannot be expected of internal audit of bank A to have used these specific constructs systematically in their investigation. Therefore, I used a broad definition of team climate references and all words used by the interviewee or the interviewer in the following categories were identified as relating to team climate as well.

b. Any words on *interactions* at working floor level within the area where the misconduct case had taken place; e.g. statements and perceptions related to exchange of information, consultations and agreements between individual employees or groups of employees such as between the business and control functions.

c. Any words on *leadership* that was exerted and perceived at working floor level within the area where the misconduct had taken place such as statements and perceptions related to actions, communications, omissions and mindsets of desk heads, middle and senior management.

Box 4 specifies the three classes of team climate indicators that were used during the analysis of the 27 interviews. If a question or an answer contained any words that could be categorised into one of the three categories mentioned, the whole paragraph was identified as 'relating to team climate' and included in the word count – even if the rest of the paragraph was not about team climate per se. By counting the number of words contained in whole paragraphs, and not restricting the count to specific words in sentences or counting separate words, the risk of false negatives (not identifying words on team climate, while during the interview these words were intended to relate to team climate) is mitigated. Because of unclear cut-off points of where the section or statements on team climate ended within a paragraph, whole paragraphs containing words on team climate were included. Therefore, the word count on team climate in my analysis is likely to be *overestimated*, or at least is giving bank A the best possible result in evaluating whether team climate was addresses in the internal investigation.

2.3. Results

Share on team climate

The analysis of the 27 interviews show that in the large majority (23 interviews), no more than 1/3 of the used words by interviewers and interviewees relate to team climate. That is, over

2/3rd of these 23 interviews do *not* address any aspect of behaviour and culture at working floor level that could harbour root causes for the unethical behaviour shown in the misconduct case. Instead, the words used in these interviews address for instance failure of procedures or support systems.

Table 8 shows the average proportion of text in interviews devoted to team climate is 17%. The other 83% of words addressed other aspects related to the misconduct, such as fact checking and failures of procedures or support systems.
82

Box 4. Team climate defined for analysis of bank A's internal investigation interviews
Any words that were used during the interviews – by interviewer or interviewee – referring to day-to- day business and working floor reality. Specifically, words addressing the following team level aspects that may harbour root causes of the unethical behaviour shown in the misconduct case:

1. 'Corrupting barrels' root causes, referring to: error management, outcome inequality, morality. Examples: blame experiences leading to fear of repercussions, unequal treatment leading to perceived unfairness or envy and signs of moral neglect. Examples:
- "Interviewee said she was very shocked as individual x had always appeared to be very nice, friendly and professional.." (answer)
- "However interviewee said that there had never been any previous signs of bad behaviour with individual x in terms of incidents reported to him either by Human Resources (HR), Regional Management or (Trading) Business Management." (answer)

2. Interactions between (groups of) employees. Examples: statements and perceptions related to exchange of information and relationships between individual employees or groups of employees, such as between the business and control functions. Examples:
- "Interviewee described department x as "listening but not helpful in closing gaps", for example leveraging best practices. Interviewee then went on to state that "they have good knowledge in internal policies, but were of no support." (answer)
- "Interviewee explained that she thought it was a good environment to work in and that everyone (in these other functions) had good professional relationships with each other.." (answer).
- "Were you ever made aware of tension between group x and other groups at that time?" (question)

3. Leadership aspects. Examples: statements and perceptions related to actions, communications, omissions and mindsets of desk heads, middle and senior management. Examples:
- "Interviewee also explained that he had an open door policy, though conceded it would have been easier for junior employees to approach him as he knew them better." (answer)

Box 5. Examples of questions and answers not related to team climate.

*Questions or answers related to **fact checking**:*

- "Are you familiar with [individual X] efforts to confirm with the bank the validity and purpose of certain transactions w.r.t. the [counterparty Y]?" (*question*)
- "What formal regular meetings did you have with [function B]?" (*question*)

*Questions or answers related to **procedures**:*

- "From what the interviewee has been told, the matter had not been escalated to individual A, but individual B also stated that if the matter could be handled by the team then there would have been no need in his opinion to escalate." (*answer*)

*Questions or answers related to **support systems**:*

- "Interviewee stated that even when sending a field enquiry within the bank the results were not always good (timely)." (*answer*)
- "The framework is defined from both a Regional and Functional perspective. Coupled with this, the interviewee stated that the bank's technology is widely recognized across the bank as poor." (*answer*)

***Table 5.3.** Proportion of text in interviews devoted to team climate*

% of text in interview devoted to team climate	No of interviews in this category
< 10 %	9
10-20 %	9
20-30 %	5
>30 %	4
Total average = 17%	**Total = 27 interviews**

Questions and answers

When broken down into questions asked by the interviewer and answers given by the interviewee, the interviews contain an average of 19 questions and 19 answers per interview. The analysis shows that on average only 2 out of these 19 questions (11%) relate to team climate. This means that on average 17 out of 19 questions (89%) do not relate to team climate, or any aspect of behaviour and culture at working floor level that could harbour root causes for the unethical behaviour shown in the misconduct case. Even though only 2 out of 19 questions on average ask about team climate, twice as many answers are given that relate to team climate. This suggest that even without prompting, interviewees spontaneously mentioned team climate aspects as potentially relevant to the incident analysis. Table 5.4 shows that in average 4 out of 19 answers given (21%) relate to team climate, or any aspect of behaviour and culture at working floor level that could harbour root causes for the unethical behaviour shown in the misconduct case.

Table 5.4. *Questions and answers on team climate*

	Average No per interview	Average No on team climate per interview
Questions	19	2 (11%)
Answers	19	4 (21%)

Follow-up questions

There are twice as many answers on team climate than questions on team climate. This suggests that interviewees volunteered this information because they thought it was relevant. It also raises concerns on to what extent the interviewers were asking follow-up questions on team climate when such information about team climate was volunteered. So, what if the interviewee answers a question by referring to team climate: would the interviewer ask follow-up questions to investigate this further? The results show that per interview, an average of four answers relate to team climate. Only 1 of those 4 answers, on average, was followed by a follow-up question on team climate, as demonstrated by Table 5.5. This means that on average, 3 out of 4 answers volunteering information about team climate per interview were not followed up by a question on team climate.

Table 5.5. *Follow-up questions on team climate*

When answer on team climate: follow-up question devoted to team climate?		
Average № answers on team climate	Average № answers on team climate – followed by a question on team climate	Average № answers on team climate – NOT followed by a question on team climate
4	1 (25%)	3 (75%)

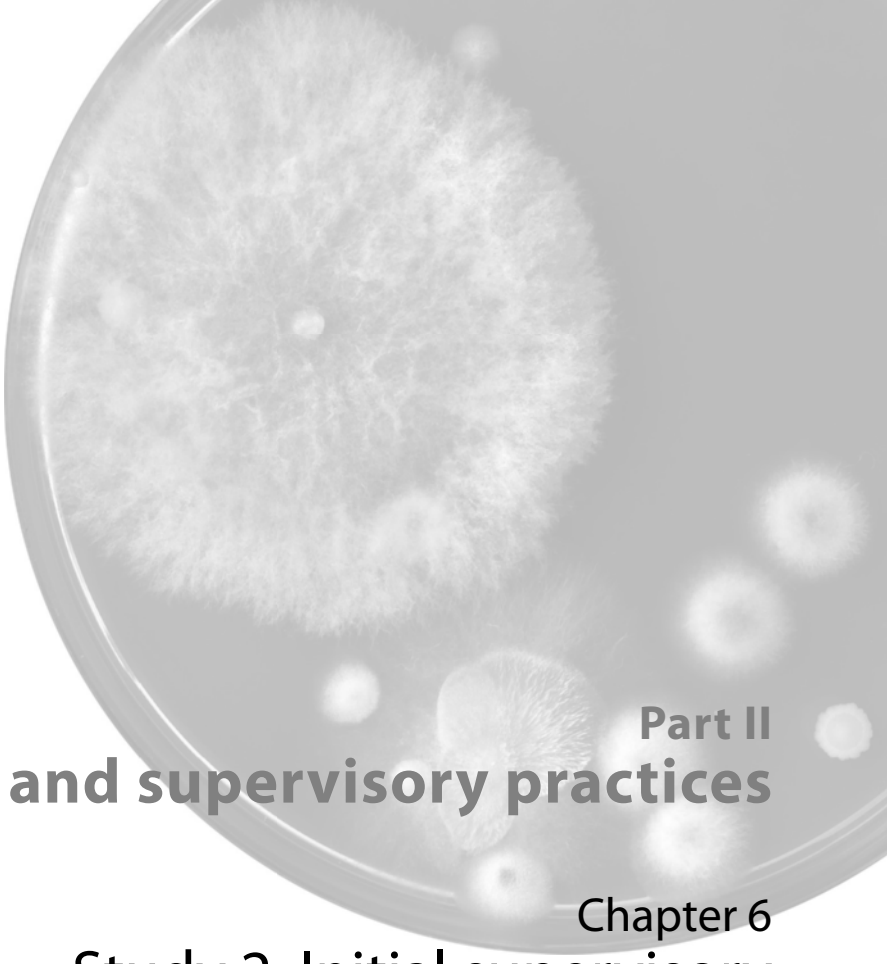
2.4. Conclusions

Bank A is missing the team climate perspective in its own analysis of a misconduct case. Hardly any questions (2 out of 19 questions on average per interview) are asked on team climate aspects that might have facilitated the unethical behaviour shown in the misconduct case. On top of that, when an interviewee answers a question by spontaneously referring to team climate, hardly any follow-up questions on team climate are asked (1 out of 4 answers is followed-up on average per interview). This internal investigation suggests that team climate, harbouring social psychological root causes of unethical behaviour, is a *blind spot* for bank A.

Bank A's employees who were interviewed during this internal investigation, the interviewees, did not refer to team climate as much as expected when analysing the root causes of a misconduct case. Hardly any answers (4 out of 19 answers) referred to team climate aspects that might have facilitated the unethical behaviour shown in the misconduct case. Of a large majority of the interviews (23 out of 27 interviews) only up to 1/3rd of the interview was in any way related to team climate or any culture aspects that could have harboured root causes of the misconduct case that was investigated. The average proportion of words used during the interviews addressing 'team climate' root causes of misconduct is 17%.

The other 83% of words addressed other aspects related to the misconduct, such as fact checking and failures of procedures or support systems. The 17% share is likely to be an overestimation rather than an underestimation, due to the inclusion of whole paragraphs to avoid false negatives.

Finally, there is some evidence that this internal investigation is the best example that bank A could demonstrate to the supervisor. As requested by bank A's team that had executed the internal investigation, there was a telephone call with the department head of the internal investigation team who was keen to hear the supervisory appraisal of the quality of the investigation. Although his objective was to learn from the supervisory feedback, he also expressed his pride of this internal investigation stating that it was their best attempt to include team climate aspects into the investigation.



Part II

Banking and supervisory practices

Chapter 6

Study 2. Initial supervisory requests: little effect

Chapter 6
Study 2. Initial supervisory requests: little effect

1. Requesting behavioural data

Within the investment banking division of bank B, the financial supervision of behaviour and culture assessed a trading business that faced high integrity risk. High integrity risk refers to the heightened inherent risk of integrity conduct rules breaches by the business. This inherent risk can for instance be rooted in the fact that the business is closing large transactions with clients from corruption prone countries. The high integrity risk for the trading business in question, was identified by the financial supervisor as well as by bank B itself and drives up the misconduct risk, that is, the risk of one or more traders of those desks embarking on some form of unethical behaviour. The trading business was therefore selected by the financial supervisor for an expertise assessment of behaviour and culture.

At the start of this supervisory assessment, the supervisors asked bank B for behavioural data – as an indicator of team climate - of the trading teams with high misconduct risk. It was clarified to the bank that the behavioural data could be any form of records, statistics or numbers on conduct or (signs of) unethical behaviour that would allow the supervisor to form a first impression of the team climates within the trading business of focus through desk research.

1.1. Research question

The following research question is addressed in this way:

Research question

3. *To what extent are banks able to (re-)produce behavioural data, as an indicator of team climate of teams with high misconduct risk, when requested to do so by supervision?*

1.2. Approach

The supervisory request for behavioural data was made in a variety of forms, at different points in time, to different people within bank B. Despite of this variety the nature of the request was always the same: asking for any behavioural data at team level of the specific trading business. Behavioural data was defined to consist of any records, statistics or numbers on conduct or (signs of) unethical behaviour, such as breaches of limits, near misses or incidents. The results in the next paragraph show how promptly and to what extent bank B delivered the behavioural data as requested for by the financial supervisor.

1.3. Results

Table 6.1 lists six (repeated) supervisory requests over a period of eleven weeks. Three modes of requesting the data were used by the supervisor: written in an email (twice), verbally during a telephone call (once), and verbally during meetings (three times) – to four different individuals / functions within the bank. Despite of the repeated supervisory request of behavioural data, to a

variety of functions and in a variety of ways, the request remained unanswered by bank B. That is, bank B did not demonstrate the ability to reproduce statistics, records or numbers of behaviours or conduct at team level in a timeframe of 11 weeks.

Table 6.1. Six requests of behavioural data by the supervisor

	Form	Who	Time	
	Written or verbal	To whom	№ of weekdays since last requests	Week
1	Written - email	Compliance officer, first point of contact for the assessment	-	1
2	Verbal - call	Head of Compliance	3	2
3	Verbal - meeting	Head of conduct team, responsible for conduct reviews	17	5
4	Verbal - meeting	Audit / regulatory affairs	0 (same day)	5
5	Written - email	Compliance officer, first point of contact for the assessment	1	5
6	Verbal - meeting	Compliance officer, first point of contact for the assessment	29	11

1.4. Conclusions

Bank B is unable to (re)produce data related to team climate - including records of breaches, near misses or incidents - of the teams within its high integrity risk trading business. Despite repeated requests by the supervisor, bank B showed to be unable to reproduce statistics or records on behaviour at these trading desks. They also did not specify what type of information they monitored for this purpose, even though they indicated that no incidents were reported. Behavioural data was broadly defined: bank B had the possibility to come up with any records, statistics or numbers on conduct or (signs of) unethical behaviour, such as breaches of limits, near misses or incidents. Despite the broad definition of data, and the acknowledged high integrity risk related to these specific trading desks, the request remained unanswered by the bank.

A second conclusion is that the supervisory request of behavioural data is ineffective. The request came from the financial supervisor, making it difficult and even against regulations for bank B to ignore. Furthermore, the supervisor uttered the requests to four different officers of different departments within the bank, in three different ways including verbally and in writing. This leaves no doubt that the request was received by bank B. And, the six requests were spread over a period of eleven weeks, giving bank B plenty of time to respond. Taken together, these observations make it reasonable to assume that requesting behavioural data of a bank as a financial supervisor will not result in further insight in team climates or the possible root causes of misconduct within these climates.

2. Requesting a root cause analysis

After assessing bank A's litigation report and its internal investigation of a misconduct case – as reported in Chapter 5 – supervisory experts of behaviour and culture requested of bank A to conduct a root cause analysis of its own misconduct cases. Bank A faced multiple misconduct cases, and would benefit from own insights regarding the root causes of these cases. Therefore the supervisor asked of bank A to conduct the root cause analysis itself. The objective of the root cause analysis, as discussed with the bank by the supervisor, was defined to analyse what root causes specifically in behaviour and culture are underlying the misconduct cases. The supervisor asked of bank A to conduct this root cause analysis, with a team climate perspective. To clarify what was meant by a team climate perspective, and to help and inspire bank A to analyse the root causes of its misconduct, financial supervision handed and explained to Bank A a description of the 'Corrupting barrels model'- as introduced in Chapter 3. Following this supervisory request, bank A conducted a root cause analysis on ten of its misconduct cases.

2.1. Research question

The following research question is answered in this paragraph:

Research question

4. *To what extent are banks able to conduct a root cause analysis of own misconduct cases with a team climate perspective, when requested to do so by supervision?*

2.2. Approach

To address the research question, the report of the root cause analysis on ten misconduct cases as conducted by bank A was analysed. To explore the misconduct reported, the number of observations and illustrative examples provided in the report were counted. Next, the culture patterns listed as root causes for the misconduct cases were analysed.

2.3. Results

Bank A starts off the root cause analysis report with the following two introductory statements:

a. "Examples presented are the illustrations of sporadic individual failures but do not constitute the suggestion of systemic issues across the bank."
b. "The behaviours displayed in presented examples are not accepted by the bank, and have resulted (where appropriate) in severe personal consequences for the individuals involved."

Statement a. clarifies that bank A regards the misconduct cases as individual misconduct incidents, that are not related to any organizational root causes. This legal disclaimer is aligned with the 'bad apple paradigm' that explains misconduct as unethical behaviour of single bad apples (the fraudulent traders), within a sound barrel (the organizational context). By opening the report with this disclaimer, Bank A shows to view the cases as individual incidents, and does not perceive or suspect patterns in the incidents or their root causes. Statement b. emphasizes that

bank A distances itself from the unethical behaviour displayed in the presented cases. It stresses that bank A has taken disciplinary measures regarding the individuals involved. This is aligned with the common response of the banking industry to misconduct that is, next to containment and strengthening control environments, focused on disciplinary measures and consequence management, instead of adopting a learning orientation (see Chapter 2).

The introductory statements are followed by a summary of 41 behavioural observations and 24 illustrative behavioural examples, summed up in Table 6.2, as detected by bank A in the (only) ten misconduct cases analysed. Thus, despite the in total 65 behavioural observations and examples observed in 10 cases, bank A claims that these are 'sporadic individual failures' and that these observations and examples do not suggest any 'systemic issue across the bank'. The report does not show any true exploration of root causes related to culture or team climate.

Table 6.2. *Culture patterns in 10 misconduct cases as defined by bank A*

	Culture patterns in 10 misconduct cases as defined by bank A	Number of observations from misconduct cases provided	Number of illustrative examples provided
1	Lack of awareness / conflict of interest	7	3
2	Roles & responsibilities / lack of supervision	8	5
3	Lack of disclosure / transparency	7	3
4	Missing courage / mentality to challenge	5	2
5	Inappropriate communication	4	5
6	Inappropriate actions	7	3
7	Excuses	3	3
	Total	41	24

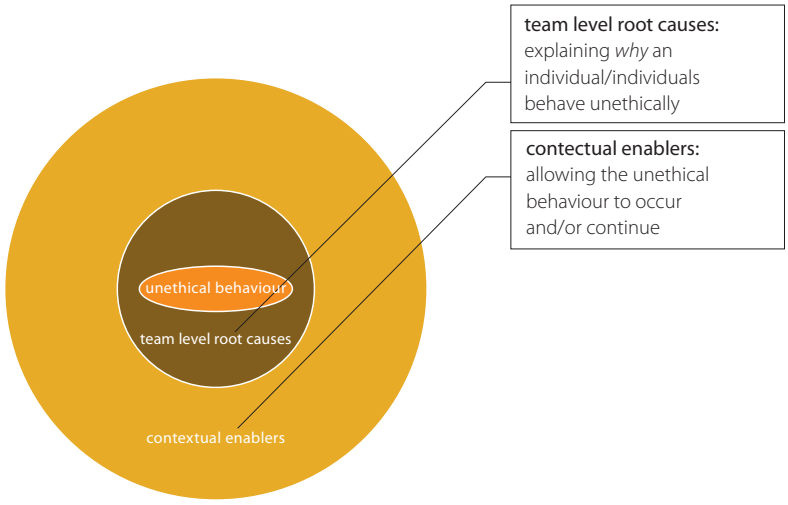
Table 6.2 also shows the seven 'culture patterns' identified in the report as root causes of the ten misconduct cases. I have related these culture patterns to the two levels of root causes in Figure 5.1 (repeated in Box 6). I categorized the culture patterns as provided by the report post-hoc: the report itself lacks an interpretation or further explanation of the seven culture patterns. The patterns are merely named and listed, not clarified. Therefore, my analysis and interpretation of the seven culture patterns is added in italics and between brackets, in the following paragraphs.

The first category of culture patterns describe the actual unethical behaviour displayed in the misconduct cases: inappropriate communications (pattern No 5: *inappropriate communication in chatrooms and through email, between employees and with third parties*) and inappropriate actions (pattern No 6: *inappropriate actions by employees, that breach conduct rules or regulations*). These two culture patterns (29% of all patterns) are not causing the misconduct, but merely describe the nature of the unethical behaviour that was demonstrated within the case. They are out of place in a list of root causes of misconduct. This category corresponds with the centre of the Figure displayed in Box 6: it details the unethical behaviour itself.

The second category of culture patterns is seeing to team level root causes of the misconduct cases. Two patterns out of seven (less than half, or 29% of all patterns) fall in to this category: lack of awareness / conflict of interest (pattern No 1: *low awareness on risk or rules around conflicts of interest*), and excuses (pattern No 7: *excuses: justifications of unethical practices*). These patterns indicate team climates that contributed to what caused the individuals involved to behave unethically. The patterns suggest team climates facilitating misconduct. This category of root causes corresponds with the inner ring or middle level of the Figure displayed in Box 6, and represent actual root causes of unethical behaviour at team level.

Finally, the third category contains three patterns out of seven (almost half, 43% of all patterns), identifying contextual enablers of the unethical behaviour: roles & responsibilities / lack of supervision (pattern No 2: *lack of oversight, possibly allowing the misconduct to occur*), missing courage / mentality to challenge (pattern No 4: *absence of challenge or voice behaviour, possibly allowing the misconduct to continue*) and lack of disclosure / transparency (pattern No 3: *absence of disclosure or speaking up, possibly allowing the misconduct to occur or continue*). These patterns refer to conditions or circumstances that contributed to the opportunity to behave unethically, and/or that allowed the unethical behaviour to continue. This category of root causes corresponds with the outer ring of the Figure displayed in Box 6: contextual enablers of unethical behaviour.

Box 6. Figure 5.1 *repeated: Two levels of root causes of misconduct*

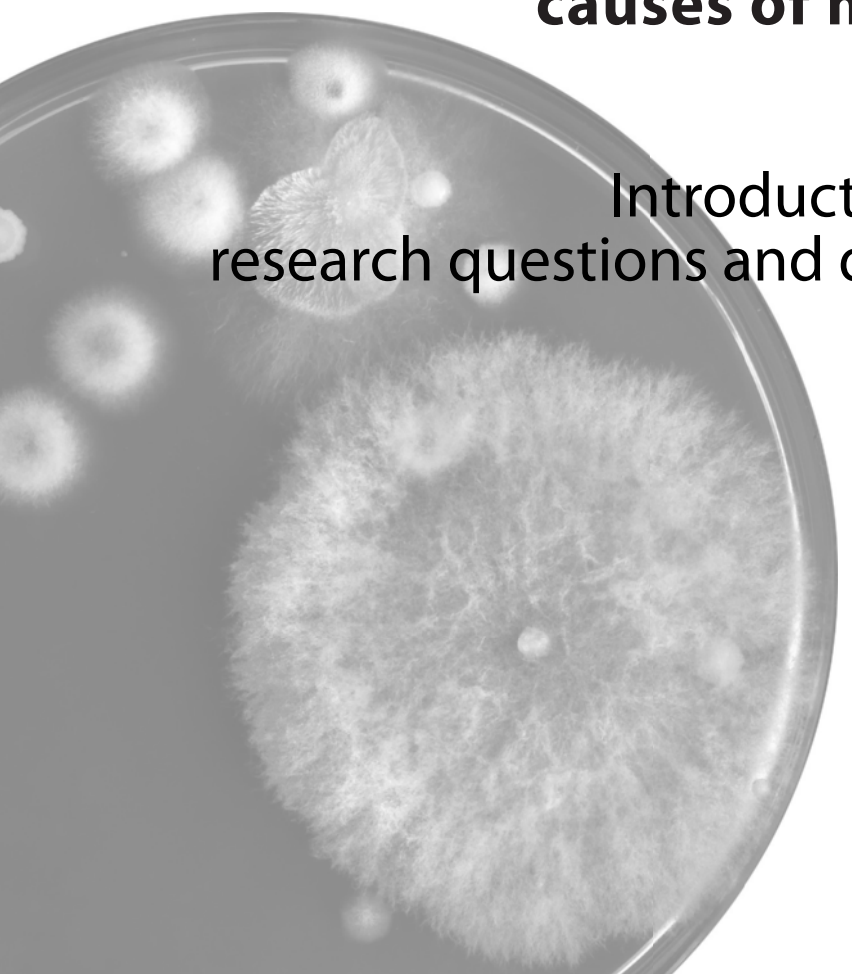


2.4. Conclusions

Bank A has conducted a root cause analysis of its misconduct cases, as an answer to an explicit supervisory request to consider team climate. Requiring this root cause analysis as a financial supervisor is insufficiently effective: less than half of the root causes considered actually address team climate (49%). The other half of the root causes considered by the bank's analysis, refer to organizational conditions allowing misconduct to occur ('contextual enablers', 29%) or further detail the actual misconduct itself ('unethical behaviour', 29%). Thus, the root causes analysis conducted by bank A provided the bank little insight in or deepened understanding of the way team climate facilitated unethical behaviours, needed to prevent future misconduct.

The conclusion that bank A has difficulty conducting a root cause analysis that addresses team climate, is based on three results. First, bank A upholds the 'bad apple perspective' by stating upfront in two legal disclaimers that there are no systemic issues, and that the cases are due to sporadic individual failures. This 'bad apple perspective' is incongruent with the large number of observations and illustrative examples listed in the report, and with the actual objective of conducting a root cause analysis from a team climate perspective. Stating that there are no systemic issues ahead of time, makes a root cause analysis on possible contextual and culture factors very difficult. Second, the seven culture patterns as identified by bank A lack a clarification or explicit interpretation. The patterns are named and listed, but not defined, explained or further analysed. Third, in my interpretation of these patterns, the identified root causes appear to be a mix of descriptions of actual unethical behaviours (i.e. inappropriate communications in chatrooms), organizational conditions that permit misconduct (i.e. lack of oversight), and potential root causes related to team climate (i.e. low risk awareness). This mix, and inconsistency in the patterns identified by the report as root causes, indicate little understanding by bank A of how team climate can facilitate misconduct.

Part III
Social psychological root causes of misconduct



Chapter 7
Introduction Study 3: research questions and data sources

Chapter 7
Introduction Study 3: research questions and data sources

In this chapter I introduce Study 3 that I have conducted with the aim to examine the way team climate can be assessed in banking and supervisory practices. Below I introduce the research questions central to this Study and the data sources that I have used to answer these research questions.

1. Assessing team climates

Whilst introducing Studies 1 and 2 in Chapter 4, I argued that team level approach offers a valuable but often neglected perspective that can help prevent unethical behaviour. Besides individual and organizational level approaches in preventing misconduct, I argue that approaches at team level should be part of banking and supervisory practices to prevent misconduct effectively.

In Study 1 and 2, reported in Chapters 5 and 6, I examined to what extent team climate analysis when examining root causes of misconduct is currently included in banking and supervisory practices. The results of these first two Studies showed that team climate, although it can harbour social psychological root causes of unethical behaviour, is a *blind spot* for banks when analysing their own misconduct cases. Furthermore, a supervisory request to conduct a root cause analysis of misconduct cases that considers team climate was insufficiently effective, since bank A had difficulty addressing team climate in its root cause analysis. The results of this root cause analysis did not deliver insights in root causes of misconduct at team level.

