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**MODELS FOR COMPLIANCE IN  
FINANCIAL SERVICE INDUSTRY:  
THEORY versus PRACTICE– Is a  
best practice model feasible in an  
environment of regulatory flux?**

**Wendy Burdon**

**A thesis submitted in partial  
fulfilment of the requirements of  
the University of Northumbria at  
Newcastle for the degree of**

**Doctor of Philosophy Research  
undertaken in the Faculty of  
Business and Law**

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## Abstract

The overall purpose of this thesis is to examine the models for effective compliance, and those currently adopted in practice within the financial service sector. The need for financial service organisations to maintain a robust compliance function has developed due to ever increasing regulatory demands following the most recent global financial crisis, alongside concerns over compliance culture within financial service organisations. An overarching research question exists of why the compliance function is often viewed as business inhibiting within practice.

This research engaged with practitioners with experience of working in financial service organisations and regulatory bodies. Repertory grid interviews (a technique stemming from Personal Construct Theory) explored practitioners' personal worldviews of what comprises effective compliance via consideration of experiences ranging from 'worst' to 'aspirational' compliance.

Practitioners do not align perceptions of benefits and costs of compliance in a linear fashion, when comparing worst and aspirational compliance experiences, which challenges the traditional models presented within academic literature. Barriers to regulatory compliance were highlighted, when exploring personal constructs with recurring themes of culture (management buy in) and also judgement (spirit, as opposed to, letter of the law). Compliance officer are highly aware of the importance of relationships with the regulator, and remain proactive in prioritising workload around the regulatory approach.

An alternative model for compliance is presented in the form of the 'Compliance Trust'. The model results in a compliance community which would operate independently from the financial service firms that they serve, and differs from traditional commercial consultancy or outsourcing with the emphasis on societal contribution and integrity, rather than economic motivations. The compliance trust would benefit organisations, via rotation of experience and knowledge sharing. This research provokes reflection on current practice in comparison to existing academic theories, and seeks to identify whether alternative models are viable for the future of compliance approaches within financial service practice.

*Keywords:* Compliance, financial services, regulation, shared service and outsourcing

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## Declaration

I declare that the work contained in this thesis has not been submitted for any other award and that it is all my own work. I also confirm that this work fully acknowledges opinions, ideas and contributions from the work of others.

Any ethical clearance for the research presented in this thesis has been approved. Approval was sought and granted by the Faculty Ethics Committee in January 2013.

I declare that the word count of this thesis is 81,578 words.

Wendy Burdon

SIGNATURE:

DATE:

## List of Abbreviations

|       |   |
|-------|---|
| AML   | Anti Money Laundering   |
| BIS   | Bank of International Settlements   |
| BBA   | The British Bankers Association (a leading trade association for the UK banking sector) |
| CBA   | Cost Benefit Analysis (see Section 3.5.1)   |
| CEO   | Chief Executive Officer   |
| FATF  | Financial Action Task Force   |
| FCA   | The Financial Conduct Authority (UK regulator)  |
| FPC   | Financial Policy Committee (UK)   |
| FSA   | The Financial Services Authority (UK regulator prior to FCA and PRA)                    |
| FSB   | Financial Stability Board (International)   |
| FSMA  | Financial Services and Market Act (2000)  |
| IMF   | International Monetary Fund   |
| LIBOR | London Interbank Offered Rate   |
| PRA   | The Prudential Regulation Authority (UK regulator)                                      |
| PCP   | Personal Construct Psychology   |
| RQ    | Research Question   |
| SAR   | Suspicious Activity Reporting   |



## Glossary

### Category

The word category is used to describe the collective grouping of data during the content analysis phase of research. This is consistent with the terminology applied within personal construct studies employing Honey's content analysis (see below).

### Concept

Concepts within this thesis are informed from the literature and knowledge gained from prior work experience. Specifically, the underlying questions which directed the course of this thesis (through the research flow discussed in Section 1.2) include a number of concepts. These have been contextualised within the introduction, in order to provide definitions of how these concepts have been interpreted and used within this research.

### Construct

This is a personal construct theory term. Constructs represent the personal thoughts and beliefs of individuals (descriptors for their personal experiences), and these form the major portion of data elicited from participants within this thesis.

### Corollary

Personal construct theory (see below) is underpinned by a number of corollary in order to analyse how individuals' understand, interpret and act (anticipate) based upon their experiences. These are presented in Appendix 3, as discussed in Kelly's original theoretical work, and how they have been adapted within this thesis.

### Elements

This is a personal construct theory term. In this thesis, elements represent the individual experiences explored with practitioners, ranging from worst compliance experience to their viewpoint of aspirational compliance experience.

### Eyeball analysis

This terminology is used with respect to repertory grid analysis, and represents the first stage within the analysis process. This includes the first look, and interpretation of the grid data formed during interview. This is introduced in further detail in Section 6.6.1.

### Honey's content analysis

This terminology is used with respect to repertory grid analysis, and represents a specific phase in the analysis process, to collectively group the constructs elicited during interviews with the group of participants into categories. This is introduced in further detail in Section 6.6.2. This technique is an adaptation of content analysis specific to repertory grid analysis.

### Personal construct theory/psychology

This theory stems from the psychology literature base and was developed by George Kelly (1955). The theory argues that a person's actions are informed by the way in which they anticipate events through their personal construct system. This is discussed in further detail in Section 6.1.

### Supposition

The word supposition is used to set out presumptions made by the researcher following the review of the literature, which have been explored specifically during the analysis of data in Chapter 7.

### Theme

The word theme is used to describe the collective grouping of data during the eyeball analysis phase of research, and also during the analysis of interview transcripts. This is consistent with the nature of analysis performed by the individual researcher, and the resulting discussion of themes within Chapter 7.

## Chapter 1 Introduction and context

“Scandal has been the agent for change in the growth of the new regulatory state” (Moran, 2000, p. 9)

“A more permanent solution to the prevention of future financial crises should combine enhancements in the risk management and governance practices implemented by financial institutions and their regulators, together with mechanisms that support cultural change” (Ashby, Peters, and Devlin, 2013, p. 2682)

The purpose of this chapter is to provide the rationale for this study which focuses on regulatory compliance in the financial service sector, alongside an introduction to the specific research aims and objectives. Thereafter, key compliance concepts are introduced, which are embedded within the research design. The chapter concludes with an overview of the thesis.

### 1.0 Motivations for compliance research

Following the most recent global financial crises of 2008-09, there has been significant commentary and calls for regulatory reform within academic literature (and the wider media). Entire books consider “Who is to blame?” (Davies, 2010). Others discuss contributory factors to the crises including the greed of various actors (Mason, 2009). However, financial crises and financial folly have reoccurred with regular frequencies throughout history across the globe (Reinhoff and Rogoff, 2009), with questions raised on each occurrence on “what needs to be done differently” (see Table 1, for a summary of crises). Posner (2009), whilst contributing to this literature from a US perspective, critiques both journalistic and academic discussions following the crisis, stating that many of the authors simply had “an axe to grind, or are too technical for non-specialist to understand [...], or at the other extreme are superficial” (2009, p. xiv).

The British Banking Association (BBA) have issued self-congratulatory press (BBA, 2013) since the financial crisis, regarding “sweeping changes” which have resulted in a “much safer financial system”, summarising changes to standards and regulatory changes within the sector (BBA, 2013). This self-congratulation conflicts with more recent empirical evidence from the sector, presented within survey research, where “33% of financial services professionals feel the industry hasn’t changed for the better since the financial crisis” (Tenbrunsel and Thomas, 2015, p. 3).

Table 1 Summary of crises over last century (summarised from reference to Reinhart and Rogoff, 2009, pp. 15-20)

| <b>Crisis</b>  | <b>Why different – thinking of the time</b>   | <b>Onset of Crisis</b>   |
|--|---|--|
| <b>Market default 1930s (The Great Depression)</b>   | There will not be other world wars – sustainability through greater political stability and global growth.  | 1929 global stock market crash.  |
| <b>Debt Crisis 1980s</b>                             | Commodity prices strong, interest rates low. Bank loans issued instead of bond loans - As individual banks taking up the loans incentives for information gathering and monitoring. | High interest rates and commodity price crash, precipitating defaults in developing countries.   |
| <b>Debt Crisis 1990s Asia</b>                        | Asian region had conservative fiscal policy and stability – no recent evidence of financial crisis.   | Foreign exchange rate losses precipitated IMF bailouts and resulting recessions.   |
| <b>Debt crisis 1990s-2000s Latin America</b>         | Bond debts as opposed to bank debts (perception at time of safety in bond debt), therefore, limitations for renegotiation and defaults.   | A series of financial crisis – Mexico 1994 collapse, Argentina’s \$95 billion default, Uruguay’s 2002 default and Brazil’s 1998-2002 crises. |
| <b>US lead up to global financial crisis 2008-09</b> | Globalisation, technology boom, sophisticated financial systems and understanding of monetary policy – “everything is fine”.  | US Subprime meltdown – global crisis and recession.  |

This thesis considers the context of the financial crisis from another angle; whether it is possible to ‘fix’ the problem of cyclical financial crises through regulation and compliance,

when there is an environment of “regulatory flux”<sup>1</sup>. The historical response to crises has been to introduce new regulation. However, the ideal would be to proactively prevent the continuous cycle of financial crisis, in order to avoid the environment of regulatory flux. UK financial institutions, whilst adhering to generally accepted corporate governance codes already had “codes of conduct and ethics training in place” (Llewellyn, Steare and Trelvellick, 2014, p. 13) which did not prevent or detect the underlying issues leading to the most recent financial crisis (Graafland and Bert, 2014) This indicates that (corporate governance) regulations did not proactively prevent the most recent crisis.

Incentives behind exploring the (global) phenomena of regulatory compliance are encompassed in the following extract that is part of a resignation email (from the AML director), which was uncovered as part of a (US) subcommittee investigation into failings within the HSBC (US) compliance function. This quotation provides an example of a prominent organisation disregarding the importance of regulatory compliance (in terms of authority and resource requirements), which ultimately leads to deterioration in the relationship with regulators:

“Until we appoint senior compliance management that have the requisite knowledge and skills in these areas, reduce our current reliance on consultants to fill our knowledge gap, and provide the AML Director appropriate authority, we will continue to have limited credibility with the regulators.” (US Senate, 2012, p. 24)

Alongside public enquiries into specific compliance issues, there is also limited evidence of public trust in the financial markets due to ongoing scandals within the media (mis-selling, interest rate rigging and continued ‘fat cat’ bonuses<sup>2</sup>). Proposals by Sir Richard Lambert called for an independent body acting as a “champion for better banking standards” (BBC, 2014) which suggests a lack of confidence in the current regulatory bodies. However, the

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<sup>1</sup> Regulatory flux is used in this context as an alternative description to the deregulation, crisis, re-regulation cycle, a term also used by Ayres and Braithwaite (1992), and Parker (2013). See also Section 3.3.1.

