Peter Engering
Senior Manager - The Netherlands

Key/special qualifications

- Conduct Risk and Risk Culture
- Strategic Risk Management with focus on (control) rationalization and trust
- (Strategic) Risk Assessments
- Anti Money Laundering, Customer Due Diligence, Transaction Monitoring, robotics
- Forward-looking & innovative

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Regulatory Risk, Risk Advisory
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Dutch Banking Supervision on Conduct and Culture

Agenda

01 Introduction
02 Dutch Banking Supervision
03 Supervision in Practice
04 Practical Solutions
05 Wrap-up and questions
What is culture?

What is conduct risk and risk culture?
How is it being perceived – an example?

Importance of culture

86% of executives surveyed around the world rate culture as "very important" or "important"

82% of survey respondents believe that "culture is a potential competitive advantage"

However,

Only 12% of companies believe their organizations are driving the "right culture"

Over 50% of companies are currently attempting to change their culture in response to shifting talent markets and increased competition

Dutch Banking Supervision
Banking Supervision in the Netherlands

Brief introduction

- The “Netherlands Banking Association” (NVB) is the link between the banking sector, government and public
- Specific task of concluding the Collective Labour Agreement for the Banking Sector
- Social-economic representation
- Has a focus in 2018 on diversity and inclusion, making diverse culture a push-factor and ‘strengthens organizations’

- “De Nederlandsche Bank” (DNB) is the supervisory body for the financial system as a whole, and as such it ensures financial stability
- DNB supervises in a prudential way
- Customers must be confident that a company can meet its financial obligations
- DNB focuses on potential risks for the financial system, giving advice and warnings

- The “Dutch Authority of Financial Markets” (AFM) supervises the manner in which financial institutions deal with each other and with customers
- The AFM promotes the fair and efficient operation of the capital markets and focuses on behavior of market parties
- Encourage financial institutions to treat their customers honestly, openly and with due care (e.g. price)
- Goal is to increase confidence of consumers and businesses in the financial markets
Banking Supervision in the Netherlands
AFM, DNB and ECB

International supervisory authorities are showing keen interest in the Dutch approach to supervision of behavior and culture.

Figure 1 Supervision of banks in the Netherlands (Source: Netherlands Court of Audit)

Source: ‘FOCUS!’ By DNB
Banking Supervision in the Netherlands
Focus on Conduct Risk and Risk Culture

Report: “Restoring Trust” by Advisory Committee on the Future of Banks
Implementation Report Banking Code by “De Wit” Committee
Introduction “FOCUS!” by DNB
DNB Report “Leading by example”
DNB & AFM Report “Capacity for Change in the Financial Sector”

- 2009: Publication of the Banking Code + Formation of DNB Center of Expertise
- 2010: Implementation Report 2012
- 2012: Implementation Report 2013
- 2013: DNB Report “Supervision of Behaviour and Culture”
- 2013: AFM Case Study “Learn from Errors: towards an Error Management Culture”
- 2014: DNB Report
- 2017: AFM Case Study
- 2018: DNB Report
Banking Supervision in the Netherlands
AFM & DNB Supervisory Priorities on conduct and culture 2018 and beyond

Priorities

- Improve a healthy organizational culture by further applying the recently introduced methodology on error management
- Protection of vulnerable customers by improving quality and information provision of investment products (MiFID2/PARP)
- Innovation in the customer’s interest (Fintech program)
- Make culture and conduct risks more tangible by using more scientific, behavioral data

Priorities

- Foster a forward-looking sector with timely strategic decision-making and ability to quickly respond
- Legislative changes require FIs to have a high absorption capacity and proactive attitude for implementing and complying to new legislation
### Supervision in Practice