So, the results of Studies 1 and 2 give rise to the concern that banks are currently not able to assess root causes of misconduct at team level: either team climate is a *blind spot* in their analysis of misconduct, or when they are requested to include team level in their analysis by supervision, they experience difficulty in doing so. This is a concern since at team level concrete practices shape individual behavioural choices and business decisions (Ellemers, *et al.*, 2009; Steenbergen & Ellemers, 2009). The empirical aim of my analysis is to elucidate how this works, and how this knowledge can be used for preventing future misconduct by banks and financial supervisors. I therefore conducted a third Study, with the aim to assess the way team climates can be included in banking and financial supervisory practices.

2. Research questions Study 3

Study 3 addresses two research questions, addressed in Chapter 9, that assess the way root causes of misconduct within team climate can be identified by banks and supervisors.

Research questions Study 3, Chapter 9.

5. *Is it possible to identify the climate of a team and to characterize and compare teams within the same organization, based onkey aspects of a dysfunctional team climate that can facilitate unethical behaviour?*

6. *Is it possible to capture key aspects of a dysfunctional team climate that can facilitate unethical behaviour with a survey instrument?*

To answer these two research questions, I conducted an assessment of two trading teams. In Chapter 9, paragraph 9.1, I present the results of a deep dive assessment of these two trading teams aimed to answer the fifth research question. I conducted this deep dive using a combination of instruments namely, desk research, a team observation and confidential interviews (the methodology is described in more detail in paragraph 9.1.).

A deep dive based on 'fieldwork', including confidential interviews and team observations, requires dedicates resources and a significant amount of time. To spend these resources in a rational and focused way, an initial indication of relevant team climate characteristics and differences in team climates of different teams should guide the choice of where to conduct a deep dive such as reported in paragraph 9.1. I therefore developed and tested a survey to provide an initial indication of relevant team climate characteristics and pockets of risk (i.e. teams that show signals of dysfunctional team climates driving misconduct). I address research question 6 – that asks whether it is possible to capture key aspects of a dysfunctional team climate that can facilitate unethical behaviour with a survey instrument – in paragraph 9.2. Table 7.1 gives an overview of the two research questions addressed in Chapter 9, and the data sources used to answer these questions.

Table 7.1. *Study 3: two research questions, and used data sources*

		Data sources	
		Study 3	
Research questions		5. Assessment of two trading teams using a deep dive	6. Assessment of two trading teams using a survey
5	Is it possible to identify the climate of a team and to characterize and compare teams in the same organization, based on key aspects of a dysfunctional team climate that can facilitate unethical behaviour?	Ch. 9, § 9.1	
6	Is it possible to capture key aspects of a dysfunctional team climate that can facilitate unethical behaviour with a survey instrument?		Ch. 9, § 9.2

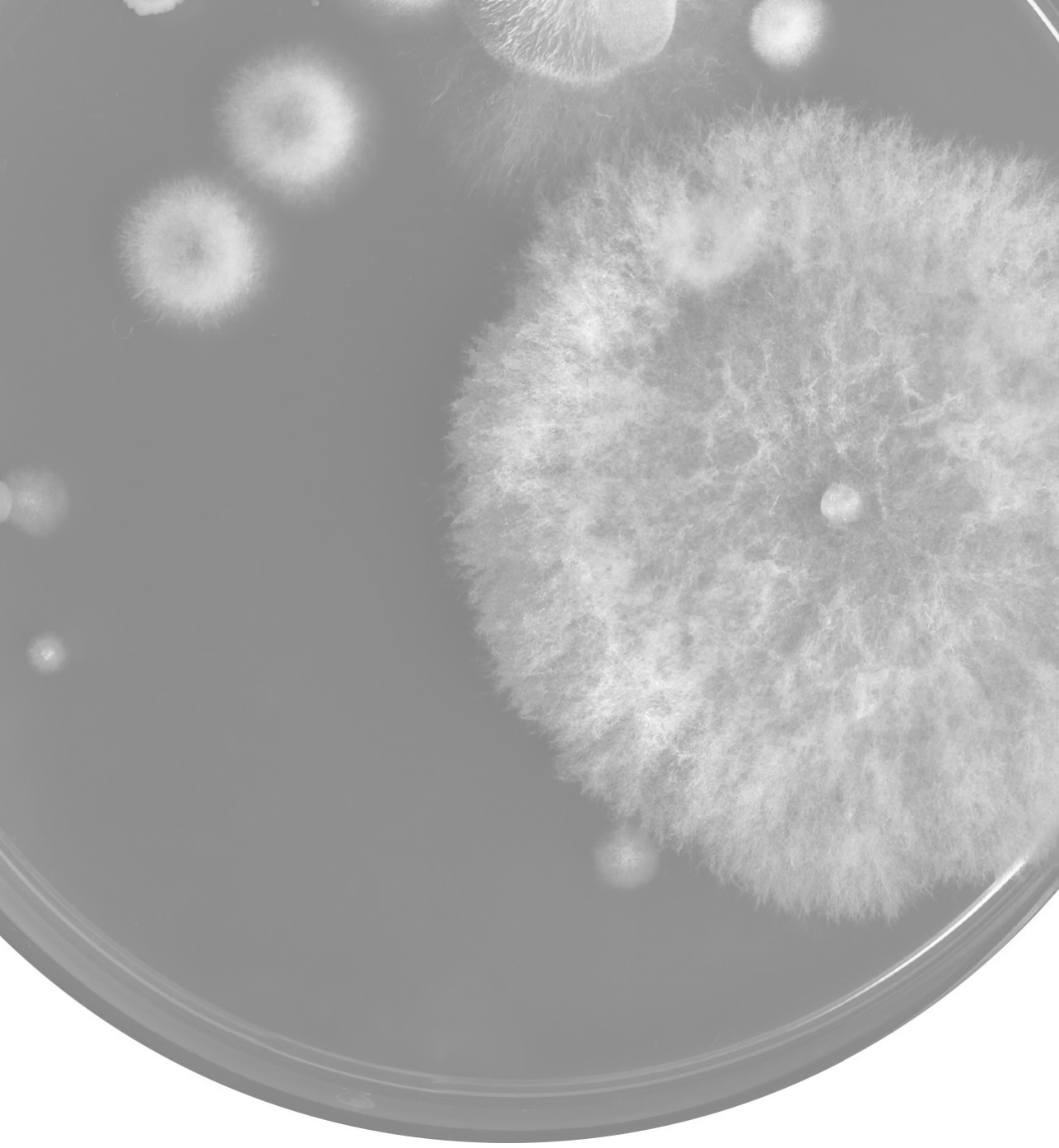
3. Data sources Study 3

The assessment of two trading teams in Study 3 was conducted within the context of DNB's behaviour and culture supervision. The data presented reflect real practices that have been documented in the context of this supervision. The identity of the individuals and organizations involved remain anonymous and irretraceable in line with the confidential nature of supervisory information, and in accordance with DNB compliance regulations. As elaborated in Chapter 4, when introducing the data sources of Studies 1 and 2, the data coming forth from the supervisory assessment is to remain anonymous and irretraceable. The supervisory data presented Study 3 is gathered at a large bank: here referred to as bank B. This is the same significant or 'too-big-too-fail' bank of which the behavioural data was gathered that I analysed in Study 2 (Chapter 6, paragraph 6.1). Table 7.2 shows for each supervisory data source used in all three studies, the bank it relates to.

Table 7.2. *Data sources for Studies 3, gathered in the context of DNB's supervision of behaviour and culture*

		Data sources					
		Study 1		Study 2		Study 3	
Research questions		1. An annual litigation report	2. An internal investigation of a misconduct case	3. Behavioural data, delivered upon request	4. A root cause analysis, delivered upon request	5. Assessment of two trading teams using a deep dive	6. Assessment of two trading teams using a survey
1	Bank A	Ch. 5, § 5.1	Ch. 5, § 5.2		Ch. 6, § 6.2		
2	Bank B			Ch. 6, § 6.1		Ch. 9, § 9.1	Ch. 9, § 9.2

The supervisory data related to Study 3 is confidential. The original data is archived in a way that is accessible to the author and others who need to access the original data for verification purposes. The original – non-anonymised – data is stored on the server of DNB in a separate protected folder. These data are not public accessible, although I and others who need to access the data for valid reasons can do so after signing a confidentiality agreement.



Part III
Social psychological root causes of misconduct

Chapter 8
Theory on team climates facilitating misconduct

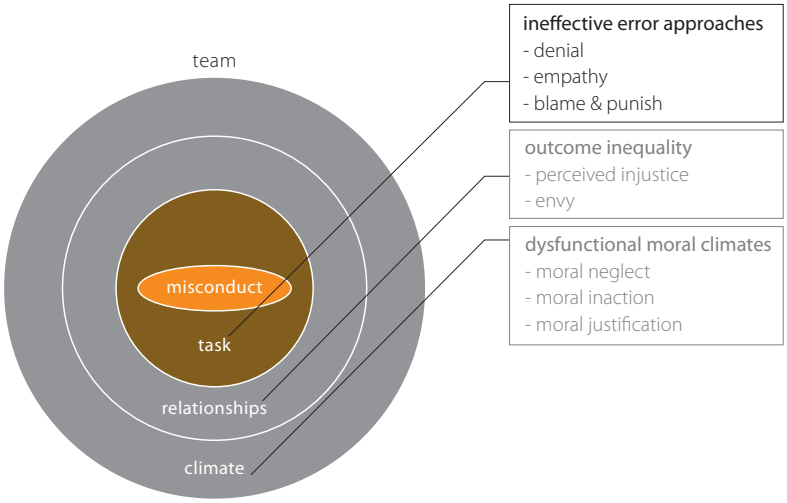
Chapter 8
Theory on team climates facilitating misconduct

In Study 3 I assessed two trading teams, using an assessment framework based on the Corrupting Barrels model (Figure 3.2, Chapter 3). Before I report Study 3, I elaborate on the underlying theory of the Corrupting Barrels framework. This underlying theory refers to three key social psychological mechanisms that may facilitate unethical behaviour within teams: ineffective error approaches (paragraph 8.1), outcome inequality (paragraph 8.2) and dysfunctional moral climates (paragraph 8.3).

1. Ineffective error approaches: denial, empathy and blame & punish

The way a team deals with task relevant errors may facilitate misconduct (see Figure 8.1).

Figure 8.1. *Ineffective error approaches at task level of team climates*



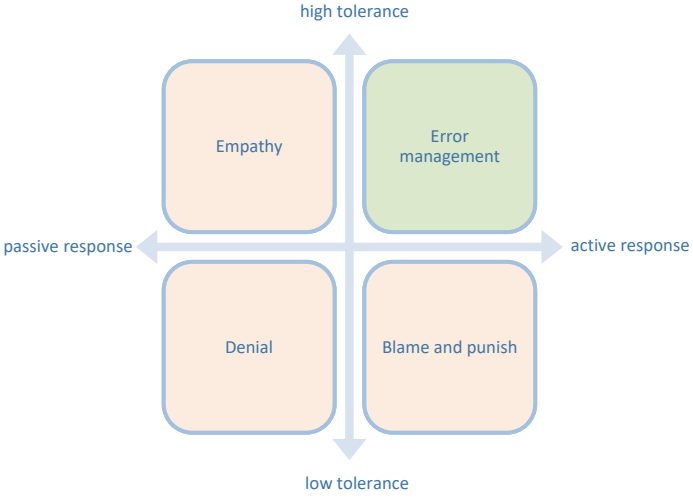
Errors refer to all kinds of unintended performance failures, ranging from experiments with novel procedures that have undesired outcomes, to severe mistakes (Van Dyck, Baer, Frese, and Sonnentag, 2005; Van Dyck, Van 't Hooft, De Gilder, and Liesveld, 2005, Frese, 1995). For instance in trading, errors may include investment decisions based on expected returns that turn out to be unrealistic, or accidentally using wrong numbers in important calculations. Errors occur whenever people are at work. They are by definition unintended and thus exclude intentional misbehavior. Thus, the occurrence of misconduct in itself should not be considered an example of erroneous behaviour. However, how a manager and teammates respond to errors, implicitly teaches traders how to deal with their task, how to act in ambiguous situations, and how management responds to problems. Moreover, the way such errors are typically dealt with determines the likelihood that employees are open about performance aspects they feel uncertain about, their willingness to discuss questions they have about behaviour of co-workers, and their ability to improve their work behaviours. So, when errors are managed ineffectively, this also creates conditions where the risk

of unethical behaviour more likely emerges and remains unchecked, even when observed by others. This chapter introduces three ineffective error approaches that have been identified in the social psychology literature and elucidates how these ineffective error approaches can facilitate misconduct.

1.1 Ineffective error approaches

Teams and organizations differ in how they approach errors. We distinguish between different approaches to errors, that can be organized along two orthogonal dimensions: the level of tolerance for errors, and the type of response. The combination of possible responses along these two dimensions thus characterizes four different organizational approaches that can be observed (Homsma, 2007; Van Dyck *et al.*, 2005). More systematic empirical evidence for these four organizational approaches to errors – see Figure 8.2 – has been obtained in prior research on organizational error handling in a variety of work settings. Homsma (2007), for example, uses these two dimensions in his analysis of organizational assumptions of errors: tolerance or errors and decisiveness towards errors. Van Dyck, *et al.* (2005) examined naturally occurring differences in error cultures in businesses with interview data. Results from these investigations allowed them to categorize organizational responses into four categories of approaches plotted in Figure 8.2: error aversion or denial (not tolerating errors and responding passively), empathy (tolerating errors and responding passively), blame and punish (not tolerating errors and responding actively) and error management culture (tolerating errors and responding actively).

Figure 8.2. *Four organizational approaches to errors (based on Homsma, 2007)*



Error management

Before three ineffective error approaches – denial, empathy and blame and punish – are introduced, first the most effective strategy is explained here. When people communicate openly about errors, are willing to reveal errors, when errors are quickly detected, analysed and corrected and knowledge on errors is shared in the organization, this is referred to as an "error management

culture" (Van Dyck *et al.*, 2005, Rybowiak *et al.*, 1999). The concepts of error management culture and error management climate are sometimes distinguished from each other in literature on error management. Whilst error management culture refers to organizational practices, error management climate refers to people's perceptions of these practices. In this analysis, I use the term error management culture to refer to organizational practices, but I assume these impact on employee perceptions.

The error management approach induces a learning orientation in employees. The error management approach accepts errors as an inevitable aspect of professional performance, where it is impossible to fully predict, prescribe or control every performance aspect (Rybowiak *et al.*, 1999). Errors are acknowledged, or 'tolerated', as something that is an inevitable part of professional life. However, this acceptance is contingent on the understanding that action is taken to redress any negative consequences, and that there is a clear ambition to learn from errors made. It requires an active response to errors by stimulating evaluation of errors and organizing means and practices to learn from them, so that ideally, the same error is not made twice. In this approach errors are primarily viewed as a chance for organizational development and improvement.

- *An illustrative example from supervisory practice (Nr. 12, see Table 2.1).*

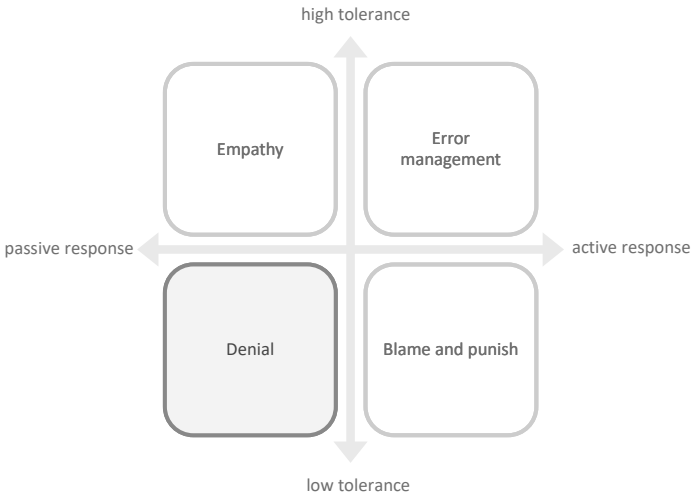
  An executive board of a too big to fail bank discovered an error of a senior manager and calls him up as soon as the error is discovered. The senior manager gets summoned up to the executive floor actively and immediately and is asked to report and explain what has happened. He is welcomed with an introduction from the executive board such as: 'We assume you have thought this over. Please explain to us your reasoning on these events'. The senior manager gets the chance to explain the situation to an executive board that takes him seriously and trusts him unless proven otherwise. This response to errors is evaluated positively by the senior manager. It stimulates him to openly and thoroughly evaluate the error together with the executive board, making full use of the learning potential an error has to offer.

This type of error management approach is negatively correlated with unethical behaviour (Van Dyck *et al.*, 2005): more error management leads to less unethical behaviour. Approaches to errors at work may fall short of this optimal form of error management in different ways, which can be ineffective in their own way (Homsma, 2007; Van Dyck *et al.*, 2005). Below, I explain three alternative approaches, and explain why these are less effective.

Denial

A first ineffective error approach assumes that current regulations and guidelines should fully prevent the occurrence of errors (no tolerance of errors). The denial that errors can and do occur, characterizes this error approach (see Figure 8.3). It does not acknowledge that errors are inevitable in professional life; errors are simply not tolerated or accepted. Therefore errors are not considered as a possibility and ignored when they occur.

Figure 8.3. Error approach 'Denial'



In this approach, due to the assumption that the possibility of errors has been ruled out (for instance by increased external supervision) no provision is made for the occasion when errors do occur. Errors made do not lead to organizational level changes (passive response). Silencing errors, implies that the circumstances leading up to their occurrence are not scrutinized, and therefore nothing is learned from them. As a result, nothing is done by the organization, by management, or by employees to learn from prior mistakes or failures. However, if there is a flaw in the system, or circumstances that were not anticipated in standard guidelines repeat themselves, similar errors may continue to occur time after time. Furthermore, this approach makes people avoid thinking about failure, and renders them unwilling to critically consider their work behaviours to search for improvement opportunities in work routines. It enhances tendencies to hide problems that occur, and to become defensive when work practices are challenged.

- *An illustrative example from supervisory practice (Nr. 13, see Table 2.1).*

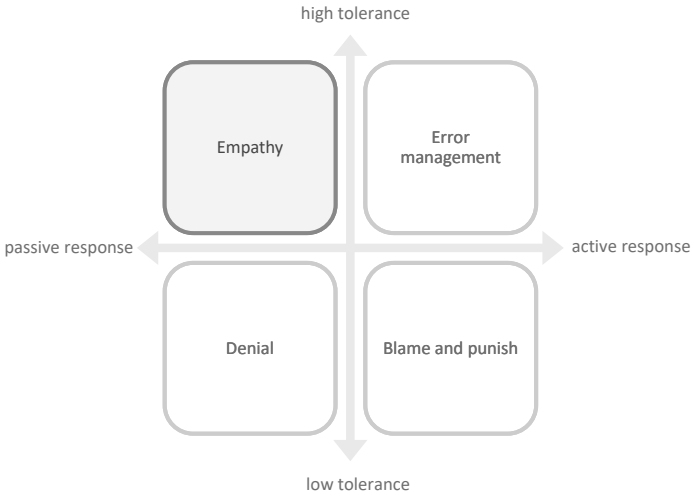
  An employee had a leading role in a project that failed. Apart from unforeseen circumstances, errors were made in this project by the employee and by other employees involved. Months after this happened, the employee received negative feedback on his performance from his superior, in the context of a performance review. Although he was aware that his performance in this project had been substandard, he was surprised that he received this feedback only then. The failure of the project was not explicitly evaluated and other causes of this failure, next to the errors the employee made, were not examined. Years later he feels that the errors he made in this project negatively affect his reputation, performance appraisal and career opportunities within the organization. Another employee of the same bank, a colleague, acknowledged this, when proffering his take on the failed project – in which he was not involved. He stated that he knows

this employee erred and that the failure of the project was apparently his fault. But what error exactly had been made by the employee responsible for the project, was unclear to this colleague. He indicated that there was no transparency about what happened on this project, and consequently, no one else had the chance to learn from what went wrong there. The colleague confirmed that the reputation of the employee was damaged, although the blame of the failed project on the employee stayed implicit. The colleague felt that everyone knows there were issues, but no one talked about it. As a result, the employee did not get the chance to clear his reputation and move on.

Empathy

A second ineffective approach towards errors is – again - a passive response, in combination with an acceptance of errors (see Figure 8.4). As in the former approach, nothing is done or organized to evaluate errors and learn from them. Contrary to the former approach, however, in this case the fact that mistakes can happen and failure occurs is accepted. In this approach, errors are tolerated and seen as an inevitable aspect of reality. There is sympathy for the ones who are involved in making the error. However, nobody acts to use these experiences of failure for the better.

Figure 8.4. *Error approach 'Empathy'*



Although there is some understanding for the fact that errors occur, the conditions leading up to undesired outcomes are not assessed for improvement opportunities. This induces employees to respond passively and makes them lax towards errors and other problems at work. As long as their shortcomings at work are simply accepted, and management does not signal these shortcomings, they are not particularly motivated to prevent work behaviours of themselves or others that may lead to problems later on or to help each other to do a better job. Their experience is that work routines are not changed or improved, even when errors are made (repeatedly).

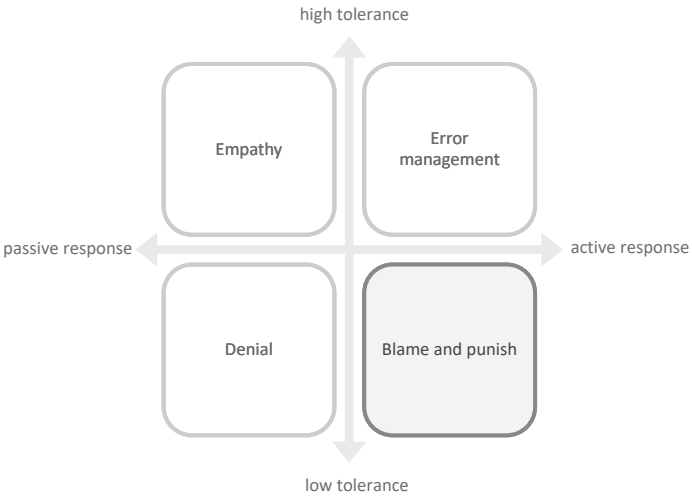
- *An illustrative example from supervisory practice (Nr. 7, see Table 2.1).*

  A chair of a management team in a bank was known for covering up detrimental social behaviour of team members. The underlying mindset of his reluctance to speak about this detrimental behaviour consisted of two assumptions. When asked about this, he explained that in his view giving feedback on behaviour was inappropriate. In his view, individuals have their own 'professional responsibility' in how they act. He did not think it was his place, as chair of this team, to say something about behaviour of individual employees, as he considered individual behaviour as reflecting stable differences in personality. "*That is just the way he is*". In this line of thinking, talking about this behaviour, or giving feedback to someone who behaves inappropriately, has no use. This chair of the management team did not believe that behaviour in a professional context could change. He accepted the occurrence of errors as a part of professional reality and made no effort to change either the individual or the situation to prevent future errors. This example might seem an exceptional case of incompetent leadership. Yet, this was a chair of a senior management team within a significant bank, who had been in this position of key decision maker for years.

Blame and punish

Banks may intensify supervision and controls, and increase sanctions for mistakes that are made, to communicate that errors are not acceptable, and to deter individual workers from making future errors (see Figure 8.5). Whilst this is a common response of banks when things go wrong, it is an ineffective response since the imposition of (deterrence) sanctions generally undermines employee trust and reduces rule compliance (Mooijman *et al*., 2015; Tenbrunsel & Messick, 1999).

Figure 8.5. *Error approach 'Blame and punish'*



In this third ineffective error approach of blame and punish, errors are not tolerated and they are responded to in an active manner by increasing sanctions for individual employees or a group of employees involved in making the error as the targets for deterrence. The primary responsibility for any errors made is placed with individual employees, regardless of the circumstances leading up to these errors or the broader organizational context in which these were made. In this approach, the standard response to errors is to increase sanctions for individuals or groups of employees involved in making the error. This primarily creates fear of the consequences of errors for the individuals involved (Van Dyck *et al.*, 2005; Mooijman *et al.*, 2015). It makes it unsafe to talk about errors or even to acknowledge that errors have occurred to evaluate them. Therefore, this error approach in fact stimulates the tendency to cover up errors, making it less likely that something is actually learned from them (Van Dyck *et al.*, 2005). When the quality of work behaviour is seen as the responsibility of individual workers alone – while leadership takes no responsibility for allowing or inviting these behaviours - this raises anxiety and stress, and reduces the willingness to comply with organizational regulations.

- *An illustrative example from supervisory practice (Nr. 14, see Table 2.1)*

  A senior manager who was responsible for an error explained how his executive board had reacted in this particular situation. This executive board had called in the senior manager as soon as an error made under his authority was discovered. In strong words – including swearing - he was summoned up to the board floor. The senior manager dreaded these calls and what would come next. Facing the executive board, he was personally blamed for the error that was made in his division. The executive boards' response to errors had a negative effect on him. The senior manager felt oppressed by the executive boards' responses to failure. He indicated feeling stressed and powerless as errors will continue to be made under his responsibility in the future, and he will suffer the shameful consequences.

1.2 How ineffective error approaches facilitate misconduct

All three ineffective approaches to performance errors – denial, empathy and blame and punish - can contribute in their own way to the emergence and continuance of unethical behaviour. How teams or organizations approach and handle errors – whether errors are hidden or discussed and evaluated openly – also influences how individual employees approach and handle errors (Frese & Keith, 2015, Van Dyck *et al.*, 2010, Van Dyck *et al.*, 2005, Cannon & Edmondson, 2001, Hofmann & Mark, 2005). This relates to employees' beliefs or experiences regarding the common responses to errors within the team or organization. These beliefs and experiences in turn influence their behaviour. Cannon and Edmondson (2001) argue that people hold tacit beliefs about failure and responses to errors. People within teams and banking organizations talk to each other, interact and communicate about courses of events and reactions of managers to failure or mistakes. This collective sense making is an important source of shared beliefs on failure (Morrison *et al.*, 2011). The relation between these shared beliefs on failure (e.g. 'it is not easy to discuss mistakes' and 'problems cannot be addressed quickly') and their ethical behaviour was empirically demonstrated (Cannon & Edmondson, 2001).

Low tolerance for errors – that characterizes the 'denial' and 'blame and punish' approaches – makes the occurrence of errors more negative to people. Making an error often leads to stress and negative emotions (Heimbeck *et al.*, 2003). Negative emotions and stress as a result of failure can be sources of new errors in themselves and distract people from analysing the error made, hindering a learning effect. An ineffective approach to errors contributes to employees feeling more negative emotions and increased stress when they make a mistake or fail to accomplish something. In addition, employees are more distracted by stress caused by errors (Hofman & Mark, 2006).