<sup>2</sup> Examples of media coverage:

Mis-selling: <http://uk.reuters.com/article/2014/08/29/uk-britain-banks-misselling-idUKKBN0GT0ZD20140829>, Libor/Interest Rate: [http://www.ft.com/cms/s/327edfb6-1879-11e4-a51a-00144feabdc0,Authorised=false.html?\\_i\\_location=http%3A%2F%2Fwww.ft.com%2Fcms%2Fs%2F0%2F327edfb6-1879-11e4-a51a-00144feabdc0.html%3Fsiteedition%3Duk&siteedition=uk&\\_i\\_referer=http%3A%2F%2Fwww.ft.com%2Findepth%2Flibor-scandal#axzz3EPWg1Sd4](http://www.ft.com/cms/s/327edfb6-1879-11e4-a51a-00144feabdc0,Authorised=false.html?_i_location=http%3A%2F%2Fwww.ft.com%2Fcms%2Fs%2F0%2F327edfb6-1879-11e4-a51a-00144feabdc0.html%3Fsiteedition%3Duk&siteedition=uk&_i_referer=http%3A%2F%2Fwww.ft.com%2Findepth%2Flibor-scandal#axzz3EPWg1Sd4), UK Banker Bonuses: <http://www.ft.com/cms/s/0/622344e2-2f5c-11e4-83e4-00144feabdc0.html#axzz3EPWg1Sd4> All accessed July 2014.

emphasis on new regulation and supervision standards may not be the solution to restore public trust.

The idea of over regulating (and over auditing) resonates with the concepts of the “audit society” of the late 1980s onwards, which may be applied to any sort of “monitoring activity” discussed by Power (2000, p. 114). However, questions arise to whether there are feasible alternatives, from the societal perspectives when trust is lacking.

“We audit, and we regulate, when we cease to trust” (Moran, 2000, p. 10)

The evolution of regulation (and deregulation) and compliance therewith, can be closely coupled to the theoretical development of both regulatory economic theory and principal-agent theory. Therefore, economic theory including the regulatory cycle acts as a theoretical base reference point through the course of the research project. Institutional theory (DiMaggio and Powell, 1983) is also considered a useful lens to review the literature; from both the perspective of regulatory-setting agencies and political influence (Clark, Jr. and Demirag, 2006), and also from the perspective of firms or management complying with the resulting regulation. Moral development theory (Kohlberg) is also a common theory used to explain management decision making processes (Crane and Matten, 2010), and so links were explored from this theoretical perspective through the course of the literature review, to consider the motivations for management to comply.

At an early stage within the research a summary to link the theoretical references considered during the course of this thesis was developed including: Jackman’s values and culture/ethical framework of compliance; moral development theory; Ayres and Braithwaite’s Enforcement Pyramid; and institutional theory (this early thought experiment is included for reference in Table 2). Each of these models and theories are discussed further within the review of the literature (for specific discussion of underpinning theory in reference to motivations to comply, see Section 2.4). Jackman’s model was chosen purposely as this was published during 2001 and 2002 from practitioner/regulator (the Financial Services Authority, FSA) viewpoints prior to the most recent financial crisis (whilst Jackman was Head of Ethics at the FSA). This model expressed the importance of ethical banking, which aligns to more recent calls for virtue and a Hippocratic Oath by

bankers<sup>3</sup>. Therefore, it is relevant to revisit these models, and consider from a current perspective by exploring practitioners' constructs of compliance<sup>4</sup>, with an emphasis on the challenges faced within the industry. Recent studies have also revisited ethics within banking, including a mass survey of over 1,200 financial service professionals which indicated some disturbing perceptions within the industry:

“Nearly one in five respondents feel financial services professionals must at least sometimes engage in illegal or unethical activity to be successful” (Tenbrunsel and Thomas, 2015, p. 3)

Therefore, it is within this environment of personal gain, relative to personal morality concerns that the insights of compliance officers are explored within this thesis.

## 1.1 Research aim and objectives

“these developments [regulatory capitalism<sup>5</sup>] create a practical and theoretical demand for at least two types of social science research on regulatory compliance: research aimed at understanding how people conceptualize and socially construct compliance; and research that seeks to explain the causes and effects of compliance” (Parker and Nielson, 2009, p. 47)

Prior to commencing this thesis, the author worked in an accounting role within a multinational manufacturing company. During the period of employment with this company (2002-2012) the methods adopted by the compliance managers had evolved and changed. These changes included going through the pain of complying with the US Sarbanes Oxley Act (SOX), to delisting (from the US) and modifying the compliance approach to risk-management, and self-assessment of controls<sup>6</sup>. Therefore, at the start of this research, personal thoughts and existing knowledge of compliance were dominated by questions around the practical implications of how to improve compliance.

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<sup>3</sup> Calls for a Hippocratic Oath by bankers <http://www.theguardian.com/sustainable-business/banking-reform-bankers-hippocratic-oath-report>; <http://www.bbc.co.uk/news/business-28535001>. Media coverage following the issue of the ‘Virtuous Banking’ report (Llewellyn et al., 2014). Oaths have also been considered by Bruin (2014) and related to ‘enhancing compliance’.

<sup>4</sup> The concept of ethical compliance continues to be an area for publication within the media, but receives less attention from academics – see Section 4.3 and also: <http://www.independent.co.uk/voices/commentators/david-jackman-business-wont-be-ethical-until-it-shares-societys-values-again-7965044.html> accessed January 2015.

<sup>5</sup> Regulatory capitalism in this article is defined as ‘the proliferation of both market and state and non-state attempts to regulate the markets and business conduct’ (Parker and Nielson, 2009, p. 45).

<sup>6</sup> The company adopted the principles of the COSO framework. See the latest guidance on Internal Control – Integrated Framework at <http://www.coso.org/IC.htm> accessed July 2015.

Within this research thesis the theories surrounding compliance function methodology, have been explored through a review of the existing literature base (see Chapters 3 to 5). On reflection, my personal knowledge relating to financial service compliance has expanded enormously during the course of this doctoral study from a very naive ‘tick box’ attitude, towards an expanded knowledge incorporating ethics and culture within compliance approaches.

The specific aim of this research project is to explore whether it is possible to identify a best practice model of compliance for the banking sector, in light of the changing regulatory cycle (or “regulatory flux”).

The underlying research objectives<sup>7</sup> to achieve the overall research aim are:

1. To understand the motives for regulatory compliance by banks in the UK
2. To explore the different structures of regulatory compliance in operation
3. To investigate the circumstances under which different approaches to compliance would be adopted

A pragmatic approach has been adopted to explore these objectives. Reference should be made to Table 8 within the methodology chapter for a mapping between outlined research objectives, literature, and specific research questions with proposed methodology. The research design is presented in Section 1.2.8 following a discussion of the key concepts driving the research flow of this study.

## **1.2 Setting the context within the research flow**

There are a number of key concepts embedded within the research aim and objectives. In order to set the context for the remaining chapters, it is appropriate to define the underlying assumptions, and the linkage between these concepts. These concepts follow a natural flow which has directed the course of this thesis, and the commitment is to contribute to knowledge through this research flow. The research flow (see Figure 1) starts with an overriding question of; why is a compliance officer/function necessary, and what are the firms complying with. This leads to an exploration of regulation. This advances to an examination of how firms can comply with the regulation, exploring compliance models. Finally, this then considers; what is seen to be best practice, and why do firms choose

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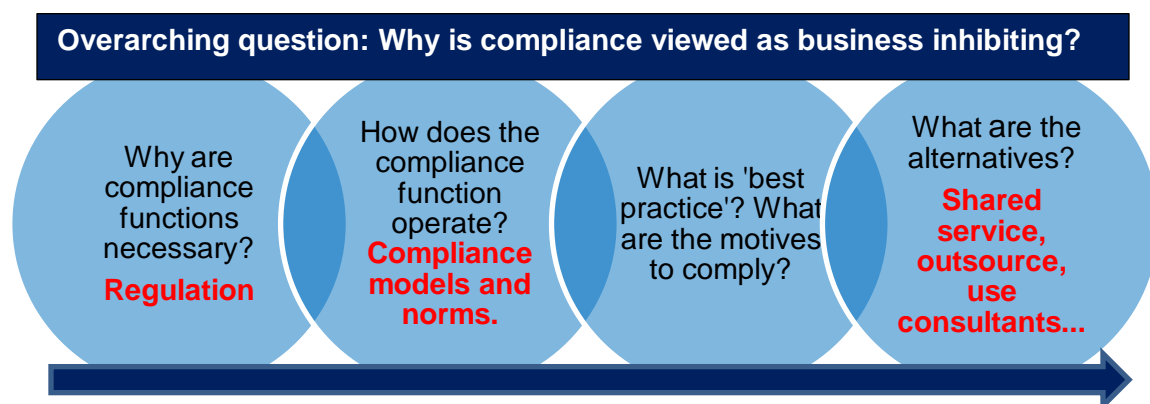
<sup>7</sup> Note that the research objectives are linked to underlying literature in each of the literature chapters, where specific research questions are formed. There is a further summary to map research objectives, to literature, to specific research questions (and adopted methodology) in Table 8.



certain strategies to comply with regulations. Underlying these specific questions, there is recognition of the importance of practitioner feedback throughout the course of the data collection, where compliance is variously described as ‘costly’, ‘business inhibiting’ ultimately a ‘nuisance’. Uncertainty remains as to whether there are potential alternatives to the current approach that firms are taking within both the financial service sector, and more widely across the corporate world.

Each of the questions, and the associated concepts will now be discussed in turn in Sections 1.2.1 through to Sections 1.2.7. The impact on research design is then presented in Section 1.2.8.