#### Examples of methods used – what can you expect?

<table>
<thead>
<tr>
<th>Examples</th>
<th>Explanation</th>
<th>Areas of attention</th>
</tr>
</thead>
<tbody>
<tr>
<td>Review of annual reports</td>
<td>• Mission, vision and values</td>
<td>• Use of words and consistency</td>
</tr>
<tr>
<td>Desk research</td>
<td>• Comply or explain (Banking &amp; Governance Code)</td>
<td>• Ensure the stand alone readability of the conduct</td>
</tr>
<tr>
<td></td>
<td>• Reviewing elements of conduct and culture</td>
<td>and culture paragraphs</td>
</tr>
<tr>
<td>Interviews</td>
<td>• Policies: e.g. Code of Conduct, PARP, Governance, Remuneration, Performance</td>
<td>• Share large # of policies, procedures and data(!)</td>
</tr>
<tr>
<td></td>
<td>appraisals, esc</td>
<td>• Ensure not only the design but also the operating</td>
</tr>
<tr>
<td></td>
<td>• Culture initiatives</td>
<td>effectiveness can be reviewed</td>
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<tr>
<td>Self Assessments</td>
<td>• Board of Directors</td>
<td>• Do not prepare the interviews too much (same answers)</td>
</tr>
<tr>
<td></td>
<td>• Supervisory Board</td>
<td>• Availability of key personnel (showing importance)</td>
</tr>
<tr>
<td></td>
<td>• Heads of Risk Management / Compliance</td>
<td>• Preparing for lengthy assessments (&gt; 100 detailed</td>
</tr>
<tr>
<td>Online Assessments</td>
<td>• Tone at the top</td>
<td>questions) irrespective of banks’ size</td>
</tr>
<tr>
<td></td>
<td>• (Risk) Culture</td>
<td>• The bank will not know who will be selected</td>
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<td></td>
<td>• Diversity</td>
<td>• Preparing employees to participate in the survey and</td>
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<td></td>
<td>• (variable) salary</td>
<td>provide them with extra time</td>
</tr>
<tr>
<td>Benchmarking</td>
<td>• Sample selection of employees of different departments</td>
<td>• The bank will see how they are ranked, but not the</td>
</tr>
<tr>
<td>Board effectiveness</td>
<td>• Comparing institutions of same size and product offering</td>
<td>position of the other banks</td>
</tr>
<tr>
<td></td>
<td>• Net Promoter Score</td>
<td>• Be aware of exaggerated politically correct behaviour</td>
</tr>
<tr>
<td>Suitability and reliability tests</td>
<td>• Psychologists in board &amp; personal meetings</td>
<td>• Psychologists trained to see group dynamics</td>
</tr>
<tr>
<td></td>
<td>• Evaluating reorganizations</td>
<td>• 10 % failed for the test; sufficient preparation is</td>
</tr>
<tr>
<td></td>
<td>• Decision-making in the organization</td>
<td>necessary</td>
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Dutch Banking Supervision on Conduct and Culture
Practical Solutions
Recommendations to Improve Conduct & Culture

- Show how the accountability of culture and behavior is set within the board of directors
- Attract different profiles in the board
- Leaders should be able to show they have made efforts to gain expertise on behavior and culture change (instead of content)
- Transparent communication on why certain decisions have been made or visibly demand input from (key) stakeholders
- Visible inclusion of control functions (risk management, compliance) in decision-making
- Strengthen the role of the 2nd and 3rd line of defense and the independent directors
- Recognize culture and behavior as an important factor in change processes and reorganizations
- Show how diversity impacts the company’s culture

How to meet the expectations of the regulator?
### Positive and negative indicators within the firm