Furthermore, another mechanism related to negative emotions as a result from failure, underlies the tendency to ignore or deny errors. This mechanism refers to one's ability to balance the tendency to correct and prevent errors with the will to learn from them. When a mistake is made, preventing the error next time is often focused on. A first response is to hide or cover up a mistake and energy of the one making the error goes to negative emotions such as shame and guilt. The person making the error feels self-conscious. When negative emotions following the error inhibit people to balance between correcting their mistakes and learning from them, they focus on themselves instead of focusing on improvement. Their cognitive resources are wasted on self-focused attention when errors are approached with a rigid focus on prevention (error averse) (Homsma *et al.*, 2007 (a); Van Dyck *et al.*, 2010).

Finally, when errors are denied or punished, people within an organization are reticent to speak up and are concerned that raising issues will be ineffective (Morrison *et al.*, 2011; Edmondson, 2003). A culture where people do not feel safe to speak up is a result of social interactions and collective sense making of prior experiences people have with speaking up. People look out for social cues from the past about the potential consequences of their 'voice behaviour'. If voice behaviour is responded to by the organization with punishment, ridicule or bad evaluations, people within that organization will think twice before they utter opinions on practices they feel uncomfortable with.

Ineffective error approaches allow or invite errors to occur in the future through different underlying processes such as those related to the experience of stress and negative emotions such as guilt and shame. Furthermore, the three ineffective error approaches as discussed impair open communication on errors and team members speaking up on issues or mistakes. These negative effects of ineffective error approaches facilitate unethical behaviour. As I explained in Chapter 2, my conceptualization of misconduct refers to *intentional* unethical behaviour, whilst error refers to *unintentional* performance failures. I argue that ineffective responses to unintentional errors pave the way for intentional unethical behaviours. Employees who experience stress and negative emotions such as shame resulting from ineffective responses to errors, are inclined to explore ways to resolve these negative emotions which could lead to an increased need to save face by financially performing well. This increased need to perform in combination with a lack of open communication on errors, could create an environment where unethical behaviour is more likely and less visible. I argue that ineffective approaches to unintentional errors therefore

create a '*slippery slope*' to intentional unethical behaviour to occur. Gronewold, Gold and Salterio (2013) showed that team members tend to behave less ethically in a team with an ineffective error approach, by examining this amongst auditors reporting errors they discovered themselves. When these auditors could easily choose to ignore or not to report errors that were made, this ineffective error approach reduced the likelihood that self-discovered errors were reported. This was different when errors were approached openly and constructively in the company, so that employees felt their error reports would be seen as a way to increase work effectiveness (Morrison *et al.*, 2011; Edmondson, 2003). On the basis of this theory and prior research I argue that ineffective error approaches discourage team members to discuss concerns they may have or to improve faulty business practices. Instead, these error approaches invite workers to cover up errors that are made instead of confronting and redressing them. These effects of ineffective error approaches contribute to the occurrence and persistence of unethical behaviour at work.

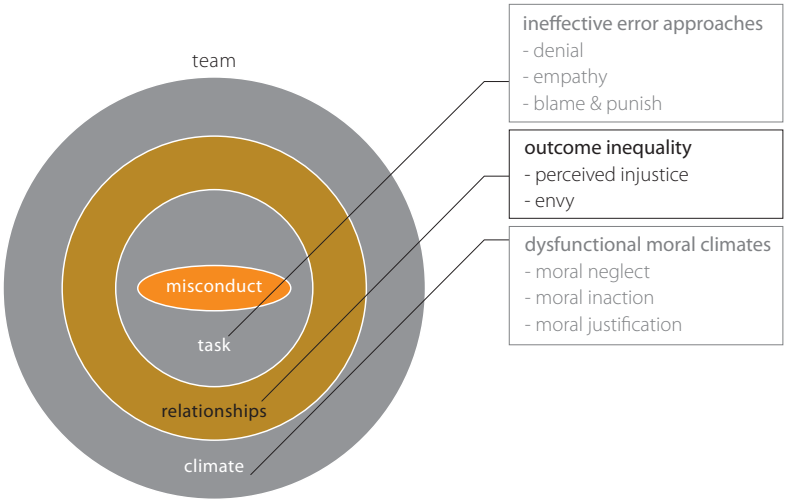
Based on the reviewed theory, I argue that assessing error approaches as a characteristic of team climates adds value to preventing future misconduct within banking. In Study 3 (Chapter 9) I will examine whether team climates can be identified and assessed on this characteristic. Furthermore, I argue that by improving error approaches within for instance trading teams, can mitigate the risk of future misconduct by team members. Improving error approaches involves first an increased awareness and deepened understanding by (senior) leaders of the variation in error approaches and their potential detrimental effects. Second, it requires an active approach to assess the current error approach in a team, and depending on the assessment findings, improve the way a team deals with errors. In Part IV, Chapter 10, I elaborate on these preventive approaches in more detail.

2. Outcome inequality: unequal relationships leading to perceived injustice and envy

In addition to ineffective error approaches, the way a team deals with outcome inequality can facilitate misconduct. Inequality in outcomes occurs whenever people work together in a team (see Figure 8.6). Team members do not receive the same salary, bonuses or opportunities for promotion or professional development. Different tasks are allocated to team members and often some tasks are perceived as more enjoyable, interesting or status enhancing than others. In day to day work, outcomes as income, promotions and tasks are not allocated equally over all team members.

Unequal outcomes within a team easily raise feelings of dissatisfaction and perceived imbalance. Especially when the inequality is (too) large, and the justification for these large outcome differences remains unclear. If not managed well, emotional consequences of outcome inequality can contribute to or evoke unethical behaviour of team members. This chapter introduces two emotional consequences of outcome inequality and elucidates how these emotional consequences can facilitate misconduct.

Figure 8.6. *Outcome inequality*



2.1 Negative emotional consequences of outcome inequality

My conceptualization focuses on two emotional consequences of inequality – through social comparison - that can lead to unethical behaviour: perceived injustice and envy. Before elaborating on these two emotional consequences, I explain the underlying process of social comparison.

Social comparison

Traders within a team, as all humans, compare themselves to each other (Festinger, 1954). This process, called social comparison, is inevitable in social interaction and thus a basic aspect of organizational life (Duffy, 2008; Brown *et al.*, 2007; Greenberg, 2007). According to Adams's (1965) equity theory, employees evaluate the fairness of their situation by comparing the ratio of their own inputs and outcomes with the ratio of inputs and outcomes of a co-worker. Employees compare themselves to others, for instance when their performance is evaluated by superiors relative to each other (Mumford, 1983) or when employees know how their pay compares to that of others (Blysma & Major, 1994). These comparisons increase when there are no objective standards on when performance or pay is perceived as 'good' or 'good enough'. When ambiguous standards lead to insecurity of team members, they use the process of social comparison to value their own inputs and outcomes (Festinger, 1954).

A trader can compare him/herself with a co-worker who is better off, called upward social comparison, or who is worse off than him, an example of *downward* social comparison (Brown *et al.*, 2007). Motives for these types of comparison differ. Through downward social comparison an individual feels better about him- or herself in comparison with a co-worker who is worse

off. Upward social comparison can be driven by a motivation to learn from the other who is better off. However, when the team member experiences low autonomy and control in his or her job, comparison with a colleague who is better off can induce perceived inequality. Perceived inequality resulting from social comparison is aversive and painful (Brown *et al.*, 2007; Tai *et al.*, 2012; Festinger, 1954).

Box 7. Example of emotions when receiving a bonus

People responded (to bonus award information) in one of three ways when they heard how much richer they were: with relief, with joy, with anger. Most felt some blend of the three. A few felt all three distinctively: relief when told, joy when it occurred to them what to buy, and anger when they heard others of their level had been paid much more. – From Michael Lewis' book Liar's Poker (p. 201) on investment banking, as quoted by Duffy (2008).

A competitive environment as can be found in the banking industry drives the negative emotional effect of (upward) social comparison processes (Brown *et al.*, 2007). Incentive structures influence the level of social comparison and competitiveness (Garcia *et al.*, 2013). The banking industry has a tradition of incentive structures in which a relatively high proportion of income depends on variable performance indicators. This induces substantial pay inequality within banks and teams within banks such as trading teams. Traders compete with each other for superior performance appraisals, which are linked to the incentive or bonus system, and determine career development opportunities. Although performance management systems aim to provide an objective standard to be used in performance reviews, in reality their performance is reviewed relative against the performance at the desk. These performance incentive systems, and how these are used in practice, thus invite individual workers to compare their efforts and outcomes against each other (Bylsma & Major, 1994; Mumford, 1983) and therefore enhance the possible detrimental effects of social comparison processes at work.

Performance incentive systems used in trading environments, and banking in general, are often result oriented. The key performance indicators used to assess performance are focused on results – i.e. profit and loss, or 'P&L' - and not so much on the efforts and actions the trader took to reach that P&L. In a markets business, fluctuations of the market can be unexpected. A trader acts upon these market dynamics, and, whilst a trader might be able to predict these changes depending on skill and experience, he or she cannot control these market dynamics and therefore cannot fully control his or her financial performance. Since this financial performance is often the key indicator for a positive performance review, hence a bonus, this can create a sense of helplessness and insecurity. The 'relief' felt in the example in Box 7 illustrates the tension a trader might feel around performance appraisal and bonus allocation. When tension or stress distracts a trader from his or her tasks, or hampers the quality of his or her decision making, this tension can be counterproductive for business. And, as discussed in paragraph 8.1.2, stress can result in errors and even unethical behaviours.

Perceived injustice

Substantial inequality in pay, performance appraisals and promotion opportunities within a trading team, are likely to lead to feelings of dissatisfaction (Brown, *et al.*, 2007; Greenberg, 2007). This inequality induces through social comparison processes perception of unfairness. When for instance relatively small performance differences can lead to large differences in outcomes, team members can feel unjustly treated by their supervisors or managerial authorities making performance appraisals (Ambrose & Cropanzano, 2003; Bies & Moag, 1986; Cohen-Charash & Spector, 2001).

Perceptions of injustice can stem from distributive, procedural or interactional concerns (Cohen-Charash & Spector, 2001). Distributive justice refers to the perceived justice of outcomes that individuals receive (Greenberg, 2007). These outcomes can for instance relate to height of pay and bonus (i.e. 'expecting 30% of fixed salary a priori whilst receiving 12,5%'), promotion decisions, decision on task allocation (i.e. 'who gets to do certain clients or transactions') and acknowledgement and praise. This concerns in a trading context for instance the decision to promote a team member, or the height of a bonus.

- *An illustrative example from supervisory practice (Nr. 15, see Table 2.1)*

  A trading-desk manager explains during a supervisory interview, that he perceives large income inequality within his team. "*I earn disproportionally more than my juniors*". He continued with his perception that this skewness is perceived as unfair by traders within his team. According to him, the juniors think "*Stop preaching to me, with your income you do not need to worry about making more money like I do*".

Procedural justice, defined as the perceived fairness of the process by which outcomes are determined (Lind & Tyler, 1988). Procedural justice concerns in this context for instance the extent to which (desk) managers come to these outcomes in a fair manner. As stated above, when uncontrollable market dynamics have impacted financial performance negatively and resulted in a lower bonus than expected, this can be perceived as unfair by a trader. His or her efforts and actions taken to achieve that financial result is outweighed by the actual (disappointing) result. Another example of procedural justice concerns situation where desk- heads receive credit for the financial performance of the desk whilst the efforts of individual traders that they took to achieve this outcome is insufficiently recognised.

Finally, interactional justice is an extension of procedural justice, and refers to the perceived fairness of the way management is behaving towards the trader in question (Bies & Moag, 1986). For example, did management explain how performance was reviewed, how bonuses were allocated or what exactly led up to a decision to promote a colleague over another? It concerns for instance whether a trader feels his desk manager treats him with honesty and respect. Managerial behaviour is here a signal of fairness (Vecchio, 2000). Perceived unfairness here can result from managers stealing ideas or taking credit for profitable business decisions.

- *An illustrative example from supervisory practice (Nr. 16, see Table 2.1)*

  A trader recalls during a supervisory interview that he was treated unfairly by a former manager. The trader had approached his manager about a proposed transaction. The trader felt that this transaction, requested by a client, included taking high risk for the bank. He therefore suggested to his manager to call a joint meeting with the compliance officer to discuss the level of risk, before deciding on next steps. His manager agreed to the traders' suggestion. During the meeting with the compliance officer, the manager and the trader, who brought a colleague from his team involved in the proposed transaction, the manager led the compliance officer to believe that he himself signalled the excessive risk and urged for the meeting to happen. The trader felt betrayed and stated to the supervisor during the interview: "*He made us look like we were criminals! I never have been so angry*". This example of interactional injustice still caused the trader to recall the situation vividly and show distress whilst discussing it.

The three kinds of perceived justice as described above are interlinked. Ambrose and Cropanzano (2003) have introduced a 'monistic approach' that treats distributional, procedural and interpersonal justice as one construct, showing that they represent outcomes that are not mutually exclusive and occur simultaneously. Thus, whilst there are three different kinds of reasons for perceived injustice, the impact of the perceived injustice is alike. As I will elaborate on in paragraph 8.2.2, this perceived unfairness can form a root cause of unethical behaviour.

Envy

Social comparisons and perceived inequalities may cause people to experience *envy* (Duffy *et al.*, 2008). As with perceived injustice, there are some organizational or contextual 123 antecedents of this emotional consequence of inequality. Envy in the workplace is easily elicited by perceived inequity in financial outcomes (Tai *et al.*, 2011) and is fuelled by competitive reward structures (Vecchio, 2000; Duffy *et al.*, 2008). Studies by Vecchio (2000, 2005) revealed also other contextual antecedents of envy, namely the employee's autonomy (the less autonomous, the more envious) and considerateness of leadership (the less considerate, the more envious). Consequently, envy arises easily amongst employees and between employees and management in organizational contexts where there is outcome inequality and competitiveness (Moore & Gino, 2013; Vecchio, 2000, 2005) as a result of unfavourable social comparisons and perceptions of unfair outcomes (Cohen-Charash & Mueller, 2007). Cohen-Charash and Mueller (2007) for example showed in their experimental study that, when envy is experienced in unfair situations, counterproductive work behaviours are augmented. Schaubroeck and Lam (2004) examined envy amongst Chinese tellers of Hong Kong branches of an international bank who were considered for promotion to teller supervisor. The most talented tellers were moved into management, and a commission including their management and HR made these promotion decisions. A month after the promotions the rise of envy amongst the tellers who were denied promotions was measured. Finally, studies of neurological activity (Takahashi *et al.*, 2009) demonstrate that envy is genuinely painful. In these studies, MRI's evidenced that parts of the brain that process social pain were activated when experiencing envy.

Envy and perceived injustice are related: envy is higher when the situation is perceived as unfair (Cohen-Charash & Mueller, 2007; Shaubroeck & Lam, 2004). Also, envy can lead to social undermining behaviour such as spreading rumours about colleagues and failing to defend a colleague. (Duffy *et al.*, 2012, Vecchio, 2005). Envy motivates employees to reduce the perceived superiority of the one who is envied. Social undermining behaviours can serve that purpose and simultaneously help to channel feelings of hostility (Cohen- Charash & Mueller, 2007, Duffy *et al.*, 2012). These social undermining behaviours could in their turn feed into perceived (interactional) injustice by the ones being socially undermined.

2.2 How negative emotional consequences of inequality facilitate misconduct.

Both perceived injustice and envy can facilitate unethical behaviour. Perceived injustice in outcomes or treatment makes people feel disrespected by organizational authorities (Lind & Tyler, 1988; Vecchio, 2000). Research shows that perceived injustice elicits dysfunctional work behaviours, such as organizational retaliation behaviour or lack of compliance with relevant guidelines (Cohen-Charash & Spector, 2001; Zoghbi *et al.*, 2014). As negative reactions to perceived injustice, behaviours such as theft, sabotage and retaliation have been demonstrated (see for an overview of these behaviours: Cohen-Charash & Mueller, 2007). Greenberg (1990) for instance found that as a reaction to perceived underpayment inequity, employee theft increased. When workplace practices are perceived to be unfair, employees are more easily tempted to reframe theft as an earned 'benefit'. This is especially true when traders compare themselves unfavourably to others (Cohen-Charash & Mueller, 2007). Through this mechanism, variable performance incentives raising perceptions of inequality can be a root cause of misconduct.

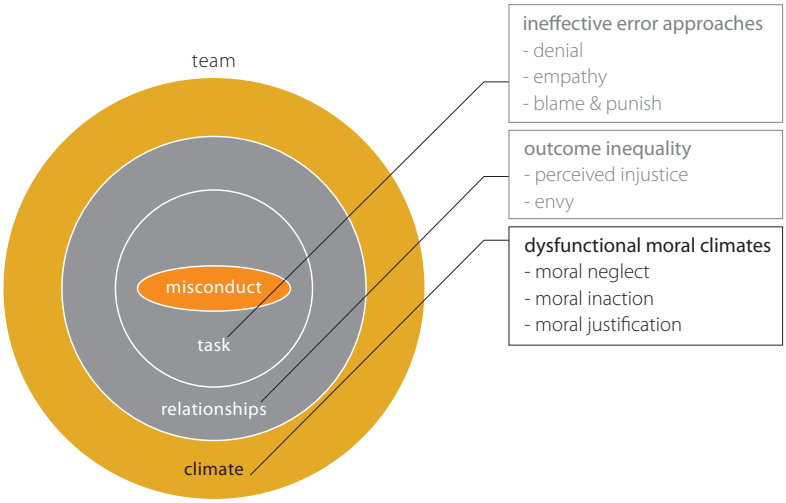
Envy can lead to the justification of unethical behaviour by believing that this behaviour helps to 'restore equity' (Moore & Gino, 2013). Furthermore, envy evoked by inequity causes team members to be motivated by the desire to aggress against the inequity and the team mates envy (Vecchio, 2000). Research showed that envy leads to dishonesty and damaging behaviour (Gino & Pierce, 2009), for instance by withholding information or sabotaging others at work (Duffy *et al.*, 2008; Cohen-Charash & Mueller, 2007).

In sum, prior empirical evidence suggests that perceived injustice and envy can facilitate misconduct. I argue that assessing inequality and its negative emotional consequences as a characteristic of team climates, adds value to preventing future misconduct within banking. In Study 3 (Chapter 9) I will examine whether team climates can be identified and assessed on this characteristic. Furthermore, I argue that reducing actual outcome inequality such as income differences within teams and banking organizations (Vecchio, 2000) can mitigate misconduct risk. Also, emotional consequences of inequality such as perceived injustice and envy can be managed in a way that mitigates the risk of these emotions resulting in unethical behaviour. In Part IV, Chapter 10, I elaborate on these preventive approaches in more detail.

3. Dysfunctional moral climates: neglect, inaction and justification

A third element I want to consider besides ineffective error approaches and the injustice of outcome inequality is the moral climate within a trading team (see Figure 8.7). This team climate characteristic can also facilitate misconduct. Moral climate refers to the way the team typically deals with the moral dimension of its work: which decisions and actions are considered 'right' or 'wrong'. Trading decisions are not straight forward: they may be complex, relying on changing market dynamics, taken under time pressure and leading to uncertain outcomes. Different stakeholders are involved, long-term implications are not always clear, and doing what is right for a client may contradict guidelines endorsed by others (e.g., regulatory requirements). Thus, in a trading context, knowing what decisions are 'right' or 'wrong' may be challenging and not straight-forward. In such instances, the importance of what our colleagues perceive as 'right' and 'wrong' rises.

Figure 8.7. *Dysfunctional moral climates*



Members of the same group or work team help us define what is moral and considered ethically good (Ellemers & Van der Toorn, 2015; Ellemers & Van den Bos, 2012; Haidt, 2001). Shared moral values tell us what is considered ethical, and specify how we should behave to be respected as a loyal team member (Ellemers *et al.*, 2013; Rai & Fiske, 2011). This is also the case for traders (Cohen & Morse, 2014). Over time, characteristic group values can be internalized and affect people's moral convictions (Manstead, 2000). Moore and Gino (2013) argue for this 'social nature of morality' and explain how this can overrule individual moral norms as we lose sight of our own 'moral compass' (Gino & Galinsky, 2012; Moore & Gino, 2013). Our 'inner voice that tells us what we should and should not do', as Moore and Gino (2013) put it, is under the influence of the group we feel we belong to. In sum, evidence from psychological research demonstrates that

internal moral standards are shaped by the groups we belong to. Hence the moral climate within a specific work team impacts on the moral behaviour of its members. This chapter introduces three dysfunctional moral team climates and elucidates how these moral climates can facilitate misconduct.

3.1 Dysfunctional moral climates

My conceptualisation of morality follows Moore and Gino (2013) and distinguishes three types of moral climate within teams that facilitate unethical behaviour. These moral climates foster (a) *neglect* of the moral content of actions, (b) *failure* to behave morally, and (c) *justification* of immoral actions. Below, these three types of dysfunctional moral climates are explained.

Climate of moral neglect

The mildest form of dysfunctionality is moral neglect. Moral neglect refers to a team climate that allows team members to remain unaware of the moral content of decisions, or the moral consequences of actions (Moore & Gino, 2013). Paragraph 8.3.2 elaborates on the way this team climate of moral neglect is facilitating unethical behaviour.

The organizational context can invite or enhance moral neglect through for instance organizational goals and socialisation (Moore & Gino, 2013). Organizational goals such as pressure on revenue, reducing costs and growing a business can direct behaviour in a way that undervalues the moral content and implications of decisions and actions (Grant, 2012). Socialisation refers to the process of new employees within a team to have them adopt social norms within that team – this can happen even if these norms are morally corrupting (Ashforth & Anand, 2003). Organizational socialisation, rule orientation and goals can support a team climates of moral neglect, though a process of 'moral fading'. That is, the moral content of decisions is not considered or is a 'blind spot' for a team and its members (Tenbrunsel & Messick, 2004), because the focus is on business or legal concerns (i.e. rules) only.

- *An illustrative example from supervisory practice (Nr. 17, see Table 2.1)*

  A middle manager, overseeing several trading desks that carry out transactions in the oil shipping industry, reflects during a supervisory interview on the alignment between his work and his moral values. He concludes a certain misalignment by stating "*It is kind of strange isn't it... I work in oil, but I personally do not think it is good for our climate and environment*". Within the bank where this manager was employed, financing and handling transactions around oils shipping was a growth market, driving excellent revenue for the business line. Although the supervisory interview did not explicitly address the organizational drivers of this misalignment, it seems plausible that the organizational goal of business advantages of engaging with this industry blinded those involved to the moral implication of financing oil shipping. These moral implications are neglected, as they are not seen as a valid concern for doing business in this industry.

Next to organizational drivers of moral neglect Moore and Gino (2013) highlight social psychological drivers of this dysfunctional moral climate. Social or shared norms within teams that neglect morally relevant consequences facilitate moral neglect (Churchland, 2011). An example of such a social norm could be that a trading desk collectively think that credit risk is covered by the credit team and is not owned by the traders, disregarding that they have a responsibility in managing credit risk in each transaction. If these 'local' shared norms do not address or include moral aspects of decisions, this dampens moral awareness.

Next to social norms, social categorization is a social psychological mechanism that leads to traders distinguishing between their own team (the *ingroup*) and other teams or others (the *outgroup*) (Hogg, 2007,). This mechanism of social categorization can drive moral neglect (Moore & Gino, 2013) in two ways. First, it can lead to a psychological closeness to the team traders identify with (their ingroup), and through this process we can be blinded to the implications or mere nature of unethical behaviour of their teammates (Gino, Ayal, & Ariely, 2009). Second, it can lead to a psychological distance to others outside their own team, as for instance other teams and stakeholders such as clients. Because of the social categorization mechanisms, the well-being of these 'outgroup others' is less important than the well-being and interests of the ingroup. This psychological distance to others outside the team traders identify with can be augmented by the general tendency within trading businesses to work long hours and be focused on work and markets outside of the trading floor as well. This may create traders to work 'in a bubble', with little outside-in perspectives.

Climate of moral inaction

Moral inaction refers to the failure to behave ethically even when realizing that the behaviour is unethical. In contrast with moral neglect, this is because when a team member is aware of the moral content of his actions, he or she feels unable to follow through with the ethical behaviour that is required (Moore & Gino, 2013).

A possible driver for a climate of moral inaction is obedience to authority (Moore & Gino, 2013). A study showed for instance that participants obeyed the request of supervisors to discriminate against potential employees, regardless and independently of their own beliefs about race (Brief *et al.*, 2000). In addition, Moore and Gino (2013) highlighted social conformity and diffusion of responsibility as social psychological drivers of moral inaction. Through a process of social conformity, individuals often conform to the decisions and behaviours of their team members (Asch, 1955). Asch showed in his research that individuals go along with the perception of a group, even when this contradicts their own perception. This process could contribute to a climate where team members do not act when they are aware of immoral behaviours. For example, when a trader thinks a certain transaction is unethical, he will be less inclined because of social conformity mechanisms to act upon his own judgement when the majority of his colleagues at the desk perceived this transaction as being ethical. Diffusion of responsibility also reduces the likelihood of team members to act in case of immorality. Team members are less likely to respond to immoral behaviours that they observe, when others are observing these behaviours with them

and do nothing (Darly & Latané, 1968). This 'bystander effect' and social conformity both could explain low whistleblowing numbers. A plausible explanation for low whistle blowing numbers is that employees are reticent to report unethical behaviour when the majority in their professional context shows this behaviours. Research shows that less than half of a team that see immoral behaviour would report it (Rothschlid & Miethe, 1999).

- *An illustrative example as reported in the media*

  The Financial Times article on Kweku Adoboli referred to in the Introduction offers a quote from one of Adoboli's colleagues that appears to indicate a climate of moral inaction. This colleague told the author of the FT article that Adoboli was the man to turn to if you had screwed up. He would fix it for you, and "*We didn't know how he did it, but we didn't want to know*". This quote suggests that the colleagues of Adoboli were aware that the solutions Adoboli found were potentially unethical. Nevertheless, this awareness did not prevent them from consulting him for help nor did they address or question his ways. In fact, this quote indicates that Adoboli's team mates consciously chose to remain ignorant.

Climate of moral justification

Moral justification refers to the tendency to reframe immoral actions in a way that distorts individuals understanding of the moral content of their actions (Moore & Gino, 2013). A climate of moral justification refers to a team climate that allows team members to reframe immoral actions as defensible.

A possible driver for a climate of moral justification is group loyalty (Ashforth & Anand, 2003). Pershing (2002) for instance showed that within the U.S. Military, loyalty to fellow officers provided a justification to normalize officially prohibited behaviour. Moore and Gino (2013) argue that self-verification facilitates moral justification. Self-verification induces team members to verify their existing view of themselves (Swann, 1983). As we would like to see ourselves as moral (Cohen & Morse, 2014; Vecchione & Alessandri, 2013), the need for team members to self-verify may lead to them regarding their behaviour as ethical and thereby motivate them to justify unethical behaviour of themselves and others. Next to self-verification, moral justification can be driven by unfavourable social comparisons (Monin, 2007). In line with outcome inequality – as described in paragraph 8.2 – negative emotional consequences of social comparisons could serve to justify immoral behaviour.

- *An illustrative example as reported in the media*

  A climate of moral justification in trading was observed for instance when traders involved in the Libor manipulation stated that "*Everyone knew*" and "*Everyone was doing it*" (see Box 1 in Chapter 1). In their perception, the widespread awareness and occurrence of the manipulation implied it was morally acceptable.