Figure 1 Development of research flow



### 1.2.1 Why are compliance functions necessary? Regulation in the context of financial regulation and compliance

Regulation in the financial services industry continues to be an area of interest and concern for both academics, and the broader public. As stated by Alexander (2006), financial regulation is necessary because of the multiplier effect that banking activities have on the rest of the economy, something which was witnessed in the most recent worldwide financial crises and resulting worldwide recession. The ultimate cost of the US real estate crisis (2007), the systematic meltdown in global financial markets (2008-2009) and the sovereign debt crisis (2010-2012) is inevitably borne by tax payers and broader society (Omarova, 2012). The magnitude of the societal impact demands attention from academics (Arnold, 2009). Despite regulatory failures being blamed by a wide audience for the financial crisis (Davies, 2010; Turner, 2009), we must also consider the role of compliance officers in the lead up to the crisis and their relationship with the regulators.

Following earlier crises and the implementation of Sarbanes Oxley<sup>8</sup>, in house legal and compliance departments (risk management or any such variant) within the financial service firms “were large and visible” at the time of the most recent financial crisis (Langevoort, 2012, p. 497). Consequently, the role of compliance officers and governance within these organisations must then be considered. It may be questioned whether the compliance functions were working effectively, despite the occurrence of the crisis. The initial assumption might be ‘No’. However, it is perhaps unfair to scapegoat<sup>9</sup> the compliance officers for the global failings of the industry.

### 1.2.2 How does the compliance function operate? Defining compliance norms

Compliance is defined (Oxford Dictionary, 2015) as the action or fact of meeting rules or standards. Regulatory compliance can consequently be described as the act of meeting regulation and legislation set out by the state or appointed regulator. As mentioned, the initial interest in this topic results from the author’s personal experience of working in a compliance role, albeit in a different business sector. In this environment, compliance was often viewed as a barrier or an annoyance to the business, whilst requiring significant investment of resource (for example staff time, system cost, consulting costs)<sup>10</sup>.

The compliance function representatives have significant roles in a relational, and communication capacity within organisations. Parker (2002, pp. 132-133) discusses the task of compliance professionals in “translating broader social and legal values into the particular and plural worlds of their organisations”, or in layman’s terms acting as a middleman:

“To harmonize business and regulatory goals and, therefore, assist good companies to be good citizens through their own two way role in regulatory effort as compliance professionals” (Parker, 2002, p. 133)

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<sup>8</sup> The Sarbanes Oxley Act of 2002 was introduced in the United States, in an attempt to reform accountability within the corporate sector, and audit independence, in order to protect investors from fraudulent activities (as evidenced in the case of Enron). See also <https://www.sec.gov/about/laws/soa2002.pdf> accessed November 2015.

<sup>9</sup> A prominent example of scapegoating would be that of HSBC’s Chief Compliance Officer (Mr Bagley) resigning following appearance at US Senate Hearing in 2012 <http://www.ft.com/cms/s/0/5267a2ce-d02b-11e1-99a8-00144feabdc0.html#axzz3kaiah0VO> accessed June 2015.

<sup>10</sup> Compliance became an additional role to existing duties as the author’s career progressed. From a personal perspective this became an ever expanding role year on year due to increasing regulatory and organisational demands.

The Basel Committee on Banking Supervision (2005) stated:

“Compliance starts at the top [...] it concerns everyone within the bank and should be viewed as an integral part of the banks’ business activities” (p. 7)

Compliance risk is defined as the risk of legal or regulatory sanctions, material financial loss or loss to reputation that a bank may suffer as a result of failure to comply with applicable laws, regulations, rules, related self-regulatory organisation standards, and codes of conducts (BASEL, 2005). This report stressed the need for the compliance function to be independent and sufficiently resourced, with clearly specified roles and activities, subject to review by internal audit.

### 1.2.3 How does the compliance function operate? The concept of compliance culture

“Implementing the right culture in a firm means changing its values, attitudes and beliefs so that they accommodate unequivocally the broad principles driving financial regulation” (Newton, 2001, p. 16)

“the cornerstone to starting and maintaining an ethics and compliance culture is a shared set of values and standards – a shared understanding that it applies to all employees regardless of their level in the organisation” (Barry, 2002, p. 39)

Academic and practitioner literature has focused on the concept of compliance culture being embedded within the firm (Newton, 2001). Culture may be considered to be embedded within an “organization’s objects, systems and structures”, which are in effect owned in practice by management (Smith, 2000, p. 154). However, this literature does not account for the turmoil in the compliance function that was brought about by the most recent financial crisis. Compliance culture remains an area of concern for the regulator, on which they have clearly reacted to violations in the form of sanctions, and issue of policy guidelines. The regulator has issued discussion papers related to culture both pre- and post-crisis (FSA, 2007, reissued 2013 by the Financial Conduct Authority (FCA); and Prudential Regulation Authority (PRA), 2014). Despite publically issued statements and documents (and announcements of sanctions) the sector continues to be plagued by compliance violations. More recently the regulator issued significant fines (£284 million) to Barclays in response to the FOREX failings, whilst blaming culture (FCA, 2015a). Quoting Georgina Philippou (the FCA’s acting director of enforcement and market oversight):

“Instead of addressing the obvious risks associated with its business Barclays allowed a culture to develop which put the firm’s interests ahead of those of its clients and which undermined the reputation and integrity of the UK financial system. Firms should scrutinise their own systems and cultures to ensure that they make good on their promises to deliver change” (FCA, 2015a, p. 1)

Irrespective of education and training provided to practitioners, implementation of an appropriate compliance culture includes inherent difficulties in changing an individual’s personal moral compass. Despite expanded personal awareness of ethical models gained during the completion of this thesis, a psychometric analysis<sup>11</sup> undertaken by the researcher in January 2015 still indicates tendencies of tick box mentality as an “enforcer” (suggesting disregard of the principles, and instead following the letter of the law). The same test performed on over 2000 bankers indicates a higher level of “virtue” within the banking community in comparison to the general population (Llewellyn et al., 2014). This perhaps demonstrates the impact (and heavy focus) of education and training, including focus on compliance culture within the industry<sup>12</sup>. However, recent scandals as discussed above appear to contradict the high virtue findings of this survey<sup>13</sup>.

More recent literature on culture appears to be focused on the regulators’ response (O’Brien, Gilligan and Miller, 2014; Ring, Bryce, McKinney and Webb, 2014), rather than positioned from the compliance officers’ viewpoint, which is the focus of this study.

#### 1.2.4 What is best practice?

Best practice is a term that seems to have an unambiguous meaning to most practitioners, and business manager are encouraged to strive for this within their teams, irrespective of their operational function. Academic literature does not ignore this phenomenon. Strategic management literature provides a theoretical background to the difficulties in achieving best practice, with blame on “motivational factors” and “barriers to internal knowledge transfer” (Szulanski, 1996). Policy options for regulators, suggested by Michael, Falzo and Shamadasi (2015), include reference to “government sponsored exchanges of compliance best practice”.

<sup>11</sup> See <http://moraldna.org/> accessed January 2015.

<sup>12</sup> An example would be the introduction of compliance training partnership between Barclays and Cambridge in light of recent scandals:

<http://www.telegraph.co.uk/finance/newsbysector/banksandfinance/10944916/Barclays-and-Cambridge-University-set-up-compliance-school.html> accessed November 2014.

<sup>13</sup> Refer also to Footnote 1.

However, a crucial difficulty in this research is exploring whether organisations and individuals are motivated to strive for best practice, and for whose interest best practice should be considered. Individual and organisational psychology (and motivations), undoubtedly vary within the financial service industry. In recent scandals there has been a public outcry<sup>14</sup>, with an apparent disregard for best practice. However, it may be argued within the media that financial institutions were engineering best practice towards themselves as individual institutions, or their major customers, with limited regard for societal impacts of their actions. This discussion can also be widened in to a consideration of how best practice is viewed in terms by stakeholder groups. There have been criticisms of the financial service sector with respect to “inadequate consideration of stakeholders” (Cuganesan and Khan, 2008, p. 86).

### 1.2.5 What are the motives to comply?

However, what are the reasons (motives) for managers choosing best practice (or alternatives). Decision making (the action or process of reaching important decisions) has been explored widely within business research literature. Cyert and March (1963) “behavioural theory of the firm” is widely cited within organisational studies literature, with regard to decision making. This theory moved away from viewing firms as profit maximizing entities, and alternatively viewing firms as a “coalition of participants” with many conflicting goals and objectives, to which firms will respond by using standardised decision rules. However, business ethicists are “largely concerned with obligations that go above and beyond what is required by law (that is with justifying beyond compliance obligations)” (Norman, 2011, p. 43).

When considering these motivations for “beyond compliance” (Norman, 2011), or alternatives, during compliance decision making, a wider discussion of stakeholders may also be relevant.

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<sup>14</sup> Any number of media articles could be considered to demonstrate this point. However, the recent media attention towards HSBC tax evasion scandal has been selected (see webpages below). Events from 2005-2007 were brought to the attention of the public by the media in February 2015. However, regulators and officials in a number of jurisdictions were aware of the issues at much earlier date (email from whistle blower was reported to have been sent March 2008). This does not represent best practice or transparency by either the regulator (HMRC, from a UK perspective), and the organisation itself (HSBC). The question could be raised as to whose interest was burying this information best served.

<http://www.theguardian.com/business/2015/feb/11/hmrc-official-mps-hsbc-pull-out-edward-troup>

<http://www.bbc.co.uk/news/business-31450005> accessed February 2015.

“That is, who (or what) are the stakeholders of the firm? And to whom (or what) do managers pay attention?” (Mitchell, Agle and Wood, 1997, p. 853)

This is a peculiar complication within this study that focuses on compliance professionals worldviews. Traditionally they hold positions within, and are paid by the financial service organisations that they serve, acting as the middleman between the regulators and these organisations. Therefore, the consideration of stakeholders from the worldview of the compliance officer is of direct relevance when considering the motivations during decision making. There may be difficulties in determining which stakeholders the compliance officers pay attention to.

### **1.2.6 What are the alternatives? Shared service/outsourcing/consulting**

During the course of this thesis the generally accepted models of compliance (from a practical perspective) are that of the in-house compliance function and the ‘alternatives’ including: use of compliance consultants; shared services; and outsourcing. The generally accepted motivation for outsourcing is to reduce cost or to transfer risk. Shared service may be considered a ‘within the firm’ form of outsourcing. Ulbrich (2010), in his case study of shared services within a public sector organisation, summarises that the essential principles behind shared service are:

“to make better use of internal resources by eliminating costly duplication of staff functions in decentralised organisations and concentrating subsets of existing business functions into one or a small number of new, semi-autonomous business units –the shared services” p. 251

Originally, an element of personal bias exists within this thesis, in order to explore the reasons why firms pay high fees to consultants in relation to compliance, when it is seen by many practitioners as a business inhibiting function. However, during interviews with practitioners, and also whilst obtaining feedback on the resulting model of this study, consultants were an area of interest for practitioners, with significant discussions arising on their role (this is revisited in Chapter 8). Therefore, the inclusion of consulting would seem inevitable in a study such as this.