<table>
<thead>
<tr>
<th>The “tone from the top”</th>
<th>Purpose and strategy</th>
<th>Individual accountability</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Positive</strong></td>
<td><strong>Positive</strong></td>
<td><strong>Positive</strong></td>
</tr>
<tr>
<td>The leadership is <strong>demonstrably responsible for</strong> setting the firm’s <strong>purpose and target culture</strong> and articulating how these are reflected in the firm’s strategy, values and the behaviours expected of staff at all levels.</td>
<td>A <strong>clearly defined purpose</strong>, linked to the firm’s culture and values and accompanied by a clear articulation of <strong>expectations and behaviours</strong> of staff across the firm, tailored for specific areas e.g. front line staff.</td>
<td>Evidence of <strong>clear lines of accountability</strong> for senior managers and other key risk takers or function holders.</td>
</tr>
<tr>
<td><strong>Negative</strong></td>
<td><strong>Negative</strong></td>
<td><strong>Negative</strong></td>
</tr>
<tr>
<td>A <strong>lack of challenge</strong> of, and amongst, the board increasing the risk that debate and decision making at senior levels are dominated by commercial and competitive considerations, and other outcomes</td>
<td>A <strong>culture of “blame” or fear</strong>, in which staff are reluctant to “speak up” or express contrary viewpoints; or a culture where staff are <strong>reluctant to deliver bad news</strong> to senior management (i.e. a good news culture).</td>
<td>Evidence of <strong>reluctance</strong> amongst senior staff at any level to be <strong>accountable</strong> for their role. For example, through the inappropriate delegation of responsibility to more junior staff.</td>
</tr>
</tbody>
</table>
### Positive and negative indicators within the firm

<table>
<thead>
<tr>
<th>Remuneration and incentives</th>
<th>Governance and controls</th>
<th>Mindsets and behaviour</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Positive</strong></td>
<td><strong>Positive</strong></td>
<td><strong>Positive</strong></td>
</tr>
<tr>
<td>Reward and incentives programs that are <strong>transparent and aligned to the achievement of the firm’s culture</strong> and the desired behaviour of staff. For example, rewarding call centre staff for the good treatment of customers rather than the number of calls they take.</td>
<td><strong>An internal governance and internal control framework</strong> that includes a clear organisational structure and well-functioning, independent risk management, compliance and audit functions.</td>
<td>A clearly <strong>defined set of positive and negative behaviours</strong> for staff at all levels within the firm.</td>
</tr>
<tr>
<td><strong>Negative</strong></td>
<td><strong>Negative</strong></td>
<td><strong>Negative</strong></td>
</tr>
<tr>
<td>Evidence of excessive <strong>pressure being placed on sales teams or customer facing teams</strong> to meet targets at the expense of good outcomes.</td>
<td><strong>Inadequate resourcing</strong> (both financial and human) of control functions such that they are not able to provide adequate oversight.</td>
<td>The firm demonstrates a <strong>legalistic, “tick-box” mentality</strong> towards regulatory compliance rather than considering the intended spirit of regulation or proactively responding to regulatory guidance before it is adopted as formal rules.</td>
</tr>
</tbody>
</table>
Proactively manage culture
Help turn insights - what does it mean - into action - what to do

The different lines of defense and the different roles across the organization all have a responsibility to manage the culture and to drive organizational alignment.

1st. The Board, chief executive, and management create the vision and aspirational culture; and define desired behaviors; reinforced by human resources to drive employee engagement and measure performance.

2nd. Risk, ethics and compliance, internal controls, finance, legal, technology, etc., help manage, monitor, and mitigate risk; report to executive on risks, set policies, provide governance.

3rd. Internal audit offers assurance and advise on culture as appropriate and validates mitigation activities.

Desired organizational culture and behavior

Organizational culture

1st line of defense

2nd line of defense

3rd line of defense

Actual organizational culture and behavior

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Supervision in Practice
Examples of methods used

- **Monitoring Committee Dutch Banking Code**
  - Report 1
  - Report 2
  - Report 3

- **Supervision NVB**
  - Future-oriented Banking package (Charter, Code, Rules of Conduct)
  - Banker’s oath and disciplinary rules

- **Supervision DNB & AFM**
  - Expert Teams researching specific root-causes of incidents
  - Culture & conduct is part of the day-to-day supervision
  - Example of investigation into behaviour and culture: error management
  - Dashboards to rank institutions on specific topics