3.2 How dysfunctional moral climates facilitate misconduct

The climates of moral neglect, moral inaction and moral justification all increase the risk of unethical behaviour or misconduct (Moore & Gino, 2013; Kish-Gephart, Harrison & Trevino, 2010). In a team climate of moral neglect, a trader might fail to recognize the moral consequences of his or her actions. This makes it easier to behave unethically, free from psychological distress, guilt, or regret. As paragraph 8.3.2 explained, a possible driver for a climate of moral neglect is the nature of 'local' shared norms that neglect morally relevant consequences (Moore & Gino, 2013; Churchland, 2011). If these shared norms within a team do not address or include moral aspects of decisions, this dampens moral awareness and reduces vigilance against possible unethical behaviours. When a trader is unaware of the moral content, unethical behaviour is less psychologically taxing and more likely to occur (Moore & Gino, 2013; Butterfield *et al.*, 2000).

A team climate of moral inaction obviously leads to unethical behaviours – failing to act morally can imply to act immorally. The fact that these unethical behaviours remain unchallenged, can be perceived as 'social proof' that these behaviours are acceptable according to the team's moral norms. The more team members behave unethically, the more compelling this behaviour becomes (Goldstein *et al.*, 2008). A more general effect of continued immoral behaviour might be that team members lose their belief in the effectiveness of addressing it. In interviews with traders who had left the trading business, Luyendijk (2015) reports that these traders indicated their frustration about feeling unable to change business practices they considered unethical after their attempts to address these practices. Moral inaction can also result when initial attempts to address immoral behaviour are unsuccessful.

Finally, a team climate of moral justification allows traders to reframe immoral behaviour as defensible. This reduces the dissonance or guilt that may prevent unethical behaviour. The justification of immoral behaviour in the present, paves the way for behaving unethically in the future (Moore & Gino, 2013).

In sum, evidence from prior studies suggests that the dysfunctional moral team climates of moral neglect, inaction and justification can all facilitate the occurrence of misconduct. Based on the insights in the personal and organizational drivers of these moral climates and the way these climates elicit or contribute to the persistence of unethical behaviours, I argue that assessing moral climates within teams adds value to preventing future misconduct in banking. Furthermore, I argue that improving dysfunctional moral climates within teams can mitigate the misconduct risk. This requires an increased awareness and deepened understanding by (senior) leaders of moral climates, their drivers and their possible detrimental effects on ethical behaviour. Based on this understanding moral climates within trading teams may be improved in order to prevent unethical behaviour from occurring. In Part IV, Chapter 10, I elaborate on these preventive approaches in more detail.

Part III

Social psychological root causes of misconduct

Chapter 9

Identifying corrupting barrels: assessing team level root causes of misconduct

Chapter 9
Study 3. Identifying corrupting barrels: assessing team level root causes of misconduct

1. Deep dive assessment of two trading teams

Bank B is an internationally operating, significant (too big to fail) bank with, investment banking and trading activities as part of its business model. Within those trading activities, financial supervision assessed a business line that faced high integrity risk. This high integrity risk was based on the large transactions and the clients from high corruption countries this business line was dealing with. The high integrity risk for this business line was identified by the financial supervisor as well as the bank itself. Financial supervision conducted a structured behaviour and culture assessment on two trading teams (desk A and B) within that risky business line (that consisted of five desks in total at the time) with the objective to identify behavioural patterns and their drivers within these teams that might facilitate current or future unethical behaviour.
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1.1. Research question

The investigation of these teams is used to address the following research question:

Research question

5. *Is it possible to identify the climate of a team and to characterize and compare teams in the same organization, based on key aspects of a dysfunctional team climate that can facilitate unethical behaviour?*

1.2. Approach

Team Climate was assessed by applying a supervisory framework in a supervisory deep dive assessment. This Corrupting Barrels framework and assessment is summarized in a two-pager that is included in Appendix A. This two-pager describes the scope, objective, deliverables, underlying model and method of this supervisory assessment. The method combines desk research with team observations and interviews. Finally, a survey is part of the assessment method. I describe the survey and its results in paragraph 9.3.

First, I analysed seven documents requested by the supervisors through desk research, as listed in Table 9.1. Appendix B lists the documents that the bank was asked for by financial supervision. The documents analysed contained all written information that could be found on the demographics of the teams of focus (desks A and B), the behavioural guidelines for the teams, and any information on the past or current climates within the teams.

Table 9.1. Documents analysed through desk research

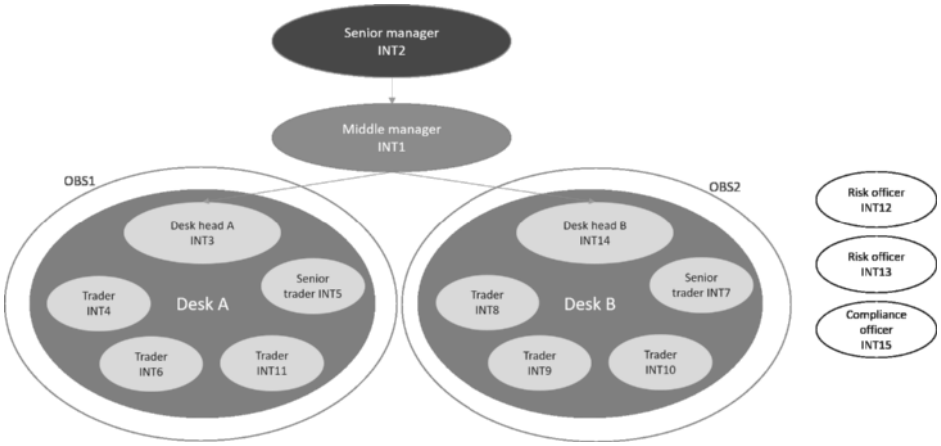
Category		Documents
Demographics	1	Overview of employees, date of birth, gender and tenure, desks A and B, Aug 2016
	2	Compensation per employee of desks A and B, Aug 2016
Behavioural guidelines	3	Code of conduct, 'Our core values and business principles in practice' – at bank level
Data (indirectly) indicating team climates	4	Sick-leave desk A, Aug 2016
	5	Sick-leave desk B, Aug 2016
	6	New hires overview, desks A and B, Aug 2016
	7	Leavers overview, desks A and B, Aug 2016

Second, I conducted two team observations: one observation per desk. These team observations were announced by the supervisors of behaviour and culture and planned together with the desk heads of desks A and B. Two supervisory observers conducted the team observations, sitting with the teams while they carried on with their daily work. I was, as the assessment leader, one of the observers for both observations. The other observer was for each observation a different supervisory expert of behaviour and culture, who was not involved in the assessment (therefore having a fresh and unbiased view). The duration of the team observations was 60 minutes per observation (i.e., per desk).

The observers used an observation format as included in Appendix D. The observation format was structured into three main categories, corresponding with the levels of the 'Corrupting Barrels' model: task (e.g. error approach), relationships (e.g. outcome inequality) and climate (e.g. moral climate). Observations that could be related to or indicate something about team climate (such as interactions between desk members, with the desk head, with clients, comments by team members, personalised gadgets on desks), were regarded as relevant and noted.

Next to desk research examining nine documents and two team observations, fifteen interviews were conducted with all members of the two trading teams, the desk heads, middle and senior management and with risk and compliance functions. Figure 9.1 gives an overview of the fifteen interviews (abbreviated as 'INT') and two observations (abbreviated as 'OBS'). The duration of each interview was 60 to 90 minutes. The interviews were semi structured: a set question format was used, and is included in Appendix C. Just as the observation format, the interview format is structured into three main categories, corresponding with the levels of the 'Corrupting Barrels' model: task (e.g. error approach), relationships (e.g. outcome inequality) and climate (e.g. moral climate). I conducted each interview, together with another senior supervisor. The bank was asked not to accompany the interviewees (with for instance a compliance or audit officer), to allow interviewees to speak freely and to ensure confidentiality.

Figure 9.1. *Fifteen interviews and two team observations*



The local leadership of the trading team by the deskhead is of influence on the team climates at the desks. How the leader responds to errors, how he or she manages the outcome inequality and discusses the moral aspects at the desk impacts the error approach, outcome inequality and moral climate (I explain the impact of leadership in greater detail in paragraph 10.2.1 Leadership is key). In the interview format and observation format leadership was therefore added as a fourth category, because of the impact of leadership on the three categories mentioned.

1.3. Results

Results desk research

The code of conduct lists the business values and behavioural principles that employees throughout the bank are expected to follow or comply with. These principles relate to for instance customer service, risk taking and sustainability or long term thinking. The code's aim is to serve as a guidance for professional decisions and all actions in the bank. As a consequence, the code is not business or team specific. To what extent the code of conduct is of influence on the decisions at team level is not assessed here.

Desks A and B can be differentiated in terms of demographics, based on the information that was provided by bank B through the desk research documents. This information showed relevant differences in gender, tenure and turnover and compensation or income between the two assessed teams. As Table 9.2 shows, while the teams are comparable in age of traders including desk heads (of 32 and 35 years of age), the teams differ in *gender* distribution. Desk A registers seven employees, including one female trader and six male traders. However, the female trader was at the time of the assessment absent due to long-term illness. Desk B also registers seven employees, with five female traders and two male traders. Also at this desk, one female trader was absent at the time of the assessment due to long-term illness. In sum, desk A has mostly male traders (87% of all desk A traders) and desk B has mostly female traders (71% of all desk B traders).

Table 9.2. Demographics per desk

Demographics desks A and B			
		Desk A	Desk B
Gender	Female	1 of 7 (14%)	5 of 7 (71%)
	Male	6 of 7 (86%)	2 of 7 (29%)
Age	Range	27 – 37 yrs	27 – 36 yrs
	Average	32 yrs	32 yrs
Tenure	Months	53	41
	Years	4.4	3.5
Turnover	Left in '15/'16	0 employees	3 employees
	Hired in '15/'16	1 employee	3 employees

Desks A and B differ slightly in *tenure*. The traders of desk A (53 months, 4,4 years) have worked on average a year longer at bank B than the traders of desk B (41 months, 3,5 years). The *turnover* of desks A and B differs more clearly. During 2015 and 2016, three employees left desk B due to 'voluntary termination' and three new employees were hired permanently. In the same period, only one new employee was hired permanently to work at desk A, while no employees left desk A. In sum, at desk A the traders have been working at bank B (a bit) longer than the traders at desk B. Also, desk A has seen less turnover of employees than desk B.

The *inequality in income within* desks A and B – expressed by the difference between the highest and lowest incomes within a team – does not differ. Within desk A, the highest income (€190.127, fixed plus variable salary) is three times the lowest income (€62.187, fixed plus variable salary). Also within desk B, the highest income (€178.475, fixed plus variable salary) is three times the lowest income (€52.360, fixed plus variable salary). However, the way fixed and variable income are set differs distinctively *between* desks A and B. Table 9.3 shows that the traders of desk A get paid more than the traders of desk B. The average fixed salary per trader is 7,2% higher for desk A (€93.825) than for desk B (€87.525). Also, the traders of desk A receive more variable income than desk B traders. The average variable salary per trader for desk A (€15.375) is almost three times the average variable salary for desk B (€4.000). The total 'bonus-pool' for desk A (€92.250) is over three times the total 'bonus-pool' for desk B (€28.000). Furthermore, for desk A 14% of the total income per trader is variable, while for desk B 4% of the total income is variable. This shows that the way fixed and variable income per trader is balanced differs per desk – irrespective of the financial performance of each desk. Finally, more traders at desk A receive variable income (83% of all traders at desk A) than at desk B (43% of all traders at desk B). Considering that desks A and B worked with the same kind of transactions in the same product group (although a different 'client' area), with the same number of traders, of about the same age and just a slight difference in tenure, with the same senior management, from the same building – the difference in fixed and variable pay balance is striking.

Table 9.3 *Fixed and variable income*

Fixed and variable salary – in euros (€)					
	Total fixed salary	Average fixed salary per trader	Total variable salary	Average variable salary per trader	% variable total from fixed total
Desk A (6 people)	562,947	93,825	92,250	15,375	14%
Desk B (7 people)	612,675	87,525	28,000	4,000	4%

Unfortunately, it remains unknown on what grounds this variable income is allocated. Information on targets or KPI's is missing from the desk research documentation – although the supervisor had requested this information from bank B. It is therefore impossible to analyse to what extent behavioural targets are included (or what these targets are) in the performance assessments.

In sum, the information on gender, age, tenure, turnover and income distribution adds to the profiling of teams. Although the team climates of desks A and B and the risks of these team climates can not be defined based on this information alone, it offers a first characterization of desks A and B as summarized in Table 9.4.

Table 9.4. *First team profile based on desk information*

First team profile based on desk information	
Desk A	Desk B
Mostly male	Mostly female
Longer tenure	Shorter tenure
Less turnover	More turnover
Higher fixed and variable pay	Lower fixed and variable pay
Higher percentage of total income is variable	Lower percentage of total income is variable
More traders recieve variable income, irrespective of performance	Less traders recieve variable income, irrespective of performance

Results observations

The team observations of desks A and B resulted in observations of their physical situation, the items on their desks and their interactions with each other. First, traders of desk A were sitting at two rows of working desks, facing each other. These rows of desks were situated on an open office floor, with many more rows of desks (other trading teams). On the other side of that same floor, traders of desk B were also sitting at two rows of desks. The traders of desk B were not facing each other, but sitting in one aisle with their backs towards each other. So, the desk A traders could look at each other by looking past their computer monitors, while the desk B traders had to turn around on their chair to see each other. All working desks were equipped with a personal computer, monitors (two to four monitors for each trader) and a desktop phone. Apart from this standard equipment, professional and personal items were visible on the working desks of the

two teams. Professional items were: pens, notebooks, forms, staplers, calculators, mobile phones and headsets / earphones. On the walls near the working desks of both desk A and B, whiteboards were placed that were used to note updates and progress of work. While the number and sorts of professional items were the same for both desks, the personal items differed per desk or team. At desk A there were more personal items, and different personal items than at desk B. The personal items at desks A and B are listed in Table 9.5

Table 9.5. *Personal items on and around the desks*

Personal items on and around desks	
Desk A	Desk B
- Poker chips - Bottle opener - Ibuprofen (pain killer) - Some change / money - Gadget of a club - A self-made drawing of a skull - Picture of two beautiful women - Poster of Mohammed Ali, standing over his opponent whom he had just knocked out - Poster of B.A. ('bad attitude') of the A-team	- Fruit - Gum - Water - Picture of the team going out

Regarding the interactions between desk members that were observed during the team observations: both teams demonstrated interactions amongst the team members and with clients during the team observations. The interactions at desk A were characterized by loud laughter and a lot of talking at the desks and on their phones. One trader asked a more senior trader about the use of some sort of form. A joke was made about a trip abroad for work, followed by laughter. The observers interpreted these interactions as friend-like and lively. At desk B the interactions were less frequent than at desk A. At some point during the observation, the desk head of desk B had a telephone call with another department within the bank to talk about how a meeting went. A trainee started talking to one of the observers about how he likes the work he does. Later this trainee asked the desk head "Do you have a moment to discuss this model with me?". Another trader laughs while she is on the phone. It is more quiet than at desk A. Traders at desk B even tell the observers that they hear the laughter of the desk A team across the floor. The observers interpreted the atmosphere at desk B as less outspoken than at desk A. A quote from one of the observers is that she experienced the desk B team as "colourless and not very personal", and "as if the traders do not know each other really". While desk A was observed as showing more camaraderie and cohesiveness.

Results interviews

The minutes of fifteen interview were analysed by identifying and counting quotes indicating the team climate aspects or characteristics that could facilitate unethical behaviour according to the Corrupting Barrels model: ineffective error approach, outcome inequality and dysfunctional moral climate.

The analysis of the fifteen interview minutes show that the two teams - desk A and desk B – can be characterized by two ineffective team climate characteristics that facilitate unethical behaviour, according to the Corrupting Barrels model:

a. Ineffective error approaches (task level). This concerns the way desks A and B deal with errors.
b. Dysfunctional moral climates (climate level). This concerns the way desks A and B typically deals with the moral dimension of work.

The interviews revealed no observation that seemed related to outcome inequality or its emotional consequences, as the third aspect of a Corrupting Barrels team climate. Table 9.6 provides an overview of the two ineffective team climate characteristics found, and lists the number of quotes and interviews that indicate these characteristics. Next to these ineffective team climate characteristics the interviews revealed some indicators of a dysfunctional leadership style. This concerns patterns in leadership of the desk head at desk A. Table 9.7 presents the number of quotes and interviews on this theme.

Table 9.6. *Number of quotes and interviews indicating team climate aspects that facilitate unethical behaviour*

Ineffective patterns - indicating a team climate that facilitates unethical behaviour (Corrupting Barrels team characteristics)						
Theme	Ineffective pattern			Desk	No of quotes	No of interviews
Error approach	'Blame & punish' error approach			Desk A	10	8
	'Denial of errors' error approach			Desk A	5	4
	'Empathy' error approach			Desk B	4	4
Moral climate	'Moral neglect'			Desks A & B	7	5
	Strong collective norms	Cohesiveness	Friend-like interactions	Desk A	6	5
			Low turnover	Desk A	3	3
		Masculine	Masculine atmosphere	Desk A	4	4
			Laugh & win	Desk A	8	6
			No serious or soft talk	Desk A	7	4

Table 9.7. *Number of quotes and interviews on dysfunctional leadership*

Dysfunctional leadership					
Theme	Ineffective pattern		Desk	No of quotes	No of interviews
Leadership	'Authoritarian'	Authoritarian style	Desk A	13	9
		High demandingness	Desk A	7	5
		Low responsiveness	Desk A	7	5

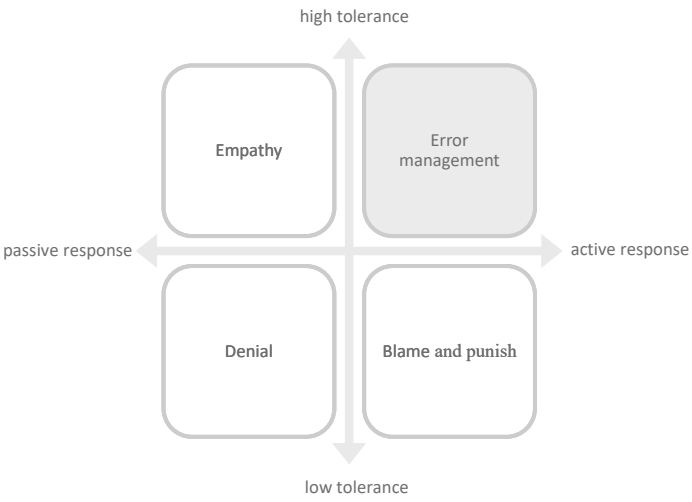
Below I will explain these patterns in more detail, and indicate how they differ per desk.

a. Ineffective error approaches - task level

The interviews indicate for both desks an error approach, that could facilitate unethical behaviour of individual traders. For desk A the interviews suggested a 'blame and punish' error approach – characterized by a low acceptance of and active response to errors, see Figure 9.1. This blame and punish error approach within a team can elicit cover-up behaviour and denial of errors. These effects facilitate unethical behaviour of team members. The blame and punish approach is generally considered to be ineffective, just as the 'empathy' and 'denial' error approaches. Chapter 8 offers a more in-depth explanation of these ineffective error approaches and their relation with unethical behaviours, and refers to underlying theory.

Seven quotes from five interviews with desk A members, indicate a blame and punish error approach at desk A. Another three quotes pointing in that direction came from interviews with risk and senior management on the error approach at desk A. Examples of the ten quotes in total (see Table 9.6) that evidence a blame and punish approach are the desk head explaining that "*he would like to see that employees thank him and bow their head when he points out that they made an error*", and that "*he does not like it when employees talk back defensively*". Another quote of an interviewee is that "*errors are sure to be called out, directly, aimed at the person who did it. Some sort of tell-off, with everyone there to hear it. It is not comfortable.*" The consequence of a blame and punish error approach can be that employees simply start to deny that error do and could occur. Six quotes from three interviews with desk A members and one interview with a non-desk A member, indicate his denial of errors at desk A. Examples of these six quotes are "*There are no problems*" and "*They thought openness on errors would turn against them*".

Figure 9.2. *Four error approaches, of which the error management approach represents the most effective way to deal with errors*



At desk B another ineffective error approach is indicated by the interviewees. Four quotes from four different interviews with desk B members suggest an 'empathy' error approach. This approach is characterized by a high acceptance of but passive responses to errors, see Figure 9.2, and risk a passive attitude of desk members towards errors, preventing that they learn from mistakes. Both effects could facilitate future unethical behaviour. Examples of the quotes that suggest the 'empathy' error approach are "*Everyone makes mistakes*" and "*Things go wrong regularly*". The interviews do not demonstrate an active response to errors: there are no signs of structured and organized learning from errors at desk B. For both desks the Employee engagement survey that was studied as part of the desk research analysis, reports "where I work we regularly discuss how we can improve the way we do things" as one of three main areas of improvement

b. Dysfunctional moral climates - climate level

The interviews indicate a climate of 'moral neglect' at desks A and B. A climate of moral neglect refers to a lack of awareness of the moral content of decisions, or the moral consequences of one's actions, independent of the extent to which team members are aware of the rules they ought to follow. This team climate can be characterized for instance by shared norms that focus on the business or legal implications of work decisions alone. This allows team members to remain unaware of the moral implications of the choices they make or other morally relevant consequences of their actions. This moral neglect could create blind spots and inhibit careful considerations, both enhancing possible unethical behaviours. Chapter 8 explains ineffective moral climates and their relation to unethical behaviour in more detail and refers to the underlying theory.

The lack of quotes on perceived moral aspects of work, derived from the fifteen interviews, are suggestive of a climate of 'moral neglect'. Although questions were asked by the interviewees on this moral dimension, the interviewees were not talking about it. However, seven quotes indicate a low moral awareness, such as "*I do not like to blow things out of proportion*" and a lack of dialogue on moral aspects within the teams, such as "*We do not talk about soft things*". Next to this climate of 'moral neglect' for both desks, the interviews suggest strong collective norms within the team of desk A that might contribute to a climate of moral neglect. These strong collective norms concern cohesiveness and masculinity – both strengthening the social norm within the team not to discuss moral aspects. In the interviews, cohesiveness is indicated by six quotes on friend-like interactions at desk A from five different interviews. The cohesiveness is further illustrated by three interviewees with three quotes on the low turnover at desk A. Examples of the quotes that suggest a strong collective norm regarding cohesiveness are "*This is sort of a friend team*", "*We are close as a team*" and "*They do a lot after work hours with each other*". Masculinity is evidenced by four quotes from four different interviews, such as "*It is like a football team, all guys*" and "*A lady would have a hard time in this team*". This masculinity is further illustrated by eight quotes from six interviews, on the importance of laughing and winning. Examples are "*Laughing and having a good time is important*" and "*I call him the CEO: Chief Entertainment Officer*". Seven quotes out of four interviews express a reluctance for 'too soft or serious talk'. Examples of these quotes are "*It is*

not common to talk about soft things in this team", "*I am impatient, that is why I chose this work*" and "*Now we do weekly starting meetings, where we talk about private stuff too, although that is not easy in this team. Here it is more about making money*".

c. Leadership level: dysfunctional leadership style

The interviews suggest a dysfunctional leadership style of the desk head of desk A. His dysfunctional leadership style is characterized by demanding a lot from employees and showing little responsiveness to their needs. This authoritarian or autocratic leadership style (Chan et al, 2012; Schuh & Zhang, 2013) can strengthen a team climate that facilitates unethical behaviour. For instance, high demandingness may strengthen an ineffective error approach by inhibiting learning from mistakes and eliciting cover-up behaviour, and thereby facilitate future unethical behaviour. Low responsiveness may enhance a lack of dialogue within the team on moral dilemmas, contributing to a climate of moral neglect that facilitates unethical behaviours. The authoritarian leadership style of the head of desk A is evidenced by thirteen quotes from nine interviews. Examples are "*He is too direct and authoritarian*". "*Desk head is very direct. This can be shocking to people*" and "*He is very hierarchical*". His high demandingness, including impatience and results-driven behaviour is illustrated by seven quotes from five different interviews, including an interview with himself. Examples are "*I* (the desk head) *am allergic to lazy or stupid colleagues. I like quick thinkers. I like to put energy in smart and quick people. I find it more difficult to give time to people with a lower tempo*" and "*He is impatient*". His low responsiveness is illustrated by seven other quotes of five interviews, such as "*If I* (the desk head) *can chose between HR things like development of people and making a deal, I want to make a deal*", "*He could do a better job in listening*" and "*He can be a little too strict or directive. If I would be manager of that team, I would give more room to people. I would do more about team development*".

In sum, the interviews indicate ineffective error approaches and dysfunctional moral climates within desks A and B. Table 9.8 provides an overview of the team climate patterns that were found in the fifteen interviews, and sums up their possible effects that facilitate unethical behaviour of team members. Next to these two team climate characteristics that may facilitate misconduct, the interviews indicate an authoritarian leadership style at desk A that strengthens the two ineffective team climate characteristics. The detrimental impact of this leadership style on team climate is summarized in Table 9.9.

Table 9.8. *Assessed team climate aspects, and how they facilitate unethical behaviour*

Category	Team climate aspect	Possible effects that facilitate unethical behaviour
Error approach	'Blame & Punish' – desk A	- Denial of errors - Cover up behaviour
	'Empathy' – desk B	- Passive attitudes - Lack of learning from mistakes
Moral climate	Moral neglect – desks A and B	- Disregard of moral dimension of decisions, enhances blind spots - Inhibits careful consideration
	Strong collective norms – desk A	- Inhibits independency and countervailing power: this increases the chance of taking excessive risks or compliance failures.

Table 9.9. *Assessed leadership style, and its effect on team climate*

Category	Pattern	Possible effects that facilitate unethical behaviour
Leadership	Authoritarian style – desk A	- Strengthens dysfunctional moral climate: this leadership style inhibits careful considerations, indepency and countervailing power. - Strengthens ineffective error approach: this leadership style enhances cover-up behaviour and inhibits learning from mistakes.

The interviews with middle and senior management – the management layers above the desks, see Figure 9.1 – and with risk management, also show concern about the behaviours within the desk A team. In these interviews, previous unethical behaviour of desk A members was discussed explicitly. These behaviours came to light through excessive expenses by desk A members and the desk head (e.g. spending too much money on dinners and champagne, with or without clients). An example of a quote on this subject is "*Large checks: this team is very commercial and has known the days of large expenses. I have collected these checks and expense tickets, and have discussed them in the management team, making clear that this was unacceptable behaviour and that I draw the line*".

Even though senior management has been clear about expense behaviour, there are lingering concerns about the ethical behaviour at desk A. This is evidenced by two actions. First, senior and risk management still check the expenses for desk A, including the deak head, with great attention. "*The expenses of the desk head I check every six months myself, and I will keep doing that, because he tends to cross the line*". Second, senior and risk management have placed a senior trader at desk A, as a 'right hand' of the desk head, that they know and trust. Their quote on his influence is that he is "*the conscience of the desk*".

1.4. Conclusions

The team climate assessment reported here defined team climate and identified differences in team climate characteristics facilitating unethical behaviour, that characterize teams in the same organization. By combining desk research, team observations, and interviews, it is possible to effectively define team climates and identify these differences in team climate aspects.

The results of the desk research, team observations and interviews suggest distinct team climates that differ per team. These differences in team climate of desks A and B suggest that the team climate of desk A has more 'corrupting' patterns and characteristics, than the team climate of desk B. Yet, the assessment also shows an ineffective error approach at desk B, the 'empathy' approach, and signs of moral neglect. However, the assessment reveals more risk factors at team climate level for desk A as it shows:

1. A 'blame and punish' error approach, that already shows some signs of denial of errors (low acceptance that errors are part of professional life). The results of the interviews indicate this ineffective error approach tends to be used in this team.

2. A climate of moral neglect, discouraging awareness and dialogue on the moral dimension of the work. This moral neglect is possibly reinforced by social collective norms at desk A on cohesiveness and masculinity, that were not found at desk B. Next to the large number of interview quotes backing this up, the desk research and team observations resulted in some evidence for cohesiveness (e.g. desk A showed a lower turnover than desk B, the team at desk A was physically facing each other on the working floor, while desk B was sitting with their backs facing each other, and friend- like interactions were observed at desk A that were not observed at desk B) and in some evidence for masculinity ((a) all men, while desk B has mostly women, (b) masculine personalised items on and around their working desks, while desk B lacked these items, and (c) higher variable income connected to performance than desk B) as well.
3. A dysfunctional leadership style at desk A, that was not indicated for desk B. This authoritarian leadership style was evidenced by the interview results.

Next to the three indicators reported here – desk research, team observations and interviews – a fourth indicator for a corrupting team climate at desk A (in contrary to desk B) revealed itself during the interviews. Management information at senior management and risk management level indicated inappropriate behaviours at desk A (in the form of excessive expenses). Their information was differentiated per team, which enabled them to assess behaviours per desk.

Taken together, this information suggests that it is possible and sensible to assess team climates when analysing and preventing unethical behaviour. Teams are distinct units or groups that show distinctive patterns indicating team climates, that can be identified and assessed with the indicators provided by the Corrupting Barrels model.

2. Corrupting Barrels survey

Conducting a team climate assessment – using desk research, team observations and interviews – as reported in paragraph 10.1 requires dedicated time from behavioural experts. It can be more appropriate and realistic to use a survey as a quick scan to assess team climate, for instance when a larger part of a banking organization needs to be assessed simultaneously and pockets of risk ought to be identified. This paragraph reports on the first use of a tailor- made survey, using the three team climate characteristics of the Corrupting Barrels model (see Figure 3.2 in Chapter 3), to assess team climate indicators that facilitating unethical behaviour.

2.1 Research question

This paragraph addresses the method that was used to examine the following research question:

Research question

6 *Is it possible to capture key aspects of a dysfunctional team climate that can facilitate unethical behaviour with a survey instrument?*

2.2 Approach

Based on existing validated scales, the 'Corrupting Barrels' survey was developed to assess team climates facilitating unethical behaviours. The survey contains twenty-seven statements that can be answered by desk members on a nine-point Likert scale (from 1= strongly disagree to 9 = strongly agree). The survey is included in Appendix E, which showed how the items that were used relate to the underlying theory and original items from the existing scales. *Error approach* was measured with three items, adapted from the Error Aversion Culture dimension by Van Dyck *et al.* (2005): "In this team people feel stressed when making mistakes", 'In general people in this team feel embarrassed after making a mistake" and "People within my team prefer to keep errors to themselves".

Nine items measured perceived justice, as a result of *outcome inequality*, adapted from the scale developed by Colquitt (2001). Three items measured distributive justice: "The reward that I receive (compensation, promotions e.g.) reflect the effort I have put into my work", "The rewards that I receive (compensation, promotion e.g.) are appropriate for the work I have completed" and "The rewards that I receive (compensation, promotion e.g.) reflect what I have contributed to the company". Interpersonal justice was measured by "My team manager treats me in a polite manner", "My team manager treats me with dignity" and "My team manager treats me with respect". Procedural justice was measured by "I am able to express my views and feelings about certain issues in this team", "I have influence over the outcome arrived at by promotion procedures in this team" and "My opinions are respected and valued within this team".

Finally, *(moral) climate* was measured with fifteen items adapted from the scale developed by Stachowicz-Stanusch & Simha (2013), which contains different sub-scales. Nine of these fifteen items indicate a principle based climate, categorized in 'independence', 'rules' and 'law and code' principle based. Independence principle based climate was measured by: "In this team, people are expected to follow their own personal and moral beliefs", "In this team, people are guided by their own personal ethics" and "Each person in this team decides for themselves what is right and wrong". Rules principle based climate was measured by: "Successful people in this team go by the book", "Successful people in this team strictly obey the company policies" and "It is very important to follow strictly the company rules and procedures here". Law and code principle based climate was measured by: "In this team, the law or ethical code of our profession is the major consideration", "In this team, people are expected to strictly follow legal or professional standards" and "People

in this team are expected to comply with the law and professional standards over and above other considerations". Instrumental climate was measured by three items: "People in this team are expected to do anything to further the company's interests", "There is no room for one's own personal morals or ethics in this team" and "In this team, people protect their own interest above other considerations". Caring climate was measured by three items as well: "In this team, our major concern is always what is best for the other person", "Our major consideration is what is best for everyone in this team" and "The most important concern is the good of all the people in the team".

The survey was sent to forty-three employees of a trading division within bank B. This trading division consists of six trading desks: desks A, B, C, D, E and F. The deep dive (using desk research, interviews and observations) focused on desks A and B as part of this division. All six desks trade in the same kind of products. Desks A and B are however in the same physical location or building. The other four desks are located in different cities and countries.

All employees of the six desks were asked by their middle manager (the manager of their desk heads) by email to complete the survey within two weeks. It was made clear to the employees that their answers would not be accessible by management or anyone else within bank B, and that they would be sent directly to DNB ensuring confidentiality.

2.3 Results

The survey was sent to forty-three recipients of whom thirty-two employees responded. This represents a total response rate of 72%. Employees of desks A and B - the desks that the supervisory deep dive focused on were also represented in this sample. The response rate was 86% (six out of seven desk members) for desk A and 71% (five out of seven desk members) for desk B.

Scale development

To facilitate the interpretation of composite scores, I ensured that for all items low scores indicate an unfavourable climate containing risk factors. To achieve this, six of the twenty-seven items were recoded to make sure that lower scores always indicate a less effective error approach, greater perceptions of outcome inequality, and a more dysfunctional moral climate. Of the six recoded items three items measure the error approach and three items measure instrumental climate. Appendix E provides an overview of all items as they were originally worded.

A factor analysis indicated that the individual items fell into four separate clusters representing meaningful constructs that relate to the three aspects of the Corrupting Barrels model. I conducted reliability analysis on these four clusters of items to see whether they could be represented as composite scales. The reliability of these four scales is indicated in Table 9.10.

Table 9.10. *The items and reliability indicators of four scales to assess relevant team climate indicators*

Corresponding team climate aspect - Corrupting Barrels model	Scales	Items		Cronbach's alpha
Error approach	Functional error approach	1	In this team, people feel stressed when making mistakes.*	.84
		2	In general, people in this team feel embarrassed after making a mistake.*	
Outcome equality	Just leadership	1	My team manager treats me in a polite manner.	.89
		2	My team manager treats me with dignity.	
		3	My team manager treats me with respect.	
		4	I am able to express my views and feelings about certain issues in this team.	
		5	I have influence over the outcome arrived at by promotion procedures in this team.	
		6	My opinions are respected and valued within this team.	
	Fair rewards	1	The reward that I receive (compensation, promotions e.g.) reflect the effort I have put into my work.	.98
		2	The rewards that I receive (compensation, promotion e.g.) are appropriate for the work I have completed.	
		3	The rewards that I receive (compensation, promotion e.g.) reflect what I have contributed to the company.	
Moral climate	Rule awareness	1	Successful people in this team go by the book.	.88
		2	Successful people in this team strictly obey the company policies.	
		3	It is very important to follow strictly the company rules and procedures here.	
		4	In this team, the law or ethical code of our profession is the major consideration.	
		5	In this team, people are expected to strictly follow legal or professional standards.	
		6	People in this team are expected to comply with the law and professional standards over and above other considerations.	

** = reverse coded*

The first scale 'Functional error approach' I used to assess the functionality of the error approach (corresponding with the Corrupting Barrels model). This scale, Cronbach's alpha = .84, consists of two items. As indicated above, these were recoded to make sure that higher scores indicate a more favorable error climate and lower scores always indicate a less favorable team climate ('In this team, people feel stressed when making mistakes' and 'In general, people in this team feel embarrassed after making a mistake'; both recoded) that correlated highly with each other, r = .73, $p < .001$. I originally intended to include a third item in this scale, (see Appendix B), but item 3 ('People within my team prefer to keep errors to themselves') was removed because it did not cluster well with the other two items.

The second and third scale correspond to the team climate aspect of outcome inequality in the Corrupting Barrels model. Perceived inequality, as I explain in Chapter 8, may facilitate unethical behaviour. In line with theory (see Chapter 8) on distributive justice (Greenberg, 2007) and interactional justice (Bies & Moag, 1986; Vecchio, 2000), unfair distribution of rewards and unfair leadership can drive perceived inequality. I created a second scale 'Just leadership' and a third scale 'Fair rewards' that assess there drivers of perceived inequality. 'Just leadership', Cronbach's alpha = .89, consists of the six interpersonal and procedural justice items which clustered together in the factor analysis: "My team manager treats me in a polite manner", "My team manager treats me with dignity", "My team manager treats me with respect", "I am able to express my views and feelings about certain issues in this team", "I have influence over the outcome arrived at by promotion procedures in this team" and "My opinions are respected and valued within this team". In 'Fair rewards', Cronbach's alpha = .98. I included three distributive justice items: "The reward that I receive (compensation, promotions e.g.) reflect the effort I have put into my work", "The rewards that I receive (compensation, promotion e.g.) are appropriate for the work I have completed" and "The rewards that I receive (compensation, promotion e.g.) reflect what I have contributed to the company".

Finally, I created a fourth scale 'Rule awareness' that indicates the extent to which the team climate is oriented on rules and codes, to indicate the risk of moral neglect in the team. This scale, Cronbach's alpha = .88, consists of the six 'rules and law and code principle based' climate items : "Successful people in this team go by the book", "Successful people in this team strictly obey the company policies", "It is very important to follow strictly the company rules and procedures here", "In this team, the law or ethical code of our profession is the major consideration", "In this team, people are expected to strictly follow legal or professional standards" and "People in this team are expected to comply with the law and professional standards over and above other considerations".

Of the twenty-seven survey items, ten did not fall into one of the four clusters as discussed so far. To explore the results for these ten separate items, I calculated the means of the separate items for each of the six desks and report these in Appendix F.

Profiles per team

To define team climate, I made team climate profiles by calculating the means of the four team climate scales for each desk. Table 9.11 lists these scale means per desk. The number of observations relative to the number of comparisons made is too small to test for statistical significance of mean differences. Figure 9.3 visualises the four scale-means plotted per desk.

Table 9.11. Means of four scale scores per desk

Corresponding team climate aspect – Corrupting Barrels model	Scales		Desk A	Desk B	Desk C	Desk D	Desk E	Desk F
Error approach	1	Functional error approach	6.1	6	6.3	5.8	6.6	4.5
Outcome equality	2	Just leadership	7.4	8	8.7	6.4	6.7	7.7
	3	Fair rewards	5.9	6.5	3.3	2.6	2.9	4.9
Moral climate	4	Rule awareness	8.4	7.3	8.8	7.3	7.3	7.8

The scale-means indicate specific team profiles that differ between the six teams. All teams show relatively high scores on rule awareness. Yet, each team has a distinct pattern of score ranges and means on the different team climate indicators. This reveals that there is no single team that shows evidence of an overall positive or negative team climate on all indicators. Instead, the scale means suggests that the teams differ from each other on specific team climate aspects. The most evidence of such differences is observed in team members' impressions of the error approach, and the fairness of the way rewards are distributed and of leaders. Here mean scores seem to be quite different per desk – despite the fact that all desks are part of the same organization and are subjected to the same formal guidelines and informal organizational culture. The Corrupting Barrels survey makes it possible to reveal these differences at team level, answering the sixth research question of this book affirmatively.

Lower scores indicate more risk, as they refer to a less effective error approach, greater perceived injustice in leadership and rewards, and a lesser extent to which the team is aware rules and codes. Lower scores lead to a smaller diamond-shape in the visualization (Figure 9.3).

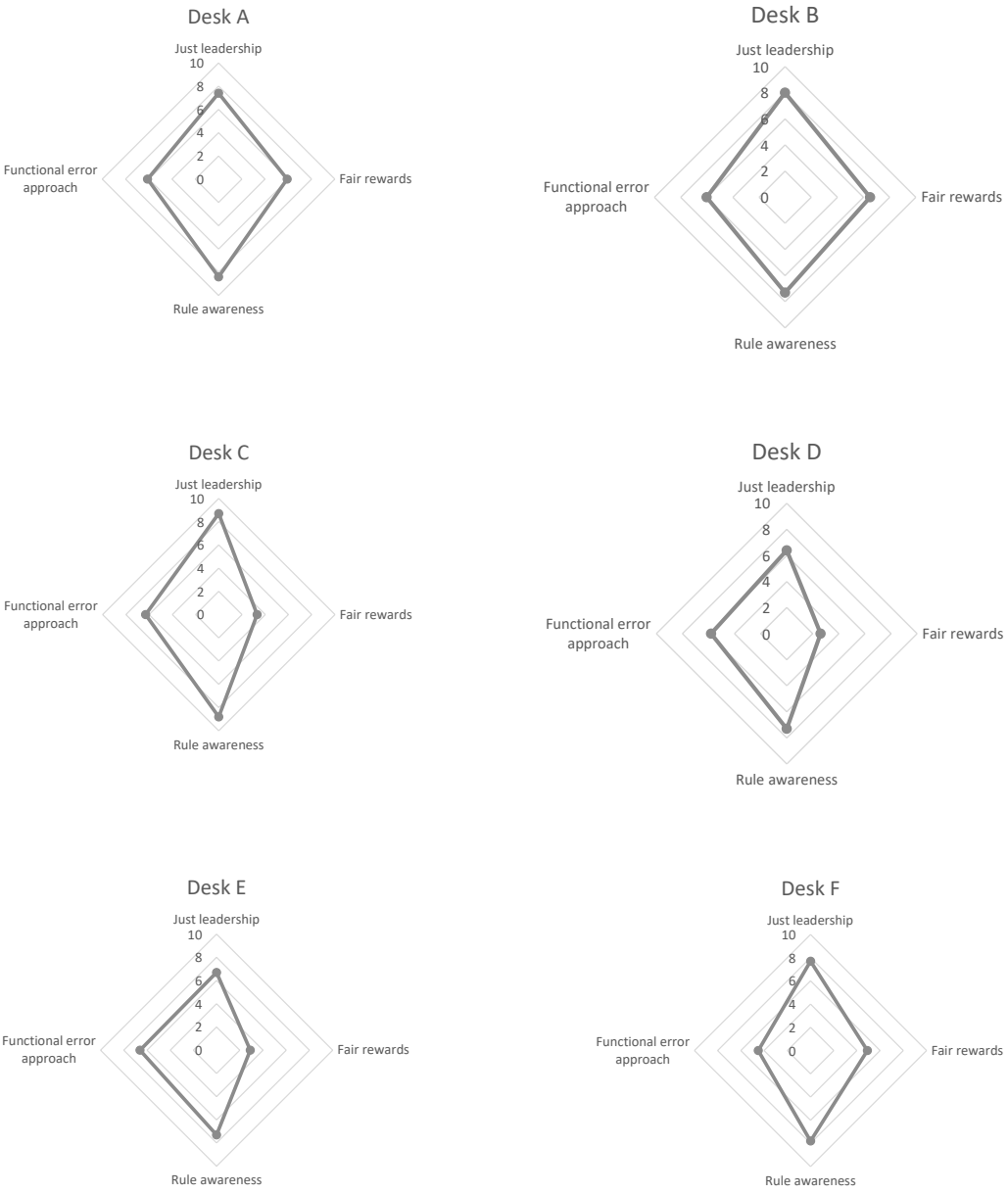
Of course, based on these self-reported team climate aspects alone, the occurrence of unethical behaviour cannot be predicted. However, plotting the scale-means creates specific team profiles that add value in the assessment of misconduct risk per team, because these profiles show differences on the team climate characteristics that have been shown to facilitate unethical behaviour in other contexts. For instance, Desks D and E show relatively low means on the 'Fair rewards' scale (M = 2.6 for desk D and M = 2.9 for desk E). This indicates a higher risk of frustration and envy at these desks, which have been documented as precursors for employee discontent and organizational misbehaviour. In Chapter 11, I elaborate on the value of the deep dive and survey results in identifying such team-level risk factors, and also consider the limitations of this analysis.

Profiles facilitating misconduct

The deep dive - carried out using desk research, observations and interviews – resulted in a characterization of team climates for desk A and desk B, with an estimated higher risk for unethical behaviour at desk A than at desk B. In this paragraph, I explore to what extent the team profiles for desks A and B, based on the survey results (which offer a quick and dirty diagnostic tool), are in line with the risk assessment resulting from the deep dive that is more labor intensive and less feasible for overall screening purposes. Does the team profile of desk A – based on the survey results - show a greater presence of team climate aspects facilitating unethical behaviour? First, the means of the scale measuring rule awareness show that there is a strong overall emphasis on rules and codes, which seems to be even higher at desk A, (M = 8.4, SD = .46), than at desk B, (M = 7.3, SD = .89). So, compared to desk B, it seems that at desk A has a slightly stricter emphasis on rules, although desk B is well aware of them as well. Furthermore, the team climate at desk A shows a higher perceived injustice than at desk B. The 'Fair rewards' scale, measuring fairness of rewards, also shows a lower mean for desk A (M = 5.9, SD = 1.80) than for desk B (M = 6.5, SD = 1.04). The 'Just leadership' scale, measuring fairness of leadership, shows a lower mean for desk A (M = 7.4, SD = .54) than for desk B (M = 8.0, SD = .49). This resonates with results from the deep dive, which showed a dysfunctional authoritarian leadership style at desk A – a highly demanding and controlling desk manager. A high expectation to strictly obey rules combined with unfair leadership, indicate a team profile of desk A that is to a greater extent facilitating unethical behaviour (for instance breaking rules to retaliate against unfair treatment by the deskhead), than the team profile of desk B.

All six desks have high means for rule awareness. Despite the strong rule awareness at all six desks, the survey results indicate at several desks dissatisfaction about the way rewards are distributed and fear to make mistakes. These climate aspects can risk unethical behaviour These survey results would therefore justify a deep dive review at the other desks as well (next to desks A and B).

Figure 9.3. *Team climate profiles for desks A, B, C, D, E and F*



2.4 Conclusions

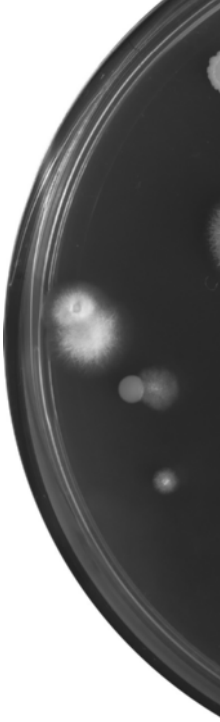
The 'Corrupting Barrels' survey can be used to define team climates and characterize different teams in the same organization. The six desks included in this analysis showed team profiles that differed on the three team climate characteristics that can facilitate unethical behaviour (measured by four scales: one on error approach, two on outcome equality / perceived fairness and one on moral climate). The Corrupting Barrels survey provides a first impression of potentially problematic characteristics of team climates. Using this survey to form a first impression of different team climates can be valuable for banks and financial supervision, for instance as an indicator for where to take a closer look to assess misconduct risk using a deep dive review.

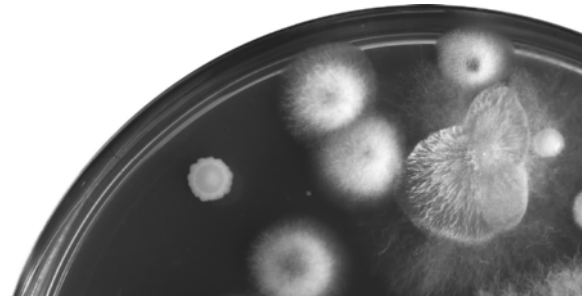
The survey shows that even when emphasizing the importance of rules and guidelines may prevent moral neglect and make people think more about the implications of their behaviors, this does not preclude the occurrence of negative emotions that result from perceived unfairness and a dysfunctional error climate. Yet these aspects of team climate form relevant risk factors for the occurrence of unethical behavior. So, a bank can focus on clarifying and stressing the rules and codes to increase rule awareness and influence the moral climate (as the outer ring of the Corrupting Barrels model, see Figure 3.2, Chapter 3) without curing all ills. At the task and relationship level of team climates (the inner rings of the Corrupting Barrels model) there can be a fear of making mistakes caused by the way errors are responded to, or jealousy between team members caused by how team members treat each other. Simha and Cullen (2012) explain that high rule and codes orientated climates can have positive effects on ethical behaviour, but that other aspects such as organizational context and the degree of competitiveness and volatility in the relevant markets can diminish this. In sum, making sure all know the rules is not enough to prevent unethical behaviour.

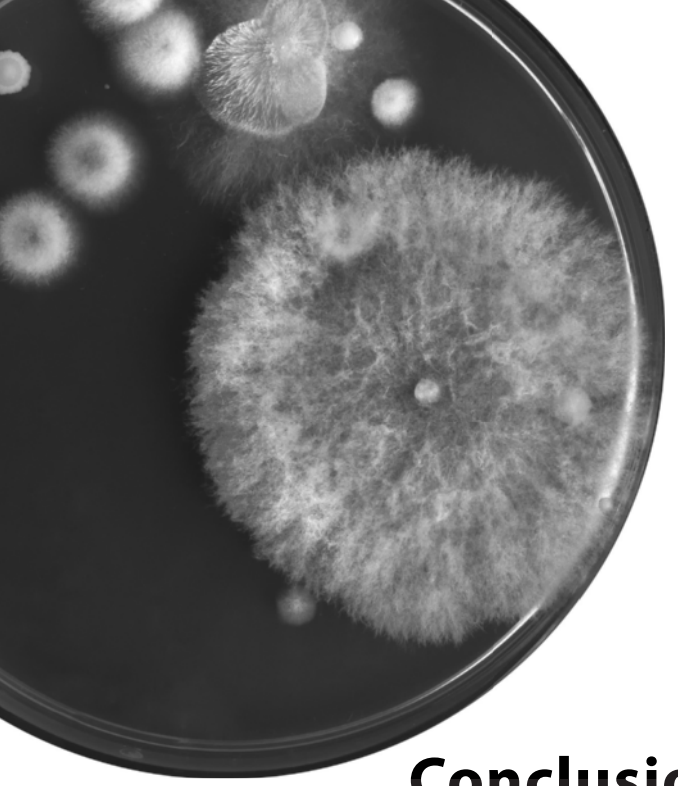
Based on these survey results alone it is hard to identify which team profiles actually predict future misconduct. This can only be established by following these teams over time to determine how different team climate aspects co-vary with observations of unethical behavior. Nevertheless, based on the theoretical basis and results of prior studies – that I reviewed in Chapter 8 - it seems safe to maintain that the risk of unethical behaviour within a team increases when the team climate profiles is characterized by lower scale means resulting in smaller diamond shape graphs (see Figure 9.3). Comparing the team climate profiles of desks A and B provides a first indication for this. When comparing the team climate profiles of desks A and B, differences between these team climate profiles suggest a greater presence of risk at desk A than at desk B – as there is more perceived injustice of leadership and rewards at desk A. This is in line with the observations made with the deep dive assessment I presented in paragraph 9.1.

No one indicator of culture or climate can be seen as an absolute identifying standard for misconduct risk. Indeed, the extent to which employees are aware of the importance of rules and codes seems very high across the board, and does not clearly distinguish between the six teams and their climates. The scale used to assess rules orientation shows the highest average mean over all six desks of all other scales and items (*M*average = 7.8 on the 9-point Likert scale).

So, every employee at the six desks included in the analysis is aware and can indicate that he or she has to comply to the rules and codes. This team climate aspect does not distinguish the six team profiles from each other. Apparently, the bank has made sure these rules and codes are known to everyone as an organizational level provision – which is to be praised. However, since the team profiles vary on other characteristics that facilitate unethical behaviour, it is fair to say that awareness of rules and codes is a necessary condition but does not by definition prevent all dysfunctional climate aspects that can contribute to unethical behavior.

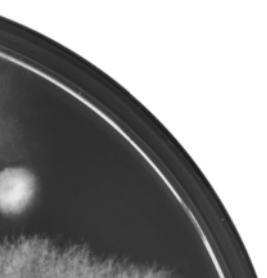






Part IV
Conclusions and practical implications for bank and financial supervisors

Chapter 10
Conclusions and practical implications



Chapter 10
Conclusions and practical implications

The current response to misconduct from banks and financial supervisors is insufficiently effective in preventing future misconduct. In the first Chapters I presented misconduct as a costly and continuous problem, that is yet to be addressed effectively. I argue that a team climate perspective is needed to identify and target the root causes of unethical behaviour, and herewith mitigate misconduct risk.

The team climate perspective is a blind spot for banks and financial supervisors. Attempts to prevent unethical behaviour focus on organizational level (i.e. values, culture change programs) or individual level (i.e. ethical recruitment tests, disciplinary measures). With Study 1, I showed that a significant bank was missing the team climate perspective in its own reporting and analysis of its misconduct cases. Team climate, that harbours social psychological root causes of unethical behaviour, is not a perspective used by banks when analysing misconduct. So, for banks, team climate is simply not in sight.

Financial supervision is in the position to put the team climate perspective in scope by asking banks to assess team climates and analyse the root causes of misconduct at team level. With Study 2, I showed that a supervisory request of behavioural data at team level remained unanswered. A significant bank was unable to reproduce data related to team climate, of the teams within its high integrity risk trading business. Furthermore, the supervisory request of a root cause analysis resulted in the bank analysing a number of incidents, but it did not result in the bank acquiring any insight in or deepened understanding of the way team climate facilitated the unethical behaviours, needed to prevent future misconduct. So, an external supervisor asking banks to focus on team climate is insufficiently effective.