### 1.2.7 Overarching question (and central argument): Why is compliance viewed as business inhibiting?

During introductory discussions with prospective participants for this study, comments were made that compliance was a 'nuisance/business inhibiting/a barrier or a hurdle' for the business to overcome. This reoccurred on a number of occasions during interviews and so this is an important mindset to introduce within the context of this research. This results from the hurdles that compliance place in the form of processes and monitoring within financial service firms, ultimately to adhere to regulation. So compliance acts as the middleman between the regulators and the business. However, risk taking and failures within the regulatory structure are seen as root causes influencing the most recent financial crisis (see Section 3.4). Therefore, the necessity for this compliance barrier for social purpose is clear (and inevitable). There are already calls in the existing literature for a movement in attitude towards compliance:

“Cultural change should be both organization wide and function specific, particularly in relation to moving the attitudes of risk functions away from compliance and towards a more business-like orientation where risk management staff and risk reports are used to support strategic decision-making” (Ashby et al., 2013, p. 2682)

This question acts as the central argument within this thesis. Why is compliance seen as business inhibiting, and are there alternative routes to regulatory compliance within the financial service sector?

A more worrying question within the (global) media and political arena is the apparent disregard of some banking organisations to regulation. Quoting Congresswoman Maxine Waters, a discussion is highlighted around the apparent disdain of some organisations to the significant fines issued by regulators in the US (an argument which has been echoed across global jurisdictions).

“the banks in question accounted for 25 percent of the \$500 billion-a-day dollars-to-euros spot market, meaning this so-called 'record fine' is literally a drop in the



bucket [...] Banks that are merely fined for their criminal activity and suffer no material impact simply view such penalties as the cost of doing business.”<sup>15</sup>

Again this discussion raises questions over the barriers facing compliance professionals in this global industry which has a poor public persona, whereby the expectation is that banks will continue to break regulatory codes and simply accept this as a cost of business. This concept (and central argument) is revisited in light of the findings of this study in Chapter 8 (when formulating and reflecting on feedback on the conceptual model), when considering the achievement of research objectives, and the implications on theory and practice.

### 1.2.8 Research Design

Following, identification of the research objectives in Section 1.1 and the development of the research flow (and associated concepts) in the preceding sections, the design for this study is presented in Figure 2. This diagram represents the (stepped) framework that has been followed in order to complete this research.

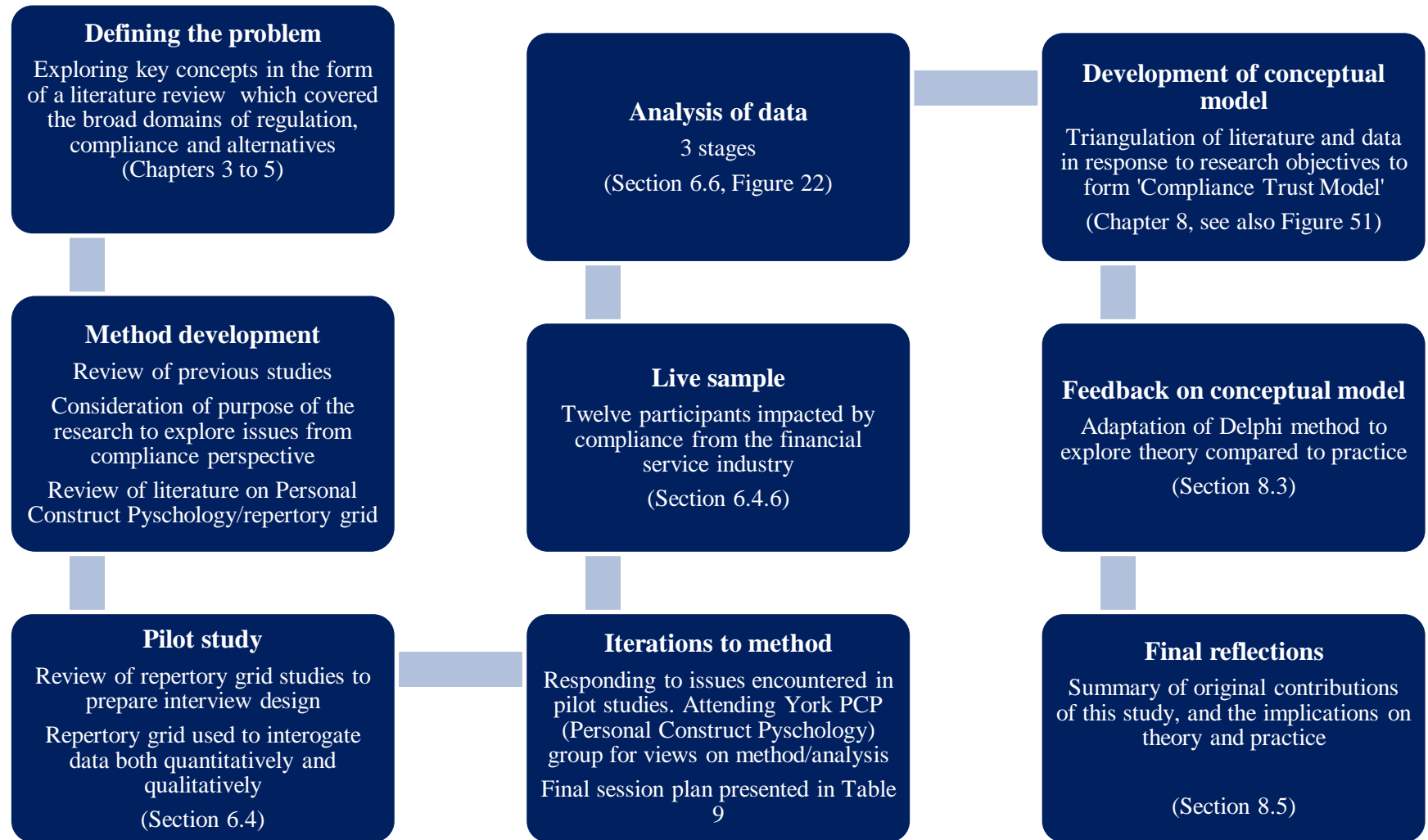
The first stage was to define the problem, which involved a broad review of the literature (which is presented in Chapters 3 to 5). The next phase was to develop the method (utilising repertory grid interview), which involved review of prior studies and completion of a pilot study. Following the pilot study, there were iterations to the method (as a result of problems identified at the pilot stage, and also due to discussions with more experienced researcher including the Personal Construct Psychology (PCP) group). A final session plan was developed which is included in Table 9. Following the finalisation of the methodology, data was collated from practitioners. The data was then analysed in three stages (described in Section 6.6) and presented in Chapter 7. Through triangulation of the literature and the data collated in this study, a conceptual model was then developed which is presented in Chapter 8. Feedback on the conceptual model was then sought from both practitioners and other academics. Following completion of the research, reflections were then made on the contribution (which is presented in Chapter 8).

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<sup>15</sup> This quote originates from a statement released 20 May 2015. See webpage: <http://democrats.financialservices.house.gov/news/email/show.aspx?ID=WSRLNK55XFK2M> accessed June 2015.



Figure 2 Research design



### 1.3 Context of tacit, implicit and explicit knowledge

To achieve the objectives of this research it was essential to develop an understanding of issues surrounding the relationship and communication of knowledge between compliance professionals, regulators and third parties such as consultants, outsourcing (and even internal shared services). An exploration of managers' behaviours and how decisions are reached (sense making) is undertaken within this study.

Due to the exploratory nature of the research objectives, the research design must capture how practitioners make sense of the issues. There is a close link to tacit, implicit and explicit knowledge within organisations and individuals, so this consideration of 'knowledge transfer' has resulted in the chosen methodology of repertory grid (which is discussed in depth in the Methodology, Chapter 6). Under the philosophy of constructive alternativism (Section 6.1), each individual invents or constructs a way of construing and interpreting our experiences (of surroundings and events). Therefore, understanding tacit knowledge and knowledge transfer is fundamentally important to this research thesis:

“The concept of knowledge creation is fundamental to organizational knowledge creation theory and important to organization science, because it explains how new ideas come forth in innovation, not only how individuals tap into rich practices and acquire the tacit knowledge of these practices” Nonaka and von Krogh (2009, p. 645)

The initial link within this piece of research to knowledge exchange (and related theories of “organizational knowledge creation theory” and the concept of “knowledge conversion”), was made during attendance at a research seminar, which has since been published (Brennan, Kirwan and Redmond, 2015). One of the main advantages of the repertory grid technique (the method of data capture employed within this thesis) is to explore and uncover tacit knowledge. However, continuing debate, and calls for further research exist amongst academics with regard to knowledge transfer. Questions are raised as to whether it possible to convert explicit knowledge to tacit knowledge and vice versa (Smith, 2001, p. 316; Nonaka, 2009, p. 638).

Nonaka and von Krogh (2009) define tacit knowledge as “knowledge tied to the senses, tactile experiences, movement skills, intuition, unarticulated mental models, or implicit rules of thumb” (p. 636). Referring to Polanyi's earlier 1967 work, tacit knowledge is likened to skills such as “riding a bike” or “knowing more than we can tell” (Smith, 2001, p.

314). Explicit knowledge conversely is knowledge which can be written down, or set out as procedures within organisations.

A major obstacle exists in transferring tacit knowledge to explicit knowledge within organisations. Smith (2001) comments on a number of strategies for knowledge transfer and learning by observation including; “knowledge warehouses”, “communities of practice”, or “best practice repositories”. However, difficulties remain in documenting tacit knowledge as this involved “expressing the inexpressible” (Smith, 2001, p. 36). To a certain extent this can be seen within the banking community in organisations such as the British Banking Association (BBA), as a means of communities of practice. However, there is always the complication of trust (and self-preservation) between individuals and organisations participating in such groups. Nonaka and von Krogh (2009) refer to the “tacit explicit knowledge continuum” as a process of “expressing certain aspects of tacit knowledge” and documenting this as explicit knowledge within (or even between) organisations (p. 642).

Nonaka and von Krogh (2009) expand the discussion much further on knowledge transfer and discuss the alignment of pragmatist philosophy to organisation knowledge creation, whereby “pragmatists adopt various solutions to explain how ‘reality’ interacts with an individual knowledge” (p. 639). This also aligns to the direction of this research thesis, whereby the researcher is seeking to understand how the knowledge and experiences of individual financial service practitioners may influence the decision making over compliance approaches.

#### **1.4 Contribution and central argument**

This thesis makes a number of contributions to existing academic literatures (which are discussed further in Section 8.5). This thesis challenges and extends existing literature on regulatory and compliance approaches, in comparison to practitioners’ views. In addition, this thesis demonstrates the application of a lesser used methodological tool of repertory grid, within compliance business research (see Section 6.4, and Appendix 4 for discussion).

Hopwood (2007) commented on the “detachment” between practice and academia. Berry, Coad, Harris, Otley and Stringer (2009) also commented that “control research needs to build a new knowledge production process to enable better and more fruitful links between practice and theory”. The intention, through this research topic and methodology to collect

data from practitioners, is to help close the compliance practitioner/academia gap and contribute to theoretical knowledge, in light of both the current extensive regulation requirements and also new legislation and regulation requirements, in the financial service industry. This goal has been partially achieved through disseminating and receiving feedback to a broader audience of experts (through wider distribution of the resulting conceptual model, see Section 8.3). This demonstrates how research can be “relevant and rigorous, to serve the scientific enterprise even while doing work that informs policy and practice” (Pfeffer, 2007, p. 1342)

The timing of the data collection of this research (during 2013-2014) coincided with an extremely difficult period in the regulatory cycle for both regulators and the practitioners, who continue to face significant changes and disruption following the aftermath of the 2007-2009 financial crisis. The changes to the UK regulatory regime following the Financial Services Act of 2012 are discussed in Chapter 2.

The findings offer a link between existing models of regulatory compliance within the literature, with the major (current) concerns of compliance professionals. Through analysis of the data collated the significant drivers and barriers for compliance have been identified and compared to existing models. Existing literature promotes a variety of drivers for compliance, however, the findings of this study indicate instead that more focus is required on the barriers to compliance. Based on the review of the literature and the analysis of the findings a conceptual model has been presented to practitioners for comments (see Section 8.3) on potential alternatives to current practice.

## 1.5 Overview of the thesis

“One has to train oneself constantly to write and speak in a clear and simple language. Every thought should be formulated as clearly and simply as possible” (Popper, 1976, p. 292)<sup>16</sup>

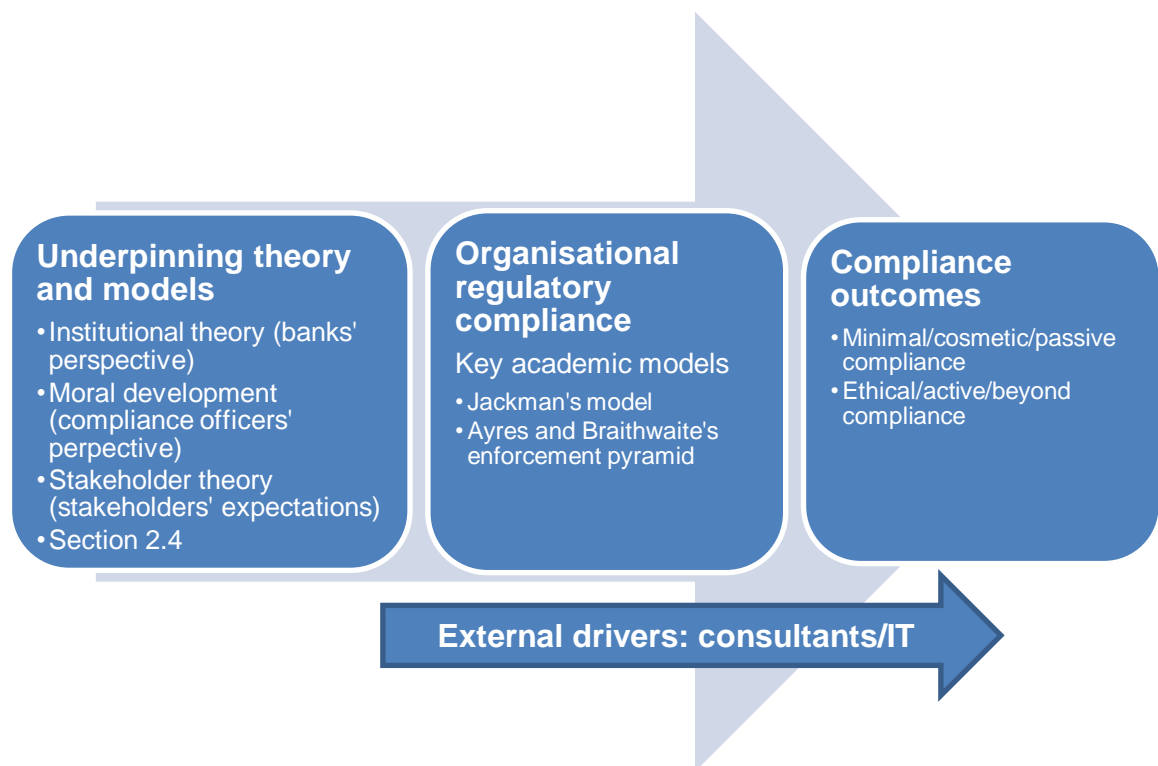
The above quote, despite its positivist routes, has been an important mindset whilst writing this thesis which is broadly qualitative in design. In order to facilitate this, mind maps and visual representation have been used throughout. A summary of each of the chapter is set out in Sections 1.5.1 through to 1.5.5.

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<sup>16</sup> This ‘post positivist’ quote is referenced in Silverman’s 2013 guide to ‘qualitative research’ as part of his ‘anti bullshit agenda’.

Figure 3 summarises the underpinning theoretical inputs, key models reviewed in this study, and the extremes of potential compliance outcomes. The main drivers of compliance are presupposed from a normative viewpoint as meeting regulation and meeting expectations of stakeholders, which drives the organisation's compliance strategy. There are external factors which can be used to greater or lesser extent to drive strategy such as tooling and use of consultants. Ultimately (and simplistically<sup>17</sup>) this will lead to two extremes of compliance in the form of "active" or "passive" compliance (Crump, 2007).

**Figure 3 Author developed theoretical inputs and outputs map to summarise an organisation's compliance strategy**



A number of theories were considered to align to the principles set out within Jackman's model (which is discussed further in Section 4.3). Table 2 was developed to summarise thoughts on this broad alignment. The linear scale of Jackman's model is seen to have a direct and inverse alignment to the enforcement pyramid set out by Ayres and Braithwaite (1992). However, similarities may also be considered with linear extremes of Kohlberg's moral reasoning, and to a lesser extent to institutional theory. Kohlberg's theory is relevant

<sup>17</sup> Of course this is a simplistic process map which does not fully consider the implications of ethics and culture which was explored in more depth following the review of the literature. The main drivers (personal constructs) have been analysed and incorporated in the model through the discussion in Chapter 8.

from the personal nature of this research which focus on the compliance officer's role within the organisations they serve (and hence personal morality issues arise). Institutional theory applies, due to the nature of compliance which is viewed at an organisational level by regulators and wider society. However, it should be noted that institutional theory is not without its critics, due to the perception that institutional theory overlooks "the role of the manager, thereby falsely assuming that organizations are passive entities whose course is shaped by institutional context" (Fashola, 2014 p. 3, quoting Bada et al., 2004). Within this thesis, there is a contribution to the literature using the personal constructs of managers, which impacts at the organisation level through compliance (which acknowledges the institutional context). The Literature and Conclusion Chapters reviews alignment to these theories in further detail (specifically Section 2.4, and Section 8.5).

A summary of each of the chapter is set out in Sections 1.5.1 through to 1.5.5.

**Table 2 Initial integration of Jackman's ethical framework, Kohlberg's moral reasoning, Ayres and Braithwaites' responsive regulation and institutional theory (discussed further in Section 2.4, and the literature chapters)**

| Jackman's Model:<br>Culture, the FSA's role and the Firm's value and culture (2001)*                                     | Kohlberg's Six stages of moral reasoning (1958, 1977)<br>(Perspective of the individual)                              | Ayres and Braithwaites' Enforcement Pyramid (1992)<br>(Perspective of the Regulator) | Institutional theory (DiMaggio and Powell, 1983)<br>(Perspective of the firm) |
|--|---|--|---|
| Minimum standards:<br>FSA's role, Policing.<br>Firm's values,<br>Unthinking/mechanical compliance.                       | Pre Conventional Stage 1 - Punishment and obedience, and Stage 2 - Instrumental purpose and exchange (self-interest). | Command Regulation: Sanctioning, Insistent Strategy, Broadly Accommodative.          | Coercive  |
| Aspirational Culture:<br>FSA's role, Persuading/Educating.<br>Firm's values,<br>Sound intentions and approach.           | Conventional Stage 3 - Interpersonal conformity<br>Stage 4 - Social accord and system maintenance.                    | Persuasive Strategic Accommodative, Education, Advice, Persuasion                    | Mimetic   |
| Ethical Culture:<br>FSA's role. Educating/Consulting.<br>Firm's values, Competence and ethical framework.                | Post Conventional Stage 5 – Social contract and individual rights.  | Enforced Self-Regulation Supervisory Role  | Normative   |
| Sustainable Regulation:<br>FSA's role, Mature Relationship.<br>Firms's values, Internalise ethos of statutory objective. | Post conventional Stage 6 – Universal ethical principles.   | (no mapping made)  | (no mapping made)   |

\*Note that the direction of arrows indicates positive movements in behaviours, from the perspective of individuals, the regulator and the firms.

### 1.5.1 Chapter 2 Boundaries of this research – background to the UK regulatory framework

The purpose of this chapter is to provide some context to this study, in terms of the different approaches to regulation that are adopted in the UK (and the impact of global regulation). This study is limited to a sample of data collated from participants working within the UK. However, due to the globalisation of the banking industries there is often overlap between the literature, and indeed to the personal viewpoints of participants (when considering UK, European and global reaches of regulation, and compliance thereon).

### 1.5.2 Chapters 3, 4 and 5 Literature – regulation, compliance and alternatives

“In what circumstance and for what reasons are businesses most likely to comply with different types of regulation? And, when businesses do comply, does their compliance behaviour achieve the public policy goals that motivated the regulation in the first place?” (Parker and Nielson, 2009, p. 49)

The quote above holds close alignment to the direction the literature review has taken through the course of completion of this thesis. The literature was explored initially under the concept of ‘read, read and read a bit more’ which certainly would not be classified as a systematic approach to reviewing the literature. The advantage of this approach has been the breadth, and cross discipline contribution within the literature review.

The literature has been reviewed<sup>18</sup> (and split into distinct chapters) under the broad areas of regulation literature, compliance literature and shared service/outsourcing. Within the regulatory literature a central model which has directed this study is that of responsive regulation (Ayres and Braithwaite, 1992), which is discussed in Chapter 3. An inverse relationship between the “responsive regulation” model and a practitioner model proposed by Jackman in 2002 is explored (see Section 4.3). Although other models have been proposed within the literature, responsive regulation is widely cited within the literature even up to 2014. Jackman’s model is less widely cited, and the probable cause for this is the distinct lack of academic research in the financial service compliance sector. However, the concept of ethical compliance on which this model is based is broadly accepted within practice, so this model has been used to bridge the academic/practice divide. To explore possible alternatives to existing compliance

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<sup>18</sup> This was achieved through a manual process of sorting and linking key concepts from reviewed articles, via summary tables (in word) and mind maps.



models, the shared service and outsourcing literature has also been reviewed in order to understand the motivations for compliance managers adopting alternate compliance approaches.

A gap analysis of the literature is presented at the end of each chapter to summarise and align the literature review to the resulting research questions, and remaining gaps.

### **1.5.3 Chapter 6 Methodology**

The initial research proposal identified a mixed methods approach. Through reflection of the overall aim of the research, an exploratory research design was developed, utilising repertory grid tooling within interviews with practitioners.

The preparation of this chapter derived the greatest sense of achievement during completion of this thesis. The wide variety of research methods and alignment to personal philosophy was (an enjoyable!) journey of discovery during this doctoral study. A great affection for Personal Construct Psychology/Theory has developed. The opportunity to explore tacit knowledge through story telling within the grid interviews (Gray, 2007), directed this study from a very early stage within the research project.

Engagement with more experienced academics was essential for development of this section. Colleagues within the Business School, and the Northern PCP (Personal Construct Psychology) offered sage advice towards the individual choices made within this chapter. This also exposed the researcher to a variety of research disciplines and worldviews. Ultimately the methodological tool of repertory grid and analysis thereof became a very individual interpretation of personal construct theory (as endorsed by Northern PCP group) underpinned by prior academic research, which aligns closely to the pragmatic philosophy adopted within this thesis.

### **1.5.4 Chapter 7 Findings and analysis**

This chapter reflects on the data collection process. Data has been analysed in a number of ways reflecting the pragmatic use of the output of repertory grid interviews. The data collected during interview included both the personal constructs expressed by practitioners during the formation of their grids, and also the interview transcripts which acts as “story telling” (Gray, 2007) of the practitioners when forming their grids. This results in three distinct explorations of the data, firstly under “eyeball analysis” (Jankowicz, 2004), followed by interrogation of the constructs using “Honey’s content analysis” (1979), and finally thematic analysis of interview transcripts.

Agreement and reliability of the content analysis performed is also considered, with a discussion of inter judge/rater reliability using both Cohen's Kappa and Krippendorff's alpha. The importance of assessing this agreement was highlighted in the first iteration of coding which had poor alignment between coders. This led to further refinement of the coding templates, which also aided underlying theorising throughout analysis.

The data analysis is presented and aligned to the research questions presented in the methodology, alongside four main supposition statements. The results of the category formations and analysis of interview data is summarised (in terms of 'fact') and taken forward into the Chapter 8, to consider whether any steps may be taken by regulators or practitioners to overcome the issues surrounding regulatory compliance (in terms of 'interpretation').

### 1.5.5 Chapter 8 Discussion – The compliance trust<sup>19</sup>

Within this chapter the analysis and findings are revisited with reference to each of the research objectives. The data collated from practicing compliance and risk managers is triangulated with the literature in order to develop a conceptual model.

The 'compliance trust' model is presented in order to contribute to existing academic literature and provide an alternative model to current practice. Following synthesis of this model, the principles of the Delphi method were adopted (see Section 8.3) whereby feedback was sought from both practitioners and academics on the theoretical rational, as opposed to the practical implications. A number of interesting feedback avenues are then developed further in order to strengthen this model. The resulting model may be presented in future research to assess the adequacy of the model for practical implementation within the financial service sector.

The proposed alternative model results in a compliance community which would operate independently from the financial service firms that they serve. This model differs from traditional commercial consultancy or outsourcing. Budgets would be controlled through a trust structure, following the principles of a cost controlled service centre serving all of its stakeholders, rather than a profit making entity. Decision making on operations and appointments would remain within the trust structure based on open communication and dialogue with a range of stakeholder including regulators and international industry leadership i.e. G30, and the multiple financial service firms that the trust would serve. This model will also differ from banking forum groups which

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<sup>19</sup> Note that the word trust is not used here in its traditional 'inter relationship' sense, but rather to describe the organisational structure of a trust, whereby the compliance officers within the trust will manage strategic and operations decisions based on the inputs of the major stakeholders.

are already in existence (such as the BBA) as the compliance officers community would be fully independent from the banking organisation that they would serve (and hence issues surrounding confidentiality/trust would exist within the resulting compliance community, rather than the individual banking organisations). The compliance trust would also benefit organisations they serve, via rotation of experience and knowledge sharing between organisations.

There is also a final discussion of the original contributions of this study, the implications on theory and practice, the limitations of this study and plans for future research in Section 8.5. The central argument of this thesis (that compliance officers often face barriers to compliance, and are often viewed as a business inhibiting function) is revisited. Further research is called for in this area (based on both continued gaps within the literature, and also to move the conceptual model presented in this study forward). A major conclusion of this study is that the academic/practitioner divide is perhaps inhibiting progress towards regulatory compliance. In order to address the ongoing issues facing the 'compliance professional' in financial service practice further study of the obstacles to compliance must be actioned.

## Chapter 2 Background to the regulatory framework in the UK banking sector

“We have a proportionate approach, prioritising our work on the areas and firms that pose a higher risk to our objectives.” FCA<sup>20</sup>

“The PRA does not seek to operate a “zero-failure” regime. Rather, it seeks to ensure that a financial firm which fails does so in a way that avoids significant disruption to the supply of critical financial services” PRA<sup>21</sup>

The purpose of this chapter is to provide an overview of the regulatory framework in which this study is positioned. Whilst the data collated within this study focuses on the perspectives of UK participants, there will be some inevitable overlap with the literature on European and Global regulatory compliance (due to the International nature of the banking industry in which the participants have worked over the course of their careers). The UK political background to regulation (from the 1980s) is presented in Section 2.1, followed by a discussion of the evolution of deregulation in Section 2.2, which leads into an examination of the current regulatory structure in Section 2.3. The linkage to theoretical underpinnings is then presented in Section 2.4. Finally in Section 2.5 this chapter is summarised, in anticipation of the following literature chapters.

### 2.1 Regulation approaches – the UK political background

The current regulatory structure of the UK financial services industry is underpinned by historic legislation. The legislation setting out the structure of the Bank of England and the Prudential Regulation Authority (PRA) includes<sup>22</sup>: the Bank of England Act 1694; the Bank Charter Act 1844; the Bank of England Act 1946; the Financial Service and Markets Act 2000; the Banking Act of 2009; and the Financial Service Act of 2010 and 2012 (Bank of England, 2015, p. 3). Following nationalisation in the 1946 Act, the Bank of England exercised supervisory powers in “informal ways” up to the implementation of the Banking Act 1979 (Daripa, Kapur and Wright, 2013, p. 3). Out of these supervisory powers, the role of compliance officers evolved, with the Bank of England able to “request information” and make “recommendations to bankers”, with legal powers to sanction banks (Daripa, Kapur, and Wright, 2013, p. 6).

<sup>20</sup> Extracted from FCA website <http://www.fca.org.uk/about/what/regulating>, Our approach to regulation (accessed July 2015).

<sup>21</sup> Extracted from PRA website <http://www.bankofengland.co.uk/pr/Pages/about/default.aspx> (accessed July 2015), which sets out the approach to regulation around three characteristics: Judgement based, Forward looking, and Focussed

<sup>22</sup> More detail (and listing of legislation) can be seen via <http://www.bankofengland.co.uk/about/documents/legislation/1998act.pdf> (accessed December 2015). All of the listed Acts can be accessed at <http://www.legislation.gov.uk> (accessed December 2015).

However, to provide some context to the regulatory literature, the political background for the UK and its impact on the current state of regulation should also be considered. In the mid-1980s, Britain was subject to waves of deregulatory initiatives under Thatcher's Conservative government (1979-1990), which were concerned with the cost of compliance and overregulation of firms (Hutter, 2005). Financial service firms were seen to operate under self-regulation within the scope of the Financial Services Act 1986 (Black, 2001). Deregulation in practice aligned to neo liberal ideals of "freer markets" under this historical political backdrop of "privatisation, deregulation and nurturing of markets" (Parker and Nielson, 2009, p. 47). However, not all commentators agree that this was indeed deregulation but rather a stepped adjustment from private regulation<sup>23</sup>. Nevertheless, there is acknowledgement of the significant changes to regulatory design during the Thatcher regime:

"Two trends define the Thatcher period. The first is the restriction or abolition of regulatory institutions that evolved within the market. This was not deregulation but the prohibition of market-led regulation. Secondly, there was a huge expansion of financial regulation to fields it had hardly touched." (Booth, 2015, p. 1)

The Banking Act of 1987 further enhanced the supervisory powers of the Bank of England (Daripa, Kapur, and Wright, 2013, p. 6). The huge expansion in regulatory scope impacted the role of compliance officers which is discussed further in Section 4.1 and 4.2.

In 1997, the Labour government (under both Blair and subsequently Brown) developed the Better Regulation Task Force (Better Regulation Task Force, 2003). This programme continued under the coalition government (2010-2015), and the coalitions' strategy was set out on the Department for Business, Innovations and Skills web page<sup>24</sup>, to:

- "Remove or simplify existing regulations that unnecessarily impede growth
- Reduce the overall volume of new regulation by introducing regulation only as a last resort
- Improve the quality of any remaining new regulation

<sup>23</sup> A recent publication (May 2015) from the Institute of Economic Affairs discusses this "myth" of deregulation. <http://www.iea.org.uk/publications/research/thatcher-the-myth-of-deregulation> accessed June 2015.

<sup>24</sup> Accessed in 2012 via <https://www.gov.uk/government/organisations/department-for-business-innovation-skills>, representing the 2010-2015 policies of the coalition government as per <https://www.gov.uk/government/publications/2010-to-2015-government-policy-business-regulation>

- Move to a less onerous and less bureaucratic enforcement regime where inspections are targeted and risk based.”

In 1997, the government also announced the decision to merge banking supervision and investment services regulation into the Financial Services Authority (FSA). The Financial Services and Market Act 2000<sup>25</sup>, was implemented in 2001 and transferred responsibility of several other organisations to the FSA:

- Building Societies Commission (BSC)
- Friendly Societies Commission (FSC)
- Investment Management Regulatory Organisation (IMRO)
- Personal Investment Authority (PIA)
- Register of Friendly Societies (RFS)
- Securities and Futures Authority (SFA)

This transfer of responsibility was also noted by Taylor (2005), marking the formation of the FSA as “an end to the alphabet soup” of regulatory bodies that had existed up to that point. The FSA were an independent body, who received no government funding – they were funded by the firms that they regulated. However, they were accountable to Treasury, and through them, Parliament. The statutory objectives, outlined by the Financial Services Market Act 2000, were set out on the FSA website<sup>26</sup>:

- “market confidence – maintaining confidence in the UK financial system;
- financial stability - contributing to the protection and enhancement of stability of the UK financial system
- consumer protection - securing the appropriate degree of protection for consumers; and
- the reduction of financial crime - reducing the extent to which it is possible for a regulated business to be used for a purpose connected with financial crime.”

The Better Regulation Executive issued a report in 2010, which set out a diagram of alternatives to command and control regulation, including self-regulation and co regulation, information and education, and economic instruments. These practical proposals can be linked to theories of responsive regulation (Ayres and Braithwaite,

<sup>25</sup> Available at <http://www.legislation.gov.uk/ukpga/2000/8> accessed December 2015.

<sup>26</sup> See <http://www.fsa.gov.uk/pages/about/aims/statutory/index.shtml>, accessed initially during 2012 at commencement of research, and still available at December 2015.

1992), which is discussed further in Section 3.3.1. There is specific reference to the Hampton Report (2006), which outlined the principles for a “risk based approach” to regulation. This provides examples of best practice from each of the regulatory bodies at that point in time (however, it should be noted that this was pre financial crisis).

Clark Jr. and Demirag (2006) reviewed deregulation through the lens of institutional theory, and discuss the causes of institutional pressures on regulatory bodies to deregulate, and then reregulation following financial scandal (using Enron and the Californian energy crisis as an example). Therefore, institutional theory is proposed as a suitable framework to explore questions of why regulatory bodies adopt certain procedures/policies/rules and systems due to external pressures and influences (see also Section 2.4). This is of particular relevance to this study in light of the global financial crisis, where there has been a similar scenario evidenced in the UK financial regulatory regime (see Section 2.3).

#### **2.1.1 Criticisms of deregulation, and calls for reform via a macro view**

These political publications indicate the on-going support for deregulation and the use of risk based approach by government over general regulatory structures. However, following the crisis there has been specific criticism of the regulation of the financial service sector by the FSA and the Bank of England. Buller and Lindstrom (2013) discuss the “market shaping coalition” of France and Germany (with key values of financial stability and consumer protection through prescriptive rule based regulatory style). This is contrasted (and with specific criticism) to the “market making” coalition in the UK which emphasised competition and market efficiency through light touch, principle based regulation (Buller and Lindstrom, 2013, p. 394).

The Turner Review (2009) indicated there was a need to move to a system wide macro prudential<sup>27</sup> perspective. In addition to make the regulatory structure effective the report proposed that the relationship between the regulator (which was then the FSA) and the Bank of England must work effectively, particularly in respect to the macro prudential analysis and use of macro prudential tools. The International Monetary Fund (IMF, 2010) discussed the apparent differences in supervisory response to the financial crisis, and called for change to allow both “the ability” (legal authority, adequate resources etc.) and “the will” (realistic objectives, independence, accountability etc.) for supervisors to act. Despite the efforts of the Financial Sector Assessment Program

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<sup>27</sup> A later report (Tucker 2013), argued that the “creation of a macro prudential authority at the Bank of England, the Financial Policy Committee (FPC) was an essential element of the reforms to UK financial regulation architecture. Macro prudential financial regulation within this thesis is defined as the approach to regulation with the objectives of mitigating and minimizing systemic risks to the sector as a whole.



(FSAP) involving peer review between countries against the global standards, failings were evident in the most recent financial crisis.

“while most countries have the necessary legislation, regulation and supervisory guidance appropriate to their national systems a significant proportion of those do not do as well when it comes to the nuts and bolts of supervision across the different sectors” (IMF, 2010, p. 9)

The scope of this study is restricted to the UK regulatory compliance perspective (due to geographic cost limitations of the chosen method of personal interview). However, due to the international nature of the banking industry, there is an expectation that there is overlap with the international regulatory issues discussed in Section 2.3.1, as the practitioners involved in data collation have extensive experience working across a range of (multinational) organisations in the sector.

## 2.2 The UK regulatory framework

Deregulation was a feature of the UK banking industry from the late 1980's up until the financial crisis in 2007/8 (Wilson, Casu, Girardone and Molyneux, 2010; Beck, Levine and Levkov, 2010). Since the most recent financial crisis there were calls for changes in regulation surrounding the financial services industry. In response to heavy criticism of the role of the FSA in the financial crisis, the Government reacted (under the Financial Services Act of 2012<sup>28</sup>) by setting up two separate regulatory bodies the Prudential Regulation Authority (PRA) and the Financial Conduct Authority (FCA).

The political stance is now clear on regulation of the complex financial service sector. However, questions remain as to whether these changes make the compliance officers and risk managers' jobs in financial service any easier or more effective. To understand compliance it is essential to underpin knowledge with the regulatory principles:

“It is very easy to become enmeshed in the mechanisms and processes of compliance without developing a grasp of the principles underlying regulation” (Jackman, 2004, p. 106)

As the split of regulatory body in the UK was only in its infancy at commencement of this study, this research could only look to historical approaches; or towards other industries to see if there are any alternatives which could be applied to financial service regulation. Engagement with compliance officers at this critical period of change is

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<sup>28</sup> See also <http://www.bankofengland.co.uk/pru/Pages/about/default.aspx> accessed November 2015.



important to understand the difficulties faced in operating in such a fast moving regulatory environment.

Since its inception, the FCA have been active and vocal within the media, issuing direct sanctions against instances of non-compliance and misconduct, with a specific focus on compliance culture (see Section 1.2.3). The financial regulator has issued discussion papers both pre and post crisis, in relation to culture (FSA, 2007, reissued 2013 by FCA; PRA, 2014). This demonstrates a policy of “visible deterrence”, which has traditionally been associated with the rule based/deterrence based systems adopted in the US (Gunningham and Kagan, 2005; Baldwin and Black, 2010). However, despite publically issued statements and documents such as these, the sector continues to be plagued by compliance violations. The continued concerns of the regulator regarding culture, and continued scandals in the sector are evidenced in the quote below, from Tracey McDermott (Director of Enforcement and Financial Crime, FCA):

“The misconduct in relation to LIBOR has cast a shadow over the financial service industry. The findings we publish today illustrate, once again, individuals within the industry acting with a cavalier disregard both for regulatory obligation and the interests of the markets. [Bank X]’s significant failings in culture and controls allowed that misconduct to flourish and fell far short of our expectations” (FCA, 2013, p. 1)

The exploratory nature of this research does not allow for generalisability of results so a full exploration of the culture issues within the industry has not been attempted within this thesis. However, it must be acknowledged that the principles of compliance culture (see also Section 1.2.3) is of interest to both academics and practitioners, who are studying regulatory compliance and, consequently, remains a theme of discussion throughout this thesis.

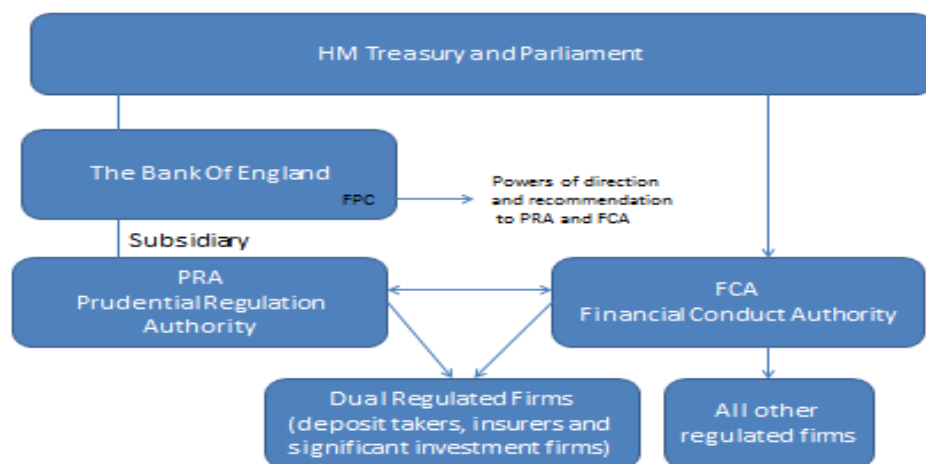
Within the academic literature the FSA has been categorised as a “principle based regulator” (Ford, 2008), or a “process orientated regulator” (Gilad, 2010). Ford (2008) likened the setup of the British Columbia Model to the FSA’s approach, and commented that proponents of the approach argue that the output is more effective and less costly regulation. Within the case study performed (Ford, 2008) it was found that in case of mandated review, those firms also had parallel internal supervisory systems on which they relied for internal review. It commented that “the need to

conduct the mandated reviews drained resources from the more effective internal system” (p. 11).

### 2.3 The current scenario – the split of the FSA

In June 2010 the government announced new regulatory arrangements in the future, as a result of concerns for consumers and as a result of the financial crises. This involved implementing a new model of financial regulation that would separate the prudential and conduct supervision of firms (Wheatley, 2012). The newly formed supervisory authorities Financial Conduct Authority (FCA) and the Prudential Regulation Authority (PRA) published separate handbooks during the course of 2013 (see Figure 4 for a summary of the new regulatory structure).

**Figure 4 The new “Regulatory Architecture” adapted from FSA report June 2011**



The PRA is responsible for supervision of insurance firms and deposit takers (as well as a small number of investment firms). This means that the PRA are responsible for the prudential supervision of over 2,000 firms (FSA, 2011a). The PRA released a document in conjunction with the Bank of England which described the new regulatory approach. One of the central messages was that the PRA would adopt a supervisory role which is “judgement based”, which would be “commensurate with level of risk”, “focused on big picture”, “will be forward looking”, and “will take supervisory action at early stage to reduce the probability of disorderly failure” (FSA, 2011a, p. 4). This change in approach was required as a result of “lessons from previous regulatory failure” (FSA, 2011a, p. 5). The report labelled the FSA’s supervisory approach prior to the 2007 Financial Crisis as inadequate, as the supervisory approach was designed

and built around the premise that regulators should only intervene following observable failings relative to a set of rules rather than seek to prevent potential failures in future (FSA, 2011a).

The FCA is responsible for regulating conduct in retail and wholesale markets, supervising the trading infrastructure that supports those markets and for the prudential regulation of firms not prudentially regulated by the PRA (FSA, 2011b). This means that the FCA regulate the conduct of around 27,000 firms which carry out a very wide range of business (retail and wholesale banking, investment, securities and insurance), and will also be responsible for the prudential supervision of around 24,500 of these firms (FSA, 2011b). The FCA approach was expected to differ to the FSA's approach, both analytically and culturally, in order for a sound economic understanding of the way relevant markets operate in order that regulatory interventions promote competition and effectively address problems identified. However, it was not expected that the FCA will have a statutory responsibility to be an economic regulator, such as Ofcom or other utility regulators (FSA, 2011b). The FCA is expected to intervene earlier and more strongly than in the past, further enhancing the credible deterrence agenda which the FSA had implement since the crisis (FSA, 2011b). The FSA's improved credible deterrence approach was evidenced within the June 2011 report, with statistics "that since 2007 the FSA had issued fines in excess of £150 million and prohibited over 200 individuals from the financial services industry" (FSA, 2011b, p. 26).

During a speech delivered in July 2012, the (then) CEO of the FCA reiterated the key messages as to the purpose and approach of the FCA:

- "The FCA's core purpose is to make sure markets work well so consumers get a fair deal – to do that we will have not only new powers, but a new supervisory approach and a new culture.
- Key to the success of this approach is ensuring that good consumer outcomes are built into the business model of the firms we regulate.
- While much of what we do is changing out enforcement approach and credible deterrence agenda is here to stay." (Wheatley, 2012, Closing Remarks)

KPMG (2012) summarise the main changes, and considers the opportunities of "more proactive regulation to prevent issues". The split into the PRA and FCA ultimately allows for an improved understanding of the risks to the stability of the financial system as a whole (by the PRA), whilst also focussing separately on product lifecycles, and

investing time on robust approval processes and monitoring (via the FCA). In terms of compliance officers role this will then focus the concept of “documented risk based decision making” in line with the PRA’s risk assessment framework (KPMG, 2012, pp. 6). In addition, compliance officers will conduct “Business Model and Strategy Analysis” (BMSA) to evidence analysis of conduct risk management for the FCA (KPMG, 2012, p. 9).

Ryder (2013) questioned the lack of accountability for the “immoral and unethical conduct” of bankers, and welcomed the reforms of the Financial Services (Banking Reform) Bill 2013-14. The regulators have since jointly issued the “Senior Managers’ Regime” (Ernst and Young, 2014), which promotes accountability of senior management (at the top of organisation) for regulatory compliance (replacing the Approved Persons Regime). This requires for the firms to have ‘Responsibility Maps’ allocating governance and management responsibility. In addition any employee within organisations with responsibilities relating to regulated activities, must also engage in the ‘Certification Regime’. The purpose of these requirements is to impact on culture (Ernst and Young, 2014).

The FCA set out the principles for good regulation, and also their expectation of principles within the organisations, including: integrity; skills, care and diligence; management and control; financial prudence; appropriate standards of market conduct; due regard for customer interests; management of conflicts of interest; relationship of trust with customers; protection of client assets; and, and open and cooperative relationship with regulators<sup>29</sup>. Haynes (2014) contends that despite the changes to the regulator and the “changing set of rule books” that desired changes may not be realised if the regulator continue to have “little appetite” to ensure responsibility within the banks. The impact of these recent publications from the regulator, in relation to accountability is considered further in comparison to the findings of this study in Section 8.3.4.

### **2.3.1 Recent changes to legislation impacting on compliance officers**

It should also be noted at this point that the UK is not alone in changes to the regulatory structure and legislation following the 2007-2009 crisis.

The US Dodd Frank Act (Dodd-Frank Wall Street Reform and Consumer Protection Act 2010) has been referenced by a number of scholars in their discussion on regulation

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<sup>29</sup> For expanded definition see FCA webpage, <http://www.fca.org.uk/about/operate/principles>, accessed December 2015.

approaches (Ford, 2011; Levine 2012; Omarova; 2012; Coates and John, 2014). The Act was signed into Federal Law in 2010 by President Obama. The impact of this act is the implementation of over 200 rules and, update of many existing rules (Coates and John, 2014) Although this is relevant for overall understanding of the evolution of regulation, this is seen to be outside the scope of this research topic as US based, and so will not be included in the full literary review. Haynes (2015, p. 125) discusses the difference between the “old US Glass Stegall Act” and Dodd Frank, and the differences in proposals in new UK legislation (Financial Service Banking Reform Act 2013). This highlights the difficulties and complexities faced by multinational dealing with cross jurisdiction legislation (and compliance thereon).

Arora (2010) examined the roles and work of some of the existing international regulatory bodies post crisis including: (the International Monetary Fund (IMF), the Financial Sector Assessment Program (FSAP); the role of the Bank of International Settlement (BIS), the work of forums such as the Committee on the Global Financial System (CGFS), the BASEL Committee; and the Financial Action Task Force (FATF), the Financial Stability Board (FSB) promoting information exchange and international cooperation in supervision, and finally the International Organisation of Securities Commission (IOSCO)). Within this scenario of “multiple standard setting agencies”, the author concludes an overall inefficiency and unwarranted complexity of the system (Arora, 2010), with much work to be done to form a more coherent system. A further review of the proposed European framework (including the findings of the Larosiere report regarding the macro prudential oversight of the European Systemic Risk Board (ESRB) and micro prudential supervision via the independent, supranational European Supervisory Authorities (ESAs)), concluded that the global financial markets cannot continue under the current scenario of “partial regulation” (Arora, 2010), with continued reform essential.

BASEL III is currently under development with phasing in of changes to capital requirements between 2013 and 2019, and new regulatory requirements relating to bank leverage and liquidity will be phased in during 2011-2018. Again this will be an area of interest for scholarly review, but will not be included in the scope of this research topic.

The European Commission have also set up the new European System of Financial Supervisors (ESFS) following the financial crisis, in attempt to restructure the system of financial sector oversight. The changes to the supervisory structure are in their infancy

(operating from 2011 onwards), which is similar to the changes in the FSA, and so there has been limited academic focus to this new architecture to date.

The discussion above represents only a summary of issues around regulatory amendment within the sector, however, these provide some context to the major change facing compliance professionals at the current time. Data on cost of compliance has been presented by Thomson Reuters annually, which represents the views (through survey research) of 500+ global compliance professionals (English and Hammond, 2012; English and Hammond, 2015).

In the most recent survey (2015) the main findings included the “regulatory fatigue” of compliance professionals with over "seventy per cent of firms" expecting increasing levels of regulatory publications within the next year (English and Hammond, 2015). One specific question asked in the surveys is to identify those areas which “pose the greatest challenges in coming year”, and this has been presented in both the 2012 and 2015 reports (English and Hammond, 2012, p. 6; English and Hammond, 2015, p. 17). As this is a global survey the issues identified by compliance professionals include international pieces of regulations, and these are summarised in Table 3.

One area to note from this summary table is that certain pieces of legislation remain the focus of compliance officer's attention despite the 3 year gap within the surveys (for example FATCA, Solvency II, BASEL III, MIFID to highlight a few, which are discussed in further detail in Table 4), which reflects the lifespan of implementation of new pieces of legislation. Although the results from these surveys represents a global view (and, thus, international pieces of legislation), it is clear that the list of concerns of compliance officers around regulations has increased (with new pieces of legislation adding to the existing concerns of compliance officers).

**Table 3 Summary of compliance officers' regulatory concerns in 2012, and 2015 respectively (sourced from English and Hammond, 2012/2015)**

| 2012 Survey – List of regulations posing greatest challenge (English and Hammond, 2012, p. 6)   | 2015 Survey – List of regulations posing greatest challenge (English and Hammond, 2015, p. 17)   |
|---|--|
| <ul style="list-style-type: none"> <li>• Foreign Account Tax Compliance Act</li> <li>• Markets in Financial Instruments Regulation and Directive II</li> <li>• Anti-money laundering</li> <li>• UK Retail Distribution Review</li> <li>• Dodd-Frank Wall Street Reform and Consumer Protection Act</li> <li>• Basel III</li> <li>• Sanctions</li> <li>• Solvency II</li> <li>• Data protection</li> <li>• Undertakings for Collective Investments in Transferable Securities IV Directive</li> <li>• European Market Infrastructure Regulation</li> <li>• Remuneration</li> <li>• Conflicts of interest</li> <li>• Suitability</li> <li>• Alternative Investment Fund Managers Directive</li> <li>• Bribery and corruption</li> </ul> | <ul style="list-style-type: none"> <li>Alternative Investment Fund Managers Directive (AIFMD), Europe</li> <li>• Basel III, international</li> <li>• Capital Requirements Directive IV (CRD IV), Europe</li> <li>• Data Protection Directive, Europe</li> <li>• Directive on Undertakings for Collective Investment in Transferable Securities (UCITS V), Europe</li> <li>• Dodd-Frank, United States</li> <li>• European Market Infrastructure Regulation (EMIR), Europe</li> <li>• Financial transaction tax (FTT), Europe</li> <li>• Foreign Account Tax Compliance Act (FATCA), United States</li> <li>• Foreign Corrupt Practices Act, United States</li> <li>• Fourth Money Laundering Directive, Europe</li> <li>• Future of Financial Advice (FoFA), Australia</li> <li>• Health Insurance Portability and Accountability Act, United States</li> <li>• Market Abuse Directive (MAD 2), Europe</li> <li>• Markets in Financial Instruments Directive II and Markets in Financial Instruments Regulation (MiFID 2/R), Europe</li> <li>• Payment Services Directive II (PSD2), Europe</li> <li>• Sarbanes-Oxley Act, United States</li> <li>• Senior Managers Regime, UK</li> <li>• Solvency II, Europe</li> <li>• TILA-RESPA Integrated Disclosