First, let me thank Governor Carney, the Lord Chief Justice, and Dame Colette for including me in today’s discussion. It is an honor to be here. As always, what I have to say reflects my own views and not necessarily those of the Federal Open Market Committee or the Federal Reserve System.

I also want to thank the Banking Standards Board for its important work on improving standards of conduct in financial services. The effects of this work will, I think, be felt throughout the industry, not just in the City of London.

We learned from the LIBOR and FX scandals that poor conduct can proliferate quickly throughout the global marketplace. That’s because short-term thinking—maxing out this year’s compensation bonus or this quarter’s accounting profits—is a catalyst for poor conduct. In contrast, good conduct may take longer to catch on. Good conduct depends on a longer-term frame of reference. It is building a viable career that one can be proud of, and, at the firm level, building franchise value and reputation that takes decades to accomplish. In both cases, though, the same enabling mechanism is at work: culture.

Culture—within a firm or across an industry—is not determined primarily by rules or laws, though certainly rules and laws can amplify good or bad attributes. Culture comprises, instead, what people observe and do, resulting in accepted and mostly unspoken norms. Mostly, people look for what succeeds and what does not, and they try to align themselves with the former.

If we want to improve culture and conduct, we need to start by being realists about human behavior. At the New York Fed’s culture conference last October, Dame Minouche Shafik observed pragmatically that an end to all misconduct is not the goal of reform. There will always be a few bad apples. Rather, the goals should be far fewer instances of misconduct and far less scope, magnitude and duration when such misconduct inevitably occurs.

I submit that the best way to keep problems small is to encourage a culture that spots issues and raises concerns early. In my view, the most dangerous type of culture in finance occurs when people see something wrong but do not say something.

I think back to the chat room transcripts from the LIBOR and FX scandals. The way traders communicated so openly about their manipulation of markets makes it hard to imagine that others in their firms did not know what was happening. So, why didn’t those people say something?

There are understandable, human tendencies that can cause each of us to avoid rocking the boat. People want to be team players. Those behavioral traits can be amplified through a firm’s culture, which can weigh on one’s willingness to do the right thing. This is, unfortunately, what seems to have occurred at Wells Fargo, one of the largest retail banks in the United States. Whether to obtain a bonus or simply to keep a job, employees felt they had to keep quiet and meet sales targets despite the cost to customers.
So, how do you change a culture where silence leads to misconduct? I will offer two ideas that might help and one idea that will not.

Here is what will not work: Merely telling your employees to speak up. Cultures do not change simply by exhortation. Eloquent speeches, a well-phrased value statement, and an annual requirement to acknowledge the code of conduct are just not sufficient.

That’s the easy one. The two ideas that might work are harder.

First, managers have to lead by example. Senior executives must be seen within the firm to expect and respect challenges, and in turn must challenge ideas themselves. And, they have to explain difficult decisions to their employees—sharing not only the news of what they have done, but why. More important, mid-level managers have to do the same. Of course, mid-level managers will not generally behave that way unless they see their senior leadership setting the example.

Second, if your organization values people when they raise their hand, your incentives have to reflect that. Employees who speak up should be recognized. The courage it takes to speak up, despite the perceived costs, should be counted as a very positive factor in evaluations. And, where raising one’s hand has saved the firm’s money and reputation by avoiding or keeping a problem small, that action should be rewarded.

It’s only natural for an economist like me to consider the issue of unintended consequences. One that comes to mind is creating a culture of distrust and suspicion, where everyone looking over his or her shoulder. That would be unfortunate and costly. But, I think it is more likely that a different culture will result. Instead, talented and conscientious people will be happy to remain at a firm or in the industry because their personal and professional values are well aligned. Such employees will feel relief that they can speak up without fear of reprisal, and they can enjoy a clear conscience for having done the right thing. There is significant value in being able to sleep well at night.

Moreover, being receptive to diverse and dissenting views will likely yield better results. It is in the industry’s self-interest to deter silence, not only because money will be saved on fines not incurred for misconduct, but also because better ideas will be brought to the table. I believe that business performance will benefit from having a culture in which people feel empowered to speak up.

Let me give you a few examples from my own experience at the New York Fed.

I want employees to speak up. That’s why, at the start of my tenure as president, I made it clear that I wanted the “best idea to win,” regardless of where it originated or whether it contradicted something that I thought. In some instances, that will require people to admit mistakes. In that regard, I have to set the example that we all make mistakes, and that recognizing and addressing them head on—and, importantly, learning from them—is the best approach.

A few years ago we created a new group at the New York Fed called Integrated Policy Analysis. Its purpose was to consolidate teams from many parts of the organization to develop a more integrated view of the economic and financial environment to help inform our policy responsibilities. I was a strong advocate for the idea. But, after two years of effort, it became clear to me and others that it was not working as well as we had hoped. There were a lot of reasons for that, and in the end we dissolved the group and reassigned the work and staff. I let our employees know that I took a calculated risk and it didn’t work out. By doing this, I aimed to show that when things do not go as planned, the best approach is to address it, not to be silent. I hope that, when our people are confronted with disappointing results in their work, they will do the same.
I mentioned earlier that we also need to reform incentives in order to encourage people to speak up. This is hard. I'll share with you some of the change we have made at the New York Fed, recognizing that we do not have a monopoly on good ideas, nor can we claim to have a perfect culture.

* Skip-level meetings are common, and occur for the purpose of providing forums for sharing ideas. They are also a signal that escalation of problems matters to us.
* We offer training for new employees that emphasizes the importance of cognitive diversity and speaking up.
* We evaluate employees on their level of engagement with colleagues and their willingness to share insights. So, part of getting promoted is contributing diverse views and raising your hand.
* We have created programs to encourage peer recognition of good ideas, including backing for actionable initiatives selected by staff. This resulted, for example, in ideas like a "share your story" series to create institutional memory of past experiences and lessons learned.

None of these ideas is a panacea. And, I know that we have not yet achieved our goal: a culture in which employees perceive that, by raising their hands and challenging what may be an orthodoxy or conventional wisdom, they are contributing to the mission of the New York Fed. I hope, however, that with the right incentives and good leadership models, we can move closer to that ideal state: an organization characterized by fresh ideas and open dialogue.

At conferences like these, we tend to focus on the cost of misconduct. But, getting rid of scandals should not be the sole reason for changing culture. The public expects more from the financial sector than a lack of another financial crisis or scandal. The industry would do well to listen to Baroness Onora O'Neill: Think about your purpose. Surely, no one would answer that question by saying, "We're for a lack of misconduct."

Rather, the financial services industry should support a well-functioning, growing economy, reflecting the interests of all its stakeholders. Banking in particular should provide critical intermediation services—the economic infrastructure that allows businesses to grow, families to save and invest, and standards of living to improve over generations for as broad a cross section of people as possible. When society prospers, the financial services industry prospers, too. Creating a culture that encourages and rewards diversity of thought, perspective, and experience is one means by which the industry can both do good and do well at the same time.

Thank you for your kind attention.

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3. To borrow from the English writer Robert Macfarlane, “proof of competence derived only from the absence of catastrophe.” Robert Macfarlane, *The Old Ways* 133 (2012). Macfarlane was describing the navigation of the English Channel by night. In that case, perhaps the proof of competence is the absence of catastrophe.