If team climate is a blind spot for banks and their financial supervisors, and supervisory requests for team climate analysis are insufficiently effective in eliminating that blind spot, there is a logical next step: tools have to be provided to analyse team climate as an internal or external supervisor. I aimed to provide a practical approach to do so. With Study 3, I showed that it is possible to define team climate and characterize teams within the same organization on the three 'Corrupting Barrels' team climate aspects that facilitate unethical behaviour: ineffective error approach (relating to the 'Functional error approach' survey scale), outcome inequality (relating to the 'Fair rewards' and 'Just leadership' survey scales) and dysfunctional moral climate (relating to the 'Rule awareness' survey scale). By combining desk research, team observations, and interviews, it is possible to effectively define team climates, identify meaningful differences in team climate characteristics that are known precursors of organizational misbehavior. The Corrupting Barrels survey is a less labour intensive way to provide a first impression of team climate characteristics. The use of the survey for my analysis is a first attempt to get this impression and although my analysis shows that the survey can serve this purpose, it also revealed opportunities to develop the survey further in future research. The instrument can be perfected and its predictive value

needs improvement. However, the first step in developing and conducting the survey is taken successfully. So, the data I presented from the deep dive review and survey attest to the validity of my analysis and suggests possible ways of taking up a practical approach in preventing misconduct by defining and assessing team climates.

1. Defining team climates: identify root causes of misconduct

Two-step approach

Based on my literature research and the different data sources examined and reported here, I propose to mitigate misconduct risk with a two-step approach (see Chapter 3). The first step, as I will explain further in this chapter, is to define team climate and identify root causes of misconduct. Based on my analysis, I suggest to further explore the use the Corrupting Barrels model and framework as a first step to analyse team climates in a structured and evidence based way.

The second step is that banks improve team climate on the back of that analysis, by targeting the team level root causes of misconduct. I propose to develop an active approach for targeting these root causes based on insights from social psychological theory and research on team climates to target team climate aspects that facilitate unethical behaviour, as I will discuss in paragraph 10.2.

Several officers and roles within banks are often involved when misconduct occurs. Next to the business and its leaders of the area where the misconduct occurs, legal departments or internal investigation units, human resources, compliance, risk management and internal audit usually are involved. Each play their own part in dealing with misconduct: leaders and staff within the business are responsible for (i.e. the first line of defense, in the three line of defense model) assessing and mitigating their misconduct risk. Risk management, compliance and HR challenge the business on their management of misconduct risk and support them in their prevention of misconduct (i.e. second line of defense). Internal audit is, as a third line of defense, in the position to reveal misconduct risk through audit reviews, and can escalate this to board level of the bank. Internal audit and the supervisor are, as internal and external supervisor, independent of the business and able to put root causes of misconduct in team climates on their agenda (in contrast to the second line of defense which tends to be more dependent on the overall business agenda for their impact on day-to-day practices). The internal and external supervisor are best placed to select the areas within a bank themselves to identify root causes of misconduct at team level, and both have a degree of power to force the business to improve team climates actively on the back of that identification. I argue that because of this independence and escalating and disciplinary powers, especially internal and external supervision can have significant impact on the prevention of future misconduct by using the assessment framework, especially in (areas within) banks that are unable or unwilling to address misconduct risk themselves. Internal audit and the supervisor are in a unique position to eliminate that blind spot for team climates within banks by revealing misconduct root causes within team climates, and to force banks to improve these team climates in order to mitigate misconduct risk.

The team climate perspective in examining misconduct offers a relatively new perspective for internal audit and financial supervisors (see Chapter 2, paragraph 2.2). As a senior supervisor of behaviour and culture in the banking industry at DNB and later as head of an internal audit team dedicated to identify behavioural risk, I argue that there are at least three important success factors for internal or external supervisors to embark upon team climate assessments effectively.

The first success factor is that team climates are assessed explicitly by a team that is dedicated to assess and mitigate these specific risks. When financial supervisors and internal audit groups commence with supervising behaviour and culture, they often debate on whether to assess behaviour and culture as a specific topic, and whether - in terms of organizational structure - a separate dedicated team on the topic is justified. Although behaviour and culture is part of any supervisory assessment, addressing and assessing behaviour and culture (including team climate) explicitly, gives a strong message to the supervised banks and business areas that the blind spot for this topic is creating risks that need to be mitigated. Positioning behaviour and culture audit and financial supervision as a specific risk area should therefore be more effective in mitigating risks related to behaviour and culture, than blending in this new perspective with more familiar (and for some more therefore comfortable) risk areas. A specific audit or supervisory team dedicated to behaviour and culture should help achieve this explicit positioning of behaviour and culture risks.

The second success-factor for effectively mitigating behaviour and culture risk is to resource this team with audit or supervisory professionals that have experience with assessing behaviour and culture, and have an expertise in this field. To define team climate and assess misconduct risk requires a structural method (such as the framework discussed in the next paragraph), and sound professional judgement built by that experience and underlying expertise. The expertise – an academic background in psychology for instance - adds to the credibility that is needed to land the messages effectively with the leaders that have to impact or change their businesses and the team climates within.

The final success-factor I highlight is to use a specific assessment approach, that often differs from other audit and supervisory assessment (more control oriented) approaches. To define team climate and its root causes of misconduct, it is important that internal and external supervisors assess reality within teams: what is the day to day reality for people in the team? What is their professional context and how do they perceive this context? It requires an interactive and realistic assessment, that cannot be fully captures with a standard checklist. To define team climate a combination of qualitative and quantitative instruments is most effective (Raaijmakers, 2015; p. 78 on triangulation in a supervisory approach).

The assessment framework

The assessment framework, that I used for my analysis reported in Chapter 9, offers an effective triangulated and structured approach to define team climate and identify root causes of misconduct. As presented in Chapter 9, the framework includes five instruments: a two- pager

on the assessment framework, a list of documents that can be requested for desk research, an interview format, an observation format and a survey. The instruments as included in Appendices A t/m E offer a concrete example: these are the exact instruments as I have used in my analysis reported in Chapter 9, applied to the context of the banking trading business. However, they are not meant as a fixed or prescriptive method for all contexts: I do not present the instruments as definite and suitable for all. To embark upon defining team climates to identify misconduct risk, three underlying principles of the assessment framework presented are to be considered. First, the focus of the assessment should be at team level, second a combination of qualitative and quantitative instruments is needed, and third, it should aim to address indicators of the three categories of root causes as presented by the Corrupting Barrels model (ineffective error approach, outcome inequality and dysfunctional moral climates). By using an assessment approach in line with these three principles, team climate and its root causes for misconduct can be defined effectively.

2. Improving team climate: mitigate misconduct risk

Once a team climate is defined, the patterns within that team climate that could facilitate unethical behaviour can be identified. These patterns concern the error approach in the team, outcome inequality and the overall moral climate. These root cause categories can be improved by the bank with an active and targeted approach. Before I suggest improvements within these specific categories, I explain the importance of leadership in improving team climates.

2.1 Leadership is key

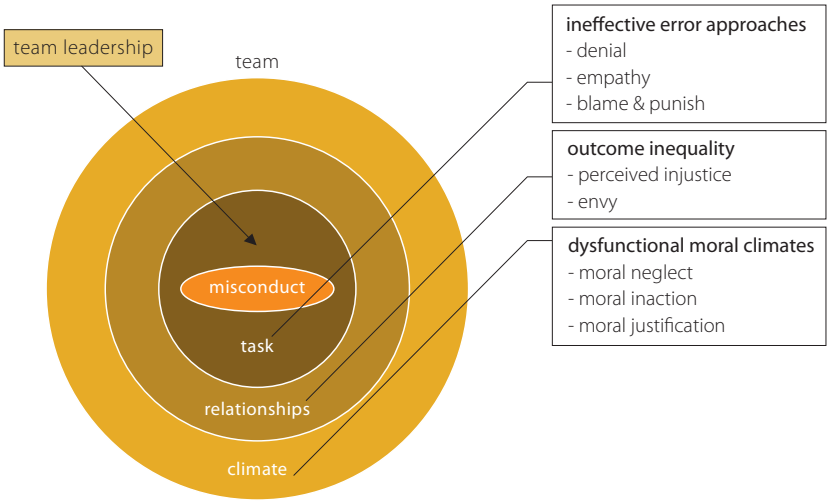
The common denominator of all improvements to team climates is leadership. Team leadership is an important lever in improving team climates and thereby mitigating misconduct risk. Team climates and leadership are interconnected, in fact, team leaders are in a way embodiments of the teams they lead (Haslam *et al.*, 2013). Haslam, Reicher and Platow (2013) have defined leadership as being the ingroup champions, who help shape and reaffirm social collective norms in the group. According to their social identity approach to leadership, heads of trading desks live the values of their teams and thus make them reality.

Team leaders impact team climate in all facets, through their actions, inactions and choices (see Figure 10.1). Dysfunctional team climates, facilitating unethical behaviour, are not only caused by ineffective leadership. I argue however that failing leadership is an important risk factor and can frustrate and lead astray even the best and most morally upright employees. This also implies that through effective leadership, team climates can be improved and misconduct risk can be mitigated.

To improve ineffective error approaches team leaders can stimulate open communication about errors and create a learning climate (Rybowiak *et al.*, 1999; Cannon & Edmondson, 2001).

Leaders can do this by openly talking about errors in the organization, including their own failures, and present these as a learning opportunity. Next to modelling desired behaviour, leaders can react to errors consciously and consistently in a way that minimizes concerns employees might have about consequences for their status in the team (Edmondson, 2003). Finally, an 'error management instruction' that explicitly encourages to make errors and emphasizes the positive information feedback of errors to enhance learning, has been shown to have positive effects on performance of people because they are more inclined to discuss and learn from their errors (Keith & Frese, 2008; Heimbeck *et al.*, 2003).

Figure 10.1. *Leadership impact on team climates*



For managing negative emotional consequences of outcome inequality, as perceived injustice and envy, team leadership is an important channel too. As the survey results showed, unfair leadership affects teams apart from the perceived fairness of reward distribution. The six desks assessed showed the largest variation on these two scales – 'Fair rewards' and 'Just leadership' – whilst all six desks are part of the same organization. This illustrates how team climates and team leadership influence these drivers of perceived injustice. Furthermore, leadership can reduce envy in the workplace (Duffy *et al.* 2008). When a team member envies another team mate, a counter managerial perspective clarifying that the envious team member is behaving 'bad and unprofessional' can be effective (Tripp & Bies, 2007). If inequality within a team elicits perceived unfairness, sensitivity in interpersonal treatment of the team leader helps team members to cope better with the inequality (Tyles & Bies, 1990). Team leadership is an effective lever to improve dysfunctional moral team climates. Moral exemplars in leadership roles have a positive effect on moral team climate (Mayer *et al.*, 2012; Moore & Gino, 2013). Research on ethical leadership (Brown *et al.*, 2005) shows that next to role modelling, team leaders can promote moral behaviour through two-way communication, reinforcement and decision making.

To activate leadership as a key lever in improving team climates, banks and financial supervisors need to hold leadership accountable for healthy team climates and review to what extent senior leaders have assessed team climates with this objective. Has senior leadership a clear picture of which teams within their banking organization have increased misconduct risk? This includes inherent misconduct risk - based for instance on the nature of their business and clients and (recent) changes within their business or organizational context – and misconduct risk that comes forth from dysfunctional team climates. Did senior leaders ensure that they receive the behavioural signals and data needed for them to make that risk assessment at team level? And, to what extent has senior leadership acted to improve leadership where it is needed? From my own personal experience as an (external) supervisor, (senior) leaders often have some idea about the leadership quality within their scope, but underestimate the risk of certain leadership behaviours. I have encountered in my supervisory and audit work many dysfunctional team climates – since I work risk-based and focus on the places within banks that need improvement most – and often discussed my findings with senior leaders. I observed that on the one hand they acknowledged the accuracy of my findings, but on the other hand had to be 'educated' about the risks these indicated and needed to be actively convinced to act upon these findings.

- *An illustrative example from supervisory practice (Nr. 18, see Table 2.1)*

  The results of the team climate assessment of desks A and B as reported in Chapter 10 – using desk research, team observations, interviews and the survey – was disclosed to and discussed with middle and senior management. Desks A and B both had a desk leader; who reported to the middle manager. The middle manager reported to the senior manager. First a 1,5 hour meeting with the middle manager was organized to discuss the assessment findings, and two days later a 1,5 hour meeting with the senior manager accompanied by the middle manager was organized to do the same. A slide deck with the main results was used to facilitate the dialogue. During these meetings, the middle manager and senior manager recognised and acknowledged the assessed team climates and the identified patterns that facilitate unethical behaviour. They recognised the identified patterns, but had underestimated the risks of these team climates. An example is the senior manager calling the desk head of desk A, who clearly displayed a dysfunctional leadership style, a "high potential leader" who only needed some coaching to work on his 'relationship management'. The assessment results however indicate a dysfunctional leadership style, which should make the desk head 'low potential' for a higher management position – especially in a high integrity risk team that deals with such large transactions. This conclusion was accepted by senior management after it had been explained. Subsequently, financial supervision discussed with senior management the steps they were required to take to improve the risky patterns that were identified.

Courageous leadership is needed for team climate improvements to succeed, in which team leadership, middle and senior management are aligned. Senior management should have the courage to support leadership changes that are needed to achieve team climate improvements,

even if the financial performance of the teams and leaders is excellent. Avoiding to change dysfunctional leadership, and allowing that team members are exposed to failing guidance, invites the recurrence of misconduct within banking.

2.2 Improve the 'Corrupting Barrel' team climate characteristics

Below, I discuss ways to improve the team climate characteristics that can facilitate unethical behaviour: ineffective error approach, outcome inequality and dysfunctional moral climates.

Improve error approach

Leaders within banks can improve error approaches in teams, and herewith improve team climates and mitigate misconduct risk (Frese & Keith, 2015). This involves an increased awareness and deepened understanding by (senior) leaders of the variation in error approaches and their potential detrimental effects. Second, it requires an active approach to assess the current error approach in a team, and in line with the assessment findings, improve the way a team deals with errors. An explicit example of such an improvement is to target an ineffective error approach, by creating the possibility for 'blame-free' reporting of errors and constructively responding to such reports (Edmondson, 2003). This should help stimulate more open communication and create a learning climate (Rybowiak *et al.*, 1999; Cannon and Edmondson, 2001). Provisions can be made to facilitate the identification and analysis of errors (Raaijmakers, 2015; see Chapter 11 on error approaches that I wrote).

Prior research suggests that an effective way of facilitating the identification and analysis of errors is to combine technical and social provisions. This can be done, for instance, by building an information or registration system for errors (technical change), as well as investing in dialogue on errors (social change) (Cannon & Edmondson, 2005). Investing in technical solutions, for instance, by building better information systems, may seem most feasible as a first step. Nevertheless, to be effective such technical improvements need to be accompanied by social changes that induce feelings of safety and trust in employees allowing them to openly discuss conditions that may contribute to the occurrence of errors. Cannon and Edmondson (2005) recommend that organizations set aside space and time for relevant employees to evaluate errors as a team, and to hire or develop skilled facilitators to ensure a learning oriented dialogue is held during these meetings. Another suggestion is to invite employees with diverse backgrounds to attend these evaluations. Involving people with different views or types of expertise increases the quality of the discussion and strengthens the learning potential of the evaluation. In doing this, it is important to consider the fact that some errors are more easily discussed than others. Errors with severe consequences are more likely to be considered for formal evaluation or to be discussed informally. Nevertheless, openly discussing 'minor' errors may seems less threatening and can help the bank communicate the importance of considering all errors made, and conveys the willingness to learn from errors instead of denying them. Evaluations of errors should not only address the 'big ones'; routinely considering the learning potential of smaller errors contributes to the development of an error management culture (Sitkin, 1992; Homsma *et al.*, 2007).

Reduce outcome inequality

Another improvement of team climate in order to mitigate misconduct risk, is to reduce outcome inequality. This preventive step that could be taken by the banking industry, supported by its regulatory context, could entail to reduce income differences within teams and banking organizations (Vecchio, 2000). An inspiring example was given in 2015 by Dan Price, CEO of Gravity Payments (a credit card processing company). Price used his own income to raise the salary of his employees up to a minimum of 70.000 USD a year and hereby reduced the income inequality within Gravity Payments (Cohen, 2015). However, restructuring incentives seems to be a step banks do not easily take. A study by Boersma (2014) evidences this assumption. Boersma analysed developments in communications on remuneration and target structure of ING Bank, ABN AMRO Bank, Rabobank and SNS Bank. These four significant Dutch banks hold about 80% of total assets of the Dutch banking sector and therefore are representative of the sector in the Netherlands (Commissie Structuur Nederlandse Banken, 2013). The study showed that over the seven years that followed the start of the financial crisis in 2007, the way these banks publicly communicated about their remuneration structures did not show any changes. Their annual reports did not report changes in the development of significant compensation aspects such as the balance between financial and non-financial targets, the variable salary for the executive board and distribution of target criteria based on individual and/or group performance. Especially in those seven years after the start of the financial crisis, the societal disbelief and dissatisfaction with the banking sector called for a reconsideration of incentives within the sector. Nevertheless, Boersma showed that in their external communications, banks did not demonstrate sensitivity to their increased reputational risk regarding their remuneration. To prevent future misconduct it is however essential that banks are willing to reconsider their performance management and incentive schemes (Bies & Tripp, 2001). An alternative for setting quantitative performance and connecting bonuses to obtaining these goals, is to make teams responsible for reaching set performance objectives. Let teams figure out how they will reach these objectives, by doing the right thing and making use of different roles and capabilities within the team. Banks will have to attend to procedures and leadership interactions as these can drive perceived injustice (measures by the 'Fair rewards and 'Just leadership' survey scales).

... and manage its emotional consequences

Next to reducing actual outcome inequality, managing the emotional consequences of inequality improves team climates in a way that prevents future misconduct. Banking leaders could start as of today to reduce the negative emotional consequences of outcome inequality. Emotional consequences such as perceived injustice and envy can be managed in a way that mitigates the risk of these emotions resulting in unethical behaviour. Managing these emotional consequences effectively by treating staff fairly ('Just leadership') requires first an increased awareness and deepened understanding by (senior) leaders of antecedents of these emotions and their possible detrimental effects. In the banking industry, performance management and reward allocation are assumed to increase motivation and overall performance. These systems could however result in outcome inequality with emotional consequences that can drive unethical behaviour. Seemingly the banking industry assumes that the motivational benefits

of reward allocation outweigh the emotional burden of unequal outcomes in performance management and reward allocation. Recent costly misconduct cases (such as the Wells Fargo case) call for a fundamental discussion on how staff performance and motivation is best driven, and suggest the industry revisits its incentive assumptions.

Preventing future misconduct driven by outcome inequality requires an active approach to assess the emotional consequences of inequality within a team and improve fairness of leadership and the way emotional consequences are managed by the team-leader, the team itself and the individual team members. An explicit example of such an improvement is to inform employees of likely outcomes and adhere to fair procedures. In this way, employees feel that they are treated respectfully even when their outcomes are less favourable than those of others (Duffy *et al.*, 2008; Cohen-Charash & Mueller, 2007). Another way to reduce negative emotional consequences of inequality within a team is to increase team identifications (Duffy *et al.*, 2012). This way, team undermining norms are decreased.

Improve moral team climate

Improving dysfunctional moral climates within teams to mitigate misconduct risk requires first an increased awareness and deepened understanding by (senior) leaders of these moral climates, their drivers and their possible detrimental effects on ethical behaviour. External supervisors who know about these risks, or internal supervisors who have been trained to identify such risks can plan an important role in this process of raising this awareness amongst senior management.

Second, it requires an active approach to assess the moral climate within a team, and in line with the assessment findings, improve these moral climates. A tangible example of an activity to dampen moral neglect is to heighten one's sense of moral self-regard within a team (Moore & Gino, 2013). This can be done with certain prompts that can be woven into the professional daily context. Desai (2011) showed that team members behave more ethically after exposure to a morally relevant quote as part of an email signature. Another active approach to improve climates of moral neglect and moral justification is to explicitly invite teams and their members to consider the moral content of their business. Climates of moral neglect and moral justification can be challenged by creating dialogue on this moral content during team meetings, or including explicit moral messages in leadership communication.

Also, to impair moral justification within teams, Moore and Gino (2013) suggest to expand one's circle of moral regard. Unethical behaviour can be facilitated by a narrow circle of moral regard, for instance putting one's own family and direct colleagues first. This narrow circle of moral regard can be enhanced by a caring climate where each other's wellbeing are of the greatest concern to the team (Simha & Cullen, 2012). Caring climates have been established in prior research as climates that can counter the adherence to moral principles, and can invite organizational misbehavior, even among workers who are aware of organizational rules and guidelines. For instance, team members in a caring climate can be tempted to cover up each other's poor behaviour, eventhough this poor behaviour is breaking rules. By inviting team

members to consider customers and clients as part of their circle of moral regard, through framing and communication by team leadership for instance, justifying immoral actions towards them is less likely (Laham, 2009).

A climate of moral inaction can be improved by taking seriously any comments thus raised, and reconsidering existing business practices accordingly. Here positive management framing can be effective, where the team members that took action in case of observing immorality are rewarded and their behaviour is rewarded as being 'good and professional'.

2.3 Conflicts to resolve

I argue that there are three areas of conflict that are likely to emerge when banks work on improving team climates, and require a bank to think through these areas and take a stance or choose what its priorities are.

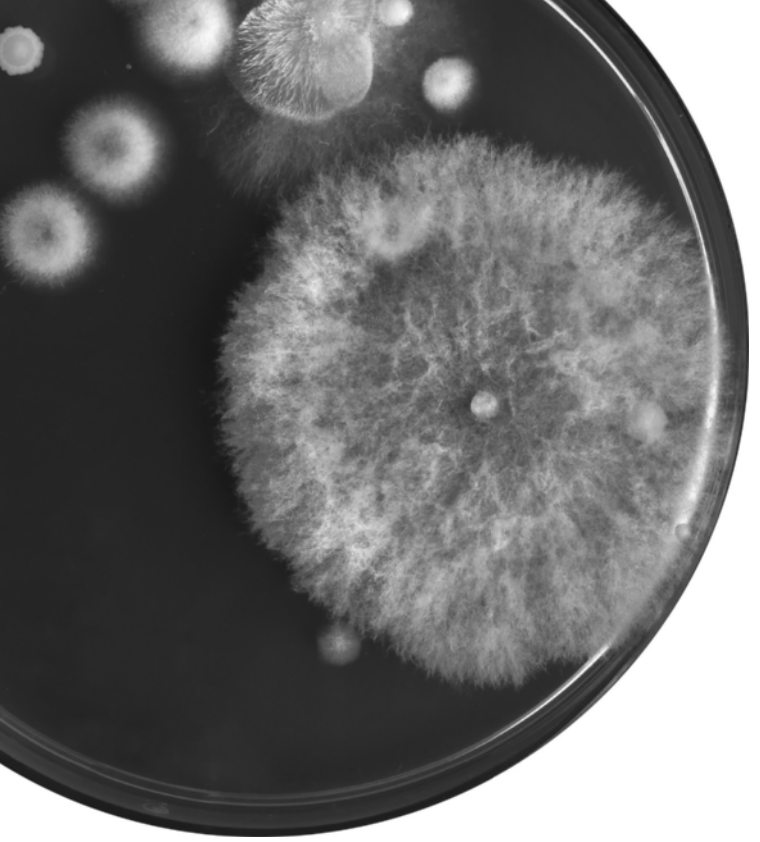
The first area of conflict concerns the contradiction between a strong control environment and an openness about errors. Say, hypothetically, that a bank employee is checked on the completeness and quality of the forms (s)he fills in to do a transaction or serve a customer. And that the outcome of this control step influences his performance review. The employee will, to protect her/his good performance, be less open about a mistake that might hav been made in an environment where the emphasis is on controls. At the same time we know that lack of openness about errors facilitates future unethical behaviours. To check up on people's actions, often stimulated by financial supervision, is a strategy many banks take with the aim to control behaviour of their employees (see Chapter 3 on common responses of the banking industry to misconduct). This controlling strategy comes with a price: by a decreasing the likelihood that employees are open about errors, the risk of misconduct increases. And again, the imposition of (deterrence) sanctions generally undermines employee trust and reduces rule compliance (Mooijman *et al.* 2015). So, it is likely that trusting employees to do the right thing until proven otherwise, and only disciplining them when needed, is a strategy that is less costly than the controlling strategy.

A second area of conflict concerns the contradictions between performance and compliance goals. During a supervisory interview a trader indicated that he felt the bank communicated two contradicting expectations to him: to act ethically, and to make profit. He was in his mind not able to reconcile these two expectations. Regardless of whether this is possible in practice – making money by doing the right thing – he felt the goals he had to meet were not in line with each other. This perception – in being forced to prioritize performance over ethics or to sacrifice performance to behave ethically - influences his individual (ethical) behaviour and therefore creates misconduct risk. I often see management structures that strengthen perceptions like these, where a bank employee even has two different managers to report to: a 'performance' manager and a 'control and compliance' manager. Both these objectives only come together at the level of the bank employee at the front line, who has to make decisions that meet contradictory expectations from

both managers. Leaving it up to the bank employee, who faces clients and customers, to marry up performance with compliance goals in his daily interactions and transactions makes it difficult to do what is required at all ties and invites unethical behaviour. Could it be that combining performance with compliance goals more explicitly resulting in integrated guidelines, instead of separating these objectives, is a strategy that is less costly in the long run?

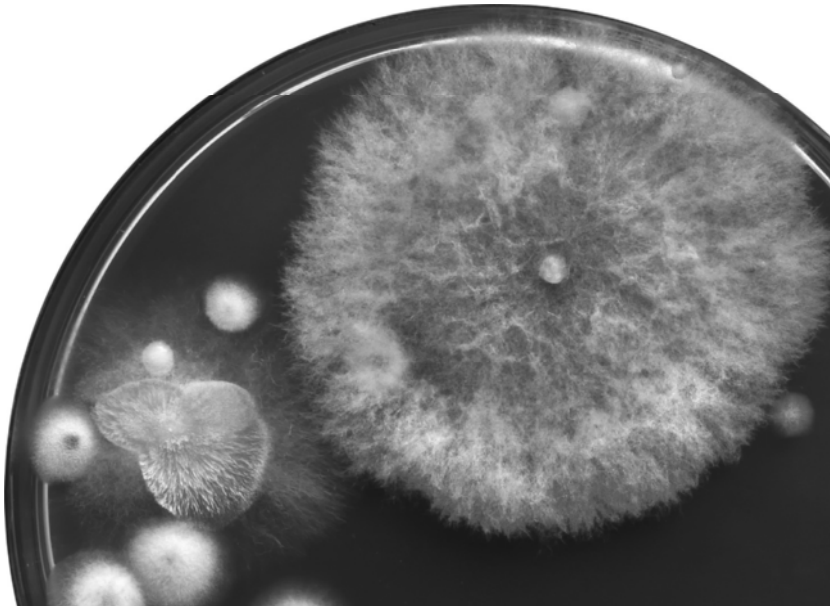
A third area of conflict concerns the contradictions between a legal and a learning approach regarding misconduct that has taken place. As revealed in the responses that are common to banks in Chapter 3 – paragraph 3.2 – the legal paradigm prescribes containment in handling misconduct cases. However, the common practice of not sharing information on the cases also leaves colleagues in the dark about what happened exactly or prevents them from realizing why this was wrong. This impairs the ability of the bank to learn from prior experiences with misconduct cases. To prevent misconduct it is vital to be able to analyse the specific circumstances and aspects of such occurrences. Legally (especially when lawsuits are involved) it can be costly to admit that the organizational and team context had a part in the origins of the unethical behaviour. Could it be that owning up to that organizational accountability to be able to prevent next cases more effectively, is a strategy that is less costly in the long run?

I strongly believe that these contradictions need to be addressed when aiming to improve team climates. Senior leadership should be asked questions about these areas of conflict. Questions on how their disciplinary sanctions and containment strategy after misconduct occurred, take into account the necessity to learn from what happened. Questions on how their performance management is married up with compliance objectives. Questions on how increased controls are managed in a way that stimulates openness about honest mistakes. Questions like these raise the awareness with senior leadership on these relevant contradictions, and enable them to make more productive decisions in their preventive approach of misconduct.



Part IV
Conclusions and practical implications for bank and financial supervisors

Chapter 11
Limitations and future research



Chapter 11
Limitations and future research

Before elaborating on the limitations of my analysis, and the opportunities I see for future research, I first sum up the strengths of the analysis reported here. Both strengths and limitations are listed in Table 11.1.

Table 11.1. Strengths and limitations

Strenghts	Limitations
1. Offering an applicable 'Corrupting barrels' model and framework at team level, that adds value in preventing future misconduct as evidenced here. 2. This model and framework is based on theoretical analyses using current research from organizational and social psychology, 3. and empirical analyses using supervisory, thus publicly inaccessible, data gathered at 'too-big-to-fail' banks including interviews at CEO level. 4. Suggesting a concrete and practical two-step approach at team level to prevent future misconduct.	1. My analysis did not provide conclusive evidence of the predictive value of the 'Corrupting barrels' model and framework for the actual occurrence of misconduct in certain teams. 2. My analysis did not intend to evidence the extent to which use of the assessment framework offered actually prevents future misconduct in teams. 3. The model addresses three team climate characteristics at task, relationship and climate level: there might be other team level root causes of misconduct. 4. Limited survey sample size that limited possibilities for statistical analysis.

1. Strengths of this analysis

Offering an applicable model and framework

My analysis started with a careful consideration of the continuous problem of misconduct in the banking industry, and the current response from banks and financial supervisors that is insufficiently effective in preventing future misconduct. I introduced the Corrupting Barrels model to offer a framework for analysing social psychological root causes of misconduct within teams, and suggested a two-step approach of first analysing team climate on these root causes and second improve team climate to prevent misconduct. This two-step approach is further described in Chapter 10, paragraph 10.1 (define team climate) and 10.2 (improve team climate).

Based on theoretical and empirical analysis on unique supervisory data

Next I conducted a theoretical and empirical analysis. The theoretical analysis focused on the three social psychological root causes of unethical behaviour that the Corrupting Barrels model refers to: ineffective error approach, outcome inequality and dysfunctional moral climate. I have analysed the current theoretical psychological research on these mechanisms, resulting in a definition (the 'what') and an elaboration on the way ('the how') these mechanisms can facilitate unethical behaviours. The empirical analysis, on data acquired through supervisory assessments, combined qualitative and quantitative methods. The data used is gathered in a supervisory context and therefore unique and not publicly available. It is gathered at significant 'too-big-to-fail' banks

and includes for instance confidential litigation reports, internal investigations of a misconduct case and illustrative examples of supervisory interviews with CEO's, senior and middle managers of trading businesses and traders. In three separate empirical studies I was able to show that team level root causes of misconduct are currently a blind spot for banks and supervisors (Chapter 5), that asking banks to analyse team climate root causes of misconduct is insufficiently effective (Chapter 6), and that the framework offered adds value in identifying team level risk factors that can help prevent future misconduct (Chapter 9). The assessment framework presented is able to characterize team climates that differ in terms of their risk of facilitating unethical behaviour. In Chapter 10 I discuss the conclusions of this empirical analysis.

Suggesting a concrete two-step approach at team level to prevent misconduct

My analysis is a first illustration of how banks and financial supervisors can define and assess team climates, in order to identify and improve aspects that facilitate unethical behaviour. It demonstrates what the added value is of analysing and improving team climates to prevent future misconduct, in addition to the current preventive approaches that primarily address individual (i.e. KPI's and disciplinary measures) and organizational (i.e. behavioural codes and corporate values) levels. In Chapter 10 I provide concrete suggestions for a two- step preventive approach of defining and improving team climates. With my analysis, I want to highlight that this team perspective, that is currently missing in current banking and supervisory practices, is a perspective that banks and financial supervisors can use in their approach to mitigate misconduct risk. The analysis of team climate results in valuable information that can clarify which teams within the same organizational context (and for instance showing the same rule-awareness) represent organizational units with increased misconduct risk.

2. Limitations of this analysis

Predictive and preventive value

Predicting in which team misconduct will occur, would be worth gold in the banking industry. If it were possible to reliably predict where unethical behaviour would occur, banks and financial supervisors would be able to target these places specifically and prevent misconduct effectively. The Corrupting Barrels model and assessment framework used in my analysis, need to be developed and tested further to validate its actual predictive value.

My analysis not only targets team climate as an additional factor in the emergence of misconduct, it also results in a suggested preventive approach of identifying and targeting root causes of misconduct. The current analysis constitute a first attempt to apply insights from social psychology to define and assess team climate aspects that increase the risk of misconduct. To what extent this two-step approach will actually allow supervisors and managers to impact team climate in a way that the misconduct risk is mitigated was beyond the scope of my current investigation. The long term impact of a preventive approach along the lines suggested here, to actually prevent unethical behaviour from occurring, needs to be further documented in future work.

Focus on three team climate characteristics

The Corrupting Barrels model addresses three specific team climate characteristics that facilitate misconduct: an ineffective error approach, outcome inequality (and its emotional consequences) and dysfunctional moral climate. I have chosen to focus the model on three aspects of team climate, that represent three layers of relevant considerations for team members: relating to the task achievement of the team members, to relationships between the team members and to the team's moral climate. Although these three team climate aspects are chosen based on current and solid social psychological theory, I argue in paragraph 10.2.1 that leadership is key in preventing future unethical behaviour. Team leadership impacts team climate to a great extent, underlining the argument to include leadership as an explicit factor in the Corrupting Barrels model and assessment framework.

Furthermore, my analysis and suggested preventive approach of defining and impacting team climates focuses on team characteristics that may drive unethical behaviour of team members. My focus on team level social psychological mechanisms implicates that the influence of organizational level and formal mechanisms in the organizational context such as performance management, controls, codes and quality of procedures is not targeted in my analysis. Mechanisms in the 'formal context' influence behaviour of employees or even team climates. Examples that I touched upon earlier are conflicting performance and compliance goals, behavioural codes (i.e. Banker's Oath) and bonus caps. My assumption is that team- level realities are likely to differ despite these organizational-level procedures and control mechanisms. My decision to focus on the psychological root causes of misconduct is deliberate: my initial analysis of current banking and supervisory practices revealed that psychology and team climates are often neglected so far. Yet, essential theoretical and empirical insights in social psychological root causes suggest that team climates merit explicit attention and require a specific diagnosis. My analysis and presented two-step approach provide the tools to do this.

Limited survey sample size

The survey, as part of the assessment framework, was tested on 32 respondents, at a single point in time. This sample is too small and the time frame examined is too limited to conclusively validate the predictive value of this survey. With the deep dive – combining desk research, observations, interviews and survey methods - I was able to assess the distinct team climates of desks A and B. On the basis of this characterization of team climates, desk A showed more evidence of aspects that facilitate misconduct, than the team climate of desk B. This was also evident from the survey, where members of desk A indicated higher perceived injustice about the way rewards were distributed and a higher unjust leadership. This is not to say that team members of desk A will certainly behave unethically in the future. Yet, management information indicates that already more unethical behaviour is shown by traders at desk A than at desk B. The relevant team climate aspects I examined indicate an increased risk of misconduct at desk A, compared to desk B, based on theoretical expectations and empirical studies of the general impact of these team climate aspects.

3. Opportunities for future research

Longitudinal analysis

A first opportunity for future research is to document behaviours over time, within teams that have been assessed using the Corrupting Barrels framework. This will help establish the predictive value of an assessment along the lines suggested. My analysis yields a model and framework that can be used to assess the risk of future misconduct. To test whether the assessed risk results in actual unethical behaviour of team members is something to be established in future work. In Chapter 5 I have shown evidence for the lack of ability for banks to present data at team level of (unethical) behaviours. Aligned with this conclusion, bank B did not provide data on (unethical) behaviour at the two trading desks that were assessed as reported in Chapter 6. This lack of relevant team-level data prevented me from examining whether the team profiles of desks A and B, theoretically indicating a higher risk of unethical behaviour at desk A on theoretical grounds, also was visible in a larger amount of behavioural signals or incidents at desk A than at desk B. So, team climates characterized by using the framework presented here, still have to be paired with existing behavioural data to make a next step in establishing the added value of my framework. Eventually, a follow up study on these team climate assessments with longitudinal documentation of unethical behaviours is needed to draw more final conclusions about the predictive value of the assessment results.

A second opportunity that can only be met by conducting longitudinal analysis is to explore the effects of improving team climates. The preventive approach that I suggest is a two-step approach aiming first to identify team climate aspects that facilitate unethical behaviours and second to improve team climates accordingly. That second step, targeting possible root causes of misconduct by improving team climate aspects, should lead to a mitigation of misconduct risk. In Chapter 10 I elaborate on the nature of these improvements. With the use of longitudinal analyses the actual impact of these mitigating team climate improvements can be empirically established.

Survey development

The current version of the Corrupting Barrels survey can be further developed in the future. Using it on a larger variety of samples and including the number of respondents who complete this survey (increase the N) can help improve the list and more clearly distinguish relevant subscales. I suggest two areas of improvement. The first concerns the three items used to measure error approach, adapted from the Error Aversion Culture dimension by Van Dyck *et al.* (2005): "In this team people feel stressed when making mistakes", 'In general people in this team feel embarrassed after making a mistake" and "People within my team prefer to keep errors to themselves". In the results of my survey, these three items loaded on two different factors. As a result, I used the perceived stress of reporting errors as the only indicator of a dysfunctional error climate. Nevertheless, other items from the questionnaire developed by Van Dyck would seem relevant too, for instance as they inquire how and when people talk about errors to learn from them. For future development of the Corrupting Barrels survey it is worthwhile to see whether the survey can be expand with these items of the original questionnaire to more fully assess different aspects of a (dys-)functional error climate.

A second area of improvement concerns the items that I used to measure moral climates of the teams examined. Six of the original fifteen items used to measure climate -the ones measuring rules and law and code principle based climate- clustered into a single reliable scale. However, the nine remaining items are also relevant, as these measure caring climates and instrumental climates. Again, caring climates and instrumental climates have been established in prior research as climates that can counter the adherence to moral principles, and can invite organizational misbehavior, even among workers who are aware of organizational rules and guidelines. Hence, it would seem of value to further explore and test whether these team climate aspects can also be assessed reliably. In my sample and analyses these items did not cluster as expected on the basis of Stachowicz-Stanusch and Simha's original questionnaire and analysis (2013). In future research, this should be explored further, for instance by repeating the survey with a larger sample of professional traders.

Explore other contexts

A final opportunity for future research is to use the assessment framework (deep dive assessment and survey) in contexts other than the trading business or the banking industry. Although I developed the Corrupting Barrels model during my work as a financial supervisor in the banking sector, the model is based on theory that is not specific for the financial industry. The social psychological root causes of unethical behaviour in principle apply to any team in a professional context. It would be of interest to explore in what way the root causes of misconduct in team climates evolve in industries that have different histories in misconduct than the banking industry has. Although unethical behaviour and neglect of team level root causes is possible in any professional context, the societal consequences and public indignation as a reaction to misconduct might be less severe. The strong rule and code based team climates that the survey results showed are not surprising in an industry that faces political and regulatory pressure and public mistrust. And although a strong rule awareness has added value in preventing misconduct, it may also unintendedly lead to a low moral awareness (i.e. the focus on rules may drive a climate of moral neglect as discussed in paragraph 8.3) In industries with a different legacy, i.e. less misconduct, this assessment framework might reveal team profiles that characterized by other commonalities than strong rule awareness.

In sum, my analysis is a first illustration of how banks and financial supervisors can define and assess team climates in order to prevent future unethical behaviour. It is fair to say that this preventive approach has its limitations and that it provides opportunities for future research as I articulated in this chapter. Nevertheless, there is much to win by addressing dysfunctional team practices, as a way to prevent future misconduct. Adjusting the conditions under which trading teams do their work, can help direct and change the behaviour of individual team members. There is by now broad consensus that cultural and behavioural changes are needed in the trading business, in order to prevent future misconduct. Applying social psychological insights about conditions that invite unethical behaviour at work, can help understand and improve current work practices in the banking sector.

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Appendix A. Two-pager on the assessment framework as used in this analysis

The Corrupting Barrels framework focuses on behavioural patterns and culture aspects within team climate, that increase the risk of misconduct of a single or multiple team members. Misconduct is illegal by law and/or unethical by violating widely accepted (societal) moral norms. It includes imputable acts (such as fraud and manipulation of interest rates) and imputable omissions (such as failing to act or perform duties). The impact is damage to the bank itself and to customers, investors, other stakeholders and society at large.

Scope

The focus of a Corrupting Barrels assessment (CBA) is on a specific team with high misconduct risk.

Objective

The supervisory objective of the CBA is to identify root causes within team climate of misconduct risk and mitigate this risk, by: (a) identifying and assessing the behavioural patterns and culture a within team climate that pose a risk for misconduct of one or more team members; (b) requiring (senior) leadership to change these risky patterns.

Besides these supervisory objectives, the supervisory team will benefit from this investigation because: CBA will create an in depth view of the behavioural root causes of other ethical or intergrity issues at the bank; and CBA adds value in the ongoing dialogue between financial supervision and the bank.

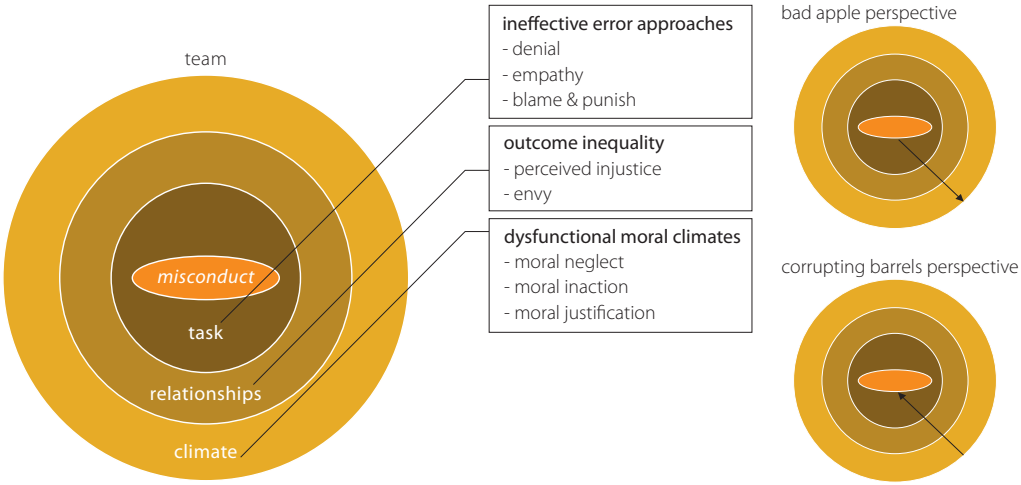
Deliverables

1. Identified behavioural patterns of and drivers within team climate, that pose a risk for misconduct of one or more team members.
- Presentation / slides with identified and assessed behavioural risks.
2. Requirements of (senior) leadership to mitigate risky behavioural patterns and drivers.
- (Non-binding) Letter to the management board, with slides (under 1) attached.
3. Specific points for the supervisory team to address in supervision on the bank.
- Session with supervisory team to debrief on conclusions and requirements.

Corrupting Barrels Model

Behavioural patterns and culture aspects relate to ineffective error management, outcome inequality and dysfunctional moral climates. Organizational facilitators such as strong growth, pressure on revenue and performance management are considered as context variables. For these behavioural categories and its drivers, there are key indicators and expectations defined that are used to identify and assess risks.

Figure A. *The Corrupting Barrels model: social psychological root causes of misconduct at team level*



Method

In about 3 months the CBA is conducted in the following steps:

1. intake with MB to introduce CBA, the approach and the selected scope (the team(s) to be assessed).
2. Root Cause analysis of misconduct cases: an analysis of 5 misconduct cases that have been documented and/or investigated by the bank in two steps: analysis of the banks internal investigation reports, and a session with involved financial supervisors. This step was not taken in the analysis as described in chapter 10, due to the absence of misconduct cases (the bank did not provide information on former incidents, see chapter 9).
3. Desk research on business strategy, performance management / incentives, ethical codes, etc. Objective: context analysis and organizational facilitators of misconduct.
4. Survey: to all team members. Questionnaire by e-mail on error approach, outcome inequality and morality.
5. Self-assessment: to all team members, on error approach, outcome inequality and morality.
6. Interviews: team members, team managers, senior leaders, second (risk management, compliance, HR, legal) and third (audit) line of defense. 90 minutes per interview.
7. Observation: of the team(s) - to 'give colour' to interview results. No conclusions based on this observation alone.
8. Challenging dialogue with the (senior) leadership (and if possible with middle/team management): using slides that give an overview of identified risks, per behavioural category, discussing with the leadership these assessed risks, and concluding with our requirements for mitigation of these risks.
9. Letter with recommendations to the management board (with a copy to the board of directors / supervisory board): letter with an overview of the identified and assessed risks, and our expectations / requirements of the senior leadership to mitigate these risks - the slides of the challenging dialogue as appendix.

Appendix B. Requested documents for desk research

Team
- Demographics per team: how many people, ages, gender, nationality. - Roles within the team. - Tenure per team member.

Misconduct
- I Codes of conduct / behavioural rules. - Risk appetite statement. - Cases, near misses, legal matters. - Compliance investigations to conduct / communication / breaches of risk limits. - Internal investigation (legal, audit, compliance) documents or reports. - Personal consequences / disciplinary measures per incident.

Task
- Strategic documents: to get a sense of the strategy of the bank, strategy of the division, organisational goals. - Business developments: information on the trading product, defining product groups, developments. - Information on legacy: growth of the business.

Relationships
- Information on compensation per team member: variable and fixed income. - Policy on incentive compensation. - Policy on promotion. - Targets + development of targets last 5 years.

Climate
- Employee satisfaction survey results. - Absence rates (ziekteverzuim) - Mobility information (verloop)

Appendix C. Interview format

Introduction
1. Introduce ourselves and the supervisory assessment. Deep dive on work climate, as part of a risk appetite assessment (thematic review). We will talk about your work, the relationships within your team, your perception of leadership of this team etc. 2. Why this desk, who we will interview 3. What will be done with the results 4. Explain link to survey: were you able to fill in? If not: hard copy, take 5 minutes. 5. Anonymity guaranteed

Task
1. Can you introduce yourself? What is your role/function? How long have you been here? 2. How would you describe what you do? What is the core of your job? 3. What skills and experience does that require / are important? What characterises a good trader? 4. Is that something that is changing? Is the work changing? 5. Please describe a situation in your work here in this team, that you look back on with great pride. 6. Please describe a situation in your work here in this team, that you look back on with regret / disappointment. 7. What do you enjoy the most in your work? What do you detest the most in your work? 8. If you look back in the last moths: can you describe an error or mistake that you have made in your work? How did you detect this error? What caused this error? How did you react? How did your teammates and deskmanager react? (zoom in on dialogue on error, learning from error).

Relationships
1. How do you interact with your colleagues? Subject of interaction: what about? Form of interaction: face to face, phone, email. Colour of interaction? 2. Are there friendships? What subgroups are there? 3. There are always differences within a team, between people. Can you talk about these differences? 4. Do you perceive big differences in pay between you and your colleagues? 5. On income/compensation procedures: do you think things are done fairly here? 6. What about promotion chances: how does that work within your team? What do you have to do to get promoted? How do you perceive your targets? 7. Does everyone have equal chances to get promoted? 8. All and all: are things being done fairly around here in your perception? 9. Can you describe a situation within this team that included some kind of unfairness?

Climate

1. Can you compare working in this team with other working experiences that you have? What strikes you if you make this comparison?
2. What is typical of this team? What is typical in the way people relate to each other?
3. If I would characterise your team: what would be the best characterisation, and what would be the worst characterisation?
4. What is the best story you could tell to another person (outside the bank) about this team? And what is the worst story?

5. What is important here?
6. What makes you successful in this team? Who is regarded as most successful in your team, why?

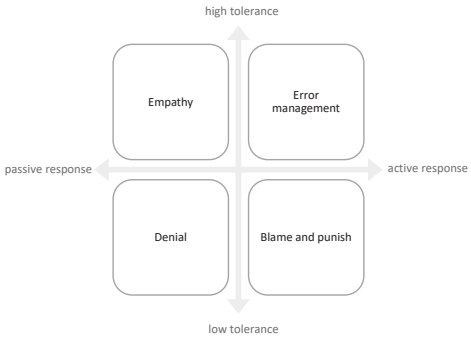
7. What are unwritten rules in this team? If I started to work here tomorrow: what would you explain to me? How would it be visible that I am new?

8. Can you talk about a situation, during your time in this team, what made you feel out of place?
9. What, if you are to move on some day, would you not miss about working in this team?
10. The people who have left this team: what have been reasons for that do you think?

11. If you were managing this team: what would you improve or change? What would you keep?

Leadership

1. How do you perceive the quality of leadership? Senior management, direct management (desk manager)? Differences?
2. If you compare this with leadership a few years ago? What kind of developments?
3. Desk manager: what is his/her leadership style? How would you describe that?
4. What is his/her best quality? What is the biggest improvement that he/she can make?
5. What is the best story that goes around about him/her? What is the worst story?
6. What is his/her style of communicating?
7. What does he/she value? What does he/she wants to see? What are his/her allergies? Examples.
8. To what extent is he/she fair to people within your team? Best / worst example?
9. How does he/she respond to human mistakes? Can you give an example? Use figure:



Appendix D. Observation format

This format was used during the observation of desks A and B. Duration about 1 hour. Sitting between the traders at the desk, observing the team during their regular work.

Task
– Task itself – Focus on task / concentration on task – Occurrence of an error / stressful situation: how detected, response to situation (self, team mates, desk manager), level of and coping with stress.

Relationships
– Frequency of interaction between traders – Subject of interaction: what about? – Form of interaction: face to face, phone, email.. – Colour of interaction: tone of voice – Subgroups / friendships

Climate
– What is important here? – Who is successful, who gets the most attention? Why? What gets attention? – Lunch: how are breaks taken? Together, separate? – Desks: what is on desks? Tokens, trophies, gadgets. – Clothes: what do people wear? Uniformity?

Leadership
– Where is the desk manager situated? On the desk, separate room? – Interaction of desk manager with others: frequency, who, why, colour – How do traders respond to him? – What does he express? Information, guidance, corrections…

Appendix E. Survey

	Demographic questions	A
a	At what desk do you work?	Desks A / B / C / D / E / F
b	What is the title of your function (your position or role in the team?)	Open
c	How long have you filled in this function (position, role) in this team?	Open
d	What is your gender?	Male / Female
e	What age are you?	< 25 / 25-35 / 35-45 / 45-55 / >55
f	What is your nationality?	Open

All 27 survey items were answered on a 9-point scale from 1 = strongly disagree to 9 = strongly agree.

	Survey item	Original item
ERROR		
– Van Dyck, C., Baer, M., Frese, M. and Sonnentag, S. (2005). Organizational error management culture and its impact on performance: A two-study replication. Journal of Applied Psychology, 90, 228–1240. – Van Dyck uses the Error Orientation Questionnaire—(EOQ) – from Rybowiak, Garst, Frese, & Batinic (1999). The EOQ measures error management culture versus error averse climate. Here, three items are used from Van Dyck's 'Error Aversion Culture'- dimension (coefficient alphas was .88 for the 11-item error aversion measure).		
1	In this team, people feel stressed when making mistakes (R).	In this organization, people feel stressed when making mistakes. (0.65)
2	In general, people in this team feel embarrassed after making a mistake (R).	In general, people in this organization feel embarrassed after making a mistake. (0.64)
3	People within my team prefer to keep errors to themselves.	People prefer to keep errors to themselves. (0.64)
JUSTICE		
– Colquitt, J.A. (2001). On the dimensionality of organizational justice: a construct validation of a measure. Journal of Applied Psychology, 86 (3), 386-400. Here, nine items are used from the Coquitt justice measure.		
Distributive justice		
4	The rewards that I receive (compensation, promotion e.g.) reflect the effort I have put into my work.	Does your (outcome) reflect the effort you have put into your work? (.86)
5	The rewards that I receive (compensation, promotion e.g.) are appropriate for the work I have completed	Is your (outcome) appropriate for the work you have completed? (.90)
6	The rewards that I receive (compensation, promotion e.g.) reflect what I have contributed to the company.	Does your (outcome) reflect what you have contributed to the organization? (.84)

Interpersonal justice		
		Colquitt: 'he/she' refers to the authority figure who enacted the procedure.
7	My team manager treats me in a polite manner.	Has he/she treated you in a polite manner? (.89)
8	My team manager treats me with dignity.	Has he/she treated you with dignity? (.85)
9	My team manager treats me with respect.	Has he/she treated you with respect? (.81)
Procedural justice		
		Colquitt: 'those procedures' refer to the procedures used to arrive at your (outcome).
10	I am able to express my views and feelings about certain issues in this team.	Have you been able to express your views and feelings during those procedures? (.67)
11	I have influence over the outcome arrived at by promotion procedures in this team.	Have you had influence over the outcome arrived at by those procedures? (.73)
12	My opinions are respected and valued within this team.	Have those procedures been applied consistently? (.72)
CLIMATE		
Stachowicz-Stanusch, A. & Simha, A. (2013). An empirical investigation of the effects of ethical climates on organizational corruption, Journal of Business Economics and Management, 14 (1), S433-S446. They selected items from the ethical climate scale of Victor & Cullen (1987, 1988).		
Principle: independence		
13	In this team, people are expected to follow their own personal and moral beliefs.	In this company, people are expected to follow their own personal and moral beliefs (0.74)
14	In this team, people are guided by their own personal ethics	In this company, people are guided by their own personal ethics (0.596)
15	Each person in this team decides for themselves what is right and wrong	Each person in this company decides for themselves what is right and wrong (0.688)
Principle: rules		
16	Successful people in this team go by the book	Successful people in this company go by the book (0.628)
17	Successful people in this team strictly obey the company policies	Successful people in this company strictly obey the company policies (0.802)
18	It is very important to follow strictly the company rules and procedures here	It is very important to follow strictly the company rules and procedures here (0.655)

Principle: law & code		
19	In this team, the law or ethical code of our profession is the major consideration	In this hospital, the law or ethical code of our profession is the major consideration (0.626)
20	In this team, people are expected to strictly follow legal or professional standards	In this hospital, people are expected to strictly follow legal or professional standards (0.859)
21	People in this team are expected to comply with the law and professional standards over and above other considerations.	People are expected to comply with the law and professional standards over and above other considerations (0.757)
Instrumental		
22	People in this team are expected to do anything to further the company's interests.	People are expected to do anything to further the hospitals interests (0.892)
23	There is no room for one's own personal morals or ethics in this team.	There is no room for one's own personal morals or ethics in this company (0.814)
24	In this team, people protect their own interest above other considerations.	In this company, people protect their own interest above other considerations (0.703)
Caring		
25	In this team, our major concern is always what is best for the other person.	In this company, our major concern is always what is best for the other person (0.627)
26	Our major consideration is what is best for everyone in this team.	Our major consideration is what is best for everyone in this company (0.751)
27	The most important concern is the good of all the people in the team.	The most important concern is the good of all the people in the company (0.632)

Appendix F. Separate survey items

Of the twenty-seven survey items, ten did not fall into the four clusters as discussed in Chapter 9, paragraph 9.2. To explore the results for these ten separate items, I calculated the means of the separate items for each of the six desks. These means are listed in Table 25. Concerning all items, low scores indicate a higher risk.

Table 25. Means of the ten separate items per desk

Items		Desks					
		A	B	C	D	E	F
1	People within my team do not prefer to keep errors to themselves (E3rc)	8.3	8.8	8.5	5.5	7.5	7.6
2	In this team, people are expected to follow their own personal and moral beliefs (PI1)	5	4.6	8	4.6	4.3	5
3	In this team, people are guided by their own personal ethics (PI2)	5.5	5.2	8	5.5	4.5	6.4
4	Each person in this team decides for themselves what is right and wrong (PI3)	3.2	2.2	6.5	4.3	4	2.9
5	In this team, our major concern is always what is best for the other person (C1)	5.2	4.8	6	5	4	6
6	Our major consideration is what is best for everyone in this team (C2)	7	5.4	9	5.3	5	6.6
7	The most important concern is the good of all the people in the team (C3)	5.8	6.6	4	4.5	4.5	6.6
8	People in this team are not expected to do anything to further the company's interests (IN1rc)	5.5	3.2	7.5	4	5.3	3.7
9	There is room for one's own personal morals or ethics in this team (IN2rc)	6.5	7.4	9	6.8	6.8	6.3
10	In this team, people do not protect their own interest above other considerations (IN3rc)	7.5	6.6	8	6.4	6.5	7

The means of the ten separate items per desk show variation. In other words, the six trading teams differ on these ten items. So, although the ten items do not connect to the clusters identified, they offer extra information on the differences per team. This implies that in the further development of the Corrupting Barrels survey, it is valuable to explore inclusion of these ten items. I would suggest to attend to the large differences between the lowest and highest mean per item in further scale development. Examples are the difference between the lowest and highest means of the items "Each person in this team decides for themselves what is right and wrong" and "People in this team are not expected to do anything to further the company's interests". This difference between means is 4,3 on a 9-point Likert scale. Another example is the difference between the lowest and highest mean for "Our major consideration is what is best for everyone in this team", of 4 on a 9-point Likert scale. These three items stem from climate scales: principle independent climate, instrumental climate and caring climate. These scales need to be further developed.

Next, I correlated the four constructed scales with the ten separate items. The correlations are summarized in Table F.2.

Table F.2. *Correlations between ten separate items and four scales.*

	SC1	SC2	SC3	SC4	E3RC	PI1	PI2	PI3	C1	C2	C3	IN1 RC	IN2RC	IN3RC
ERRORNSTR (SC1)														
LEADSHJ (SC2)	-.02													
FAIRRWRDS (SC3)	.24	.56**												
RULES&CDS (SC4)	-.15	.52**	.25											
E3RC	.14	.32	.17	.30										
PI1	-.27	.10	.15	.16	.17									
PI2	-.23	-.06	-.20	-.06	.07	.66**								
PI3	-.04	-.24	-.49**	-.17	-.24	.25	.34							
C1	-.13	.12	.03	.07	.12	.51**	.52**	.20						
C2	-.14	.34	.17	.41	.22	.63**	.44*	.19	-64**					
C3	-.21	.42	.37	.06	.34	.02	.03	-.32	.41	.38*				
IN1RC	-18	-.04	.08	.25	-.11	.04	-.06	.24	-.36*	-.13	-.69**			
IN2RC	.26	.17	.31	.06	.10	-.13	-.16	.03	-.11	-.03	.01	.08		
IN3RC	.16	.28	.22	.36	.10	.15	-.23	-.29	.11	.46**	.20	.02	-.08	

** *Correlation is significant at the 0.01 level (2-tailed)*

* *Correlation is significant at the 0.05 level (2-tailed)*

The scale measuring stress related to errors (SC1) correlates negatively with the item "In this team, people are expected to follow their own personal and moral beliefs" (PI1), r = - .27, p = .140, and shows a minor but negative correlation with the scale measuring focus on rules and codes (SC4), r = -.15, p = .426. Also, "Each person in this team decides for themselves what is right and wrong" (PI3) correlates negatively with "People within my team do not prefer to keep errors to themselves" (E3rc), r = -.24, p = .194. These correlations suggest that when employees use their own moral compass or personal ethics in their decision making, or when rules and codes are stressed, they might experience more stress when they make a mistake. Stress about errors can lead to cover up behaviour or impede speaking up when anything concerning is observed, and thereby facilitate unethical behaviour (see Chapter 8 on error approach).

"Each person in this team decides for themselves what is right and wrong" (PI3) correlates negatively with the scale measuring the perceived fairness of rewards (SC3), $r = -.49$, $p < .005$, the perceived fairness of leadership scale (SC2), $r = -.24$, $p = .194$, and – in lesser extent – with the scale measuring the focus on rules and codes (SC4), $r = -.17$, $p = .361$. This suggests that employees feel that their reliance on their personal ethics or morality in decision making, is not rewarded by their professional environment or may even lead to a decrease in respect from and fair treatment by their team management. It may indicate that when rules and codes are stressed, team members could feel that they can rely less on their own moral compass when they decide independently. When employees feel that their reliance on their personal ethics or morality in decision making is restricted, they might not use their own moral compass when situations are ambiguous and a professional judgement call is needed (see paragraph 8.3 on moral climate). A punitive leadership response to using own moral judgement or a dogmatic focus on rules and codes can 'clip the moral wings' of a bank employee, which is risky in itself since rules do not always apply to or give guidance for time pressured and complex decisions.

On the other hand, the correlations suggest that relying on individual moral compasses could have downsides. For instance, the item "Each person in this team decides for themselves what is right and wrong" (PI3) shows negative correlations with "The most important concern is the good of all the people in the team" (C3), $r = -.32$, $p < .076$. Could it be that the good of all the people in the team is associated with (financial) performance of the team, while increasing that performance might go against personal ethics? Furthermore, "In this team, people do not protect their own interest above other considerations" (IN3rc) correlates negatively with "Each person in this team decides for themselves what is right and wrong" (PI3), $r = -.29$, $p = .105$, and with "In this team, people are guided by their own personal ethics" (PI2), $r = -.23$, $p = .211$. This suggests that when employees follow their own morality or personal ethics, they feel they are protecting their own interests above other considerations. One explanation of this relation is that employees really are 'homo economicus', who merely seek to maximise their own interest and see protecting their own interest as being the 'right' decision. Alternatively, there might be little understanding of what personal ethics are, and how these may influence decision making. For instance, in a climate of moral neglect (see chapter 6) personal morality might not be understood or discussed. Both explanations are possibly facilitating future unethical behaviour.
In sum, some items correlate negatively with other scales and items. In the above instances, I can form hypothetical explanations for these negative relations. For the following negative correlations the explanation is less evident. "People in this team are not expected to do anything to further the company's interests" (IN1rc) correlates negatively with "The most important concern is the good of all the people in the team" (C3), $r = -.69$, $p < .001$, and with

"In this team, our major concern is always what is best for the other person" (C1), $r = -.36$, $p < .05$. So, if employees would do anything to further the company's interests, they would thereby be concerned with the good of all in the team, and what is best for others. To do anything to further company's interests, could lead to excessive risk taking – hence not being good for the team or others – unless taking excessive risks is seen as going against company's interests. Further development of the scales and items used in the Corrupting Barrels survey is needed to acquire more insight in the relationships between the different constructs.

Nederlandse samenvatting van Banking on Team Ethics: elementen van team klimaat die bijdragen aan onethisch gedrag in de financiële dienstverlening

In dit boek richt ik mij op sociaal psychologische oorzaken van onethisch gedrag binnen banken. Mijn centrale betoog is dat oorzaken van onethisch gedrag in teamklimaat besloten liggen. De hier geboden inzichten en praktische handvatten stellen banken en toezichthouders in staat oorzaken gelegen in teamklimaat te identificeren, om zo bij te dragen aan het voorkomen van onethisch gedrag in de financiële dienstverlening.

Onethisch gedrag van handelaren bij banken duurt voort zolang fraudezaken worden behandeld als voortkomend uit het gedrag van een enkele "rotte appel". Banken en financieel toezichthouders kijken onvoldoende naar omstandigheden in de werkomgeving die dit gedrag in de hand hebben gewerkt. De volgende stap die banken en financieel toezichthouders kunnen nemen om de stabiliteit van de financiële sector te verbeteren, is het vinden van contextuele oorzaken en het toepassen van sociaal psychologische kennis teneinde toekomstig onethisch gedrag te voorkomen. Mijn analyse heeft tot doel deze contextuele oorzaken binnen teams te identificeren - gebruik makend van empirisch psychologisch onderzoek - om zo handvatten aan te reiken die banken en toezichthouders kunnen toepassen. Ik laat hier zien hoe banken en financieel toezichthouders teamklimaat kunnen onderzoeken en belichten om toekomstig onethisch gedrag te voorkomen.

Deel 1 (hoofdstukken 1, 2 en 3): onethisch gedrag

Dit boek bestaat uit vier delen. In het eerste deel zet ik het centrale probleem uiteen en introduceer het door mijn analyse geboden antwoord. Mijn onderzoek is gebaseerd op verzamelde informatie en op gesprekken en observaties die ik als toezichthouder op Gedrag & Cultuur bij de Nederlandsche Bank (DNB) heb uitgevoerd in het kader van toezicht op verschillende Nederlandse en Europese grootbanken,. In het eerste deel van dit boek licht ik het gebruik van deze unieke data toe en ik onderbouw mijn keuze voor de handelsomgeving binnen banken als primaire context voor mijn analyse.

Onethisch gedrag heeft verstrekkende negatieve consequenties voor de financiële stabiliteit van de bankensector. Onethisch gedrag is niet een probleem uit het verleden, maar een actueel en voortdurend probleem. De huidige reactie van banken en financieel toezichthouders op onethisch gedrag is om twee redenen onvoldoende effectief om toekomstig onethisch gedrag te voorkomen. Ten eerste hebben banken en financieel toezichthouders door het 'rotte appel'-denken een beperkte kijk op wat onethisch gedrag veroorzaakt. Daarnaast reageren banken en financieel toezichthouders vooral reactief op onethisch gedrag, door achteraf controles te versterken en daders te bestraffen.

Om oorzaken van onethisch gedrag effectief te adresseren is een teamperspectief nodig – zo is mijn stellingname. Mijn analyse belicht sociaal psychologische oorzaken van onethisch gedrag, die gekenschetst kunnen worden door te denken in termen van 'corrumperende

omstandigheden'denken in plaats van zich alleen maar te richten op individuele "rotte appels'. Ik introduceer het 'Corrupting Barrels' model dat op basis van sociaal psychologische oorzaken van onethisch gedrag een effectieve preventieve aanpak hoopt te bieden. De titel van het model – Corrupting Barrels – refereert aan de werkteams en het werkklimaat in die teams die oorzaken van onethisch gedrag kunnen herbergen. Het model richt zich op drie centrale kenmerken van teams die kunnen bijdragen aan onethisch gedrag van individuele teamleden, namelijk: 1. hoe het team omgaat met fouten (op taakniveau), 2. hoe het team omgaat met ongelijkheid (op relatieniveau) en 3. de gedeelde moraliteit binnen het team (op klimaatniveau). Mijn analyse biedt aanknopingspunten voor een preventieve aanpak gericht op het identificeren van gedragspatronen en klimaatkenmerken in teams die het risico op onethisch gedrag vergroten – gebruik makend van het 'Corrupting Barrels' model - en op het verbeteren van deze patronen en kenmerken om zo toekomstig wangedrag te voorkomen. Mijn hoofdboodschap is dat met het meenemen van een teamperspectief, banken effectiever zijn in het voorkomen van onethisch handelen en toezichthouders effectiever in hun beïnvloeding van banken om dit risico op onethisch gedrag te mitigeren.

Deel 2 (hoofdstukken 4, 5 en 6): de huidige banken en toezichtspraktijk

Het tweede deel van dit boek richt zich op de mate waarin banken en financieel toezichthouders teams en teamklimaat in ogenschouw nemen als het gaat om onethisch gedrag. In twee studies analyseer ik in hoeverre analyse van gedrag en oorzaken van onethisch gedrag op teamniveau in de huidige praktijk plaatsvindt. Studie 1 laat zien dat teamklimaat een blinde vlek is voor banken en financieel toezichthouders. Een grootbank mist perspectief op teamniveau in haar eigen rapportage over en analyse van fraude. Teamklimaat, waarin oorzaken van onethisch gedrag besloten kunnen liggen, is voor banken niet in zicht wanneer zij hun eigen incidenten analyseren. Interventies gericht op het voorkomen van onethisch gedrag richten zich voornamelijk op organisatieniveau (zoals waarden en cultuurprogramma's) of op individueel niveau (zoals integriteitstests als onderdeel van wervings- en selectiebeleid en disciplinaire maatregelen).

De financieel toezichthouder is in de positie om van banken te vragen oorzaken van onethisch gedrag op teamniveau te identificeren. Studie 2 verkent in welke mate banken teamklimaat analyseren wanneer dit expliciet verzocht is door de toezichthouder. Met deze studie laat ik zien, dat een grootbank niet in staat was om op verzoek van de toezichthouder data over gedrag en teamklimaat te produceren van teams die handelden in zaken met een hoog integriteitsrisico. Vervolgens blijkt uit Studie 2 dat een andere grootbank een oorzaken analyse van incidenten uitvoerde op verzoek van de toezichthouder, zonder het teamperspectief in ogenschouw te nemen. De oorzaken analyse leidde ertoe dat de bank enkele incidenten verklaarde (veelal in feitelijk verslag van gebeurtenissen), maar niet in staat was oorzaken op teamniveau aan te pakken. Studie 2 laat zien dat het verzoek van de toezichthouder aan banken om ook het teamklimaat in oorzaken analysse te betrekken tot nu toe onvoldoende effectief is.

Deel 3 (hoofdstukken 7, 8 en 9): het identificeren van oorzaken van onethisch gedrag in teamklimaat

Het in deel 1 gepresenteerde 'Corrupting Barrels' model richt zich op drie sociaal psychologische mechanismen, gelegen in teams, die de kans op onethisch gedrag vergroten. Het gaat om een ineffectieve omgang met fouten in teams, ongelijkheid binnen teams en dysfunctionele morele teamklimaten. In deel 3 van dit boek zet ik de theoretische basis van dit model uiteen. Ik geef een overzicht van de theorie rond foutenmanagement en verken de relatie tussen ineffectieve foutenmanagement en onethisch gedrag. Vervolgens vat ik de theorie rond ongelijkheid samen en ga ik in op de mogelijke emotionele consequenties van ongelijkheid zoals gevoelens van oneerlijkheid en afgunst. Ik ga na hoe deze emotionele consequenties samenhangen met een verhoogd risico op onethisch gedrag. Ik vat de theorie rond moraliteit binnen teams samen en verken hoe een dysfunctioneel moreel klimaat, zoals een klimaat van laag moreel bewustzijn, samenhangt met een hoger risico op onethisch gedrag.

In deel 2 bleek dat banken onvoldoende in staat zijn oorzaken van onethisch gedrag op teamniveau te analyseren, ook als dit expliciet verzocht werd door de toezichthouder. Studies 1 en 2 laten zien dat banken uit zichzelf teamklimaat onvoldoende in ogenschouw nemen en dat toezichthouders onvoldoende effectief zijn in het beïnvloeden van banken om dit te doen. Hieruit volgt een logische gevolgtrekking: er zijn praktische instrumenten nodig voor banken en toezichthouders om oorzaken van onethisch gedrag op teamniveau te identificeren. In Studie 3 presenteer ik een toezichtsonderzoek naar sociaal psychologische oorzaken van onethisch gedrag, uitgevoerd op twee teams van handelaren binnen een grootbank. Met dit toezichtsonderzoek heb ik een onderzoeksraamwerk toegepast dat gebaseerd is op het 'Corrupting Barrels' model. Dit bestaat uit een deskresearch instructie, een interview vragenlijst en een observatie instrument. De uitkomsten van Studie 3 laten zien dat het mogelijk is om met het gepresenteerde raamwerk en bijbehorende instrumenten die aspecten van teamklimaat te identificeren die kunnen leiden tot onethisch gedrag, namelijk een ineffectieve omgang met fouten in het team, ongelijkheid in het team en een disfunctioneel moreel teamklimaat. Door het combineren van interviews, observaties en deskresearch is het mogelijk om teams effectief op deze aspecten te onderscheiden. Team A had, zo bleek uit Studie 3, veel meer 'hoog risico' patronen dan team B. Dit stelt de grootbank in staat een gerichte preventieve aanpak toe te passen op team A.

Het uitvoeren van een onderzoek naar teamklimaat, gebruik makende van interviews, observaties en deskresearch, is tijdsintensief en vraagt expertise en ervaring in gedragsonderzoek. Het kan praktisch en realistisch zijn om een survey te gebruiken als een *quick scan* van teamklimaat, gericht op oorzaken van onethisch gedrag. Ik heb daarvoor een 'Corrupting Barrels' survey ontwikkeld, gericht op de drie sociaal psychologische oorzaken van onethisch gedrag op teamniveau. Het tweede deel van Studie 3 laat de resultaten zien van een eerste toepassing van deze survey in een handelsomgeving binnen een grootbank. De resultaten laten zien dat banken en toezichthouders met deze survey een goede eerste indruk krijgen van teamklimaten die de kans op toekomstig onethisch gedrag kunnen vergroten. Op basis van de surveyresultaten kan een bank of toezichthouder besluiten een nader onderzoek in te stellen, gebruik makend van interviews, observaties en deskresearch.

Deel IV (hoofdstukken 10 en 11): conclusies en praktische implicaties

Ik stel voor het risico op onethisch gedrag te mitigeren in twee stappen. Banken en toezichthouders kunnen het in dit boek gepresenteerde Corrupting Barrels model en onderzoeksraamwerk gebruiken om mogelijke oorzaken van onethisch gedrag op teamniveau te analyseren. Vervolgens kunnen banken op basis van die analyse teamklimaten gericht verbeteren om zo de kans op toekomstig onethisch gedrag van individuele teamleden te verkleinen.

Er is op basis van eerder onderzoek voor elk van de drie besproken kenmerken van teamklimaat bekend welke verbeteringen effectief zijn. Zo is het voor een ineffectieve omgang met fouten bijvoorbeeld belangrijk een open communicatie van fouten te creëren. Voor een klimaat van laag moreel bewustzijn is het belangrijk dialoog te organiseren over de morele aspecten van het werk. Deze en andere *evidence based* verbetersuggesties van teamklimaat ter preventie van onethisch gedrag bespreek ik in hoofdstuk 10.

Een centrale factor in alle verbeteringen van teamklimaat is leiderschap. De direct leidinggevende is van grote invloed op de sociaal psychologische mechanismen in het team die samenhangen met onethisch handelen. Om leiderschap als de sleutel tot effectieve preventie van onethisch gedrag te activeren, moeten banken en financieel toezichthouders leiderschap verantwoordelijk houden voor gezonde teamklimaten en nagaan in welke mate hoger management teams met dat doel bekijkt. In hoeverre heeft het leiderschap van de bank teams met een verhoogd risico op haar netvlies? Heeft het hoger management ingegrepen wanneer het direct leiderschap op deze hoog risicoplekken niet in staat bleek het teamklimaat te verbeteren of mogelijk het teamklimaat negatief beïnvloedde? Dysfunctioneel leiderschap laten voortbestaan, is een uitnodiging voor onethisch handelen.

Ik bespreek de sterke kanten en de beperkingen van mijn onderzoek. Mijn analyse biedt een toepasbaar 'Corrupting Barrels' model, een onderzoeksraamwerk en perspectief op teamklimaat dat van waarde is bij het voorkomen van toekomstig onethisch gedrag. Dit model en raamwerk zijn gebaseerd op actueel sociaal en organisatiepsychologisch onderzoek. Ik presenteer een empirische analyse gebaseerd op unieke en publiek ontoegankelijke toezichtsinformatie verzameld bij grootbanken, inclusief interviews met bestuurders van deze banken. Ten slotte stel ik een concrete en praktische aanpak voor bestaande uit twee stappen, om oorzaken van onethisch gedrag in teams te identificeren en vervolgens deze oorzaken gericht aan te pakken. Mijn analyse heeft (nog) niet de voorspellende waarde van het 'Corrupting Barrels' model en onderzoeksraamwerk kunnen aantonen. Ofwel, ik heb niet laten zien dat door de toepassing van dit model en raamwerk onethisch gedrag daadwerkelijk te voorkomen is. Het model richt zich op drie karakteristieken van teamklimaat die de kans op onethisch gedrag kunnen vergroten. Er zijn wellicht meer karakteristieken van belang: de drie sociaal psychologisch mechanismen zijn niet limitatief. Tenslotte is de groep deelnemers aan de 'Corrupting Barrels' survey klein geweest waardoor ik beperkte mogelijkheden had om statistische analyses uit te voeren.

Mijn analyse biedt wel een eerste illustratie van de wijze waarop banken en toezichthouders teamklimaat kunnen analyseren en verbeteren om onethisch gedrag te voorkomen. Er is veel te winnen met het aanpakken van dysfunctionele teams binnen banken om zo het risico op fraude te verkleinen. Het aanpakken en veranderen van de sociaal psychologisch mechanismen in teams, kan helpen om het gedrag van individuele teamleden te sturen. Er is tegenwoordig een breed gedragen overtuiging dat cultuur- en gedragsverandering nodig is in de bankensector om onethisch handelen tegen te gaan. Het toepassen van sociaal psychologische inzichten over condities die onethisch gedrag kunnen uitlokken, kan helpen bij het begrijpen en verbeteren van de huidige bankenpraktijk.

Curriculum vitae

Wieke Scholten (1979) studied Organizational and Social Psychology at Leiden University after graduating in 1998 from the Alexander Hegius Lyceum, Deventer.

As Head of Audit for Behavioural Risk at RBS (London, UK) she is leading a team within Group Internal Audit that aims to identify behavioural risk within the Bank. Auditing behavioural risk is a new field within the internal audit context. The deep dive methodology is based on social and organizational psychology. The objective of the audit reviews is to reveal insight to senior management on team climates, behaviours and mindsets that drive risk within the Bank, enabling them to mitigate this behavioural risk.

Before joining RBS in 2016, Wieke worked as a senior supervisory officer in behaviour & culture supervision at De Nederlandsche Bank, as part of an expertise team that executes supervision of behaviour and culture in the Dutch financial services industry. She is co-author of the book "Supervision of Behaviour and Culture: Foundations, Practice & Future Developments" (Mirea Raaijmakers, ed, DNB, 2015). During her time at DNB, more than 60 financial firms (including about 25 Dutch and European banks) had been assessed. She was hired in 2011 by DNB to develop the method for supervising behaviour and culture with her colleagues, and has specialized in banking culture ever since.

Wieke has worked on this research project since 2012, using data that she gathered in the banking industry in her supervisory role at DNB. The paper she wrote with Naomi Ellemers titled "Bad apples or corrupting barrels: preventing traders' misconduct", appeared in the Journal of Financial Regulation and Compliance in November 2016 and has been awarded as Outstanding Paper of that year.

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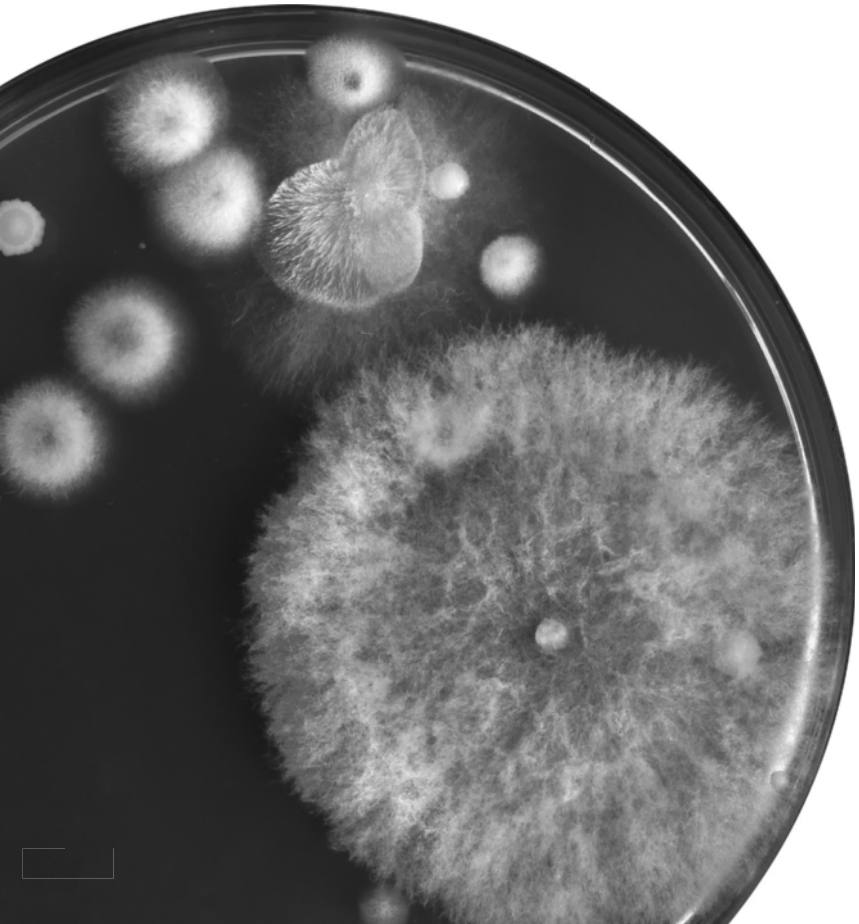
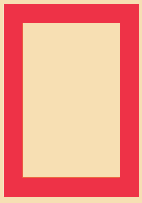


Team climates are a blind spot for banks and financial supervisors. This book provides insights and tools for managers and in- and external supervisors within financial services that help to define and assess team climates in order to prevent future misconduct.

Applying social psychological insights about team conditions that invite unethical behaviour at work, can help understand and improve current work practices in financial services. Based on these insights, the 'Corrupting Barrels' model and assessment framework is introduced and applied in banking practice. The results of the studies suggests possible ways of taking up a practical approach in preventing misconduct by defining and assessing team climates.

The analysis provided is based on data gathered in the context of behaviour and culture supervision in the financial industry. It provides illustrative examples (quotes) from interviews with board members, senior managers and traders within large European banks.



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Dissertatiereeks Kurt Lewin Instituut 2017-15

ISBN 978-90-828254-0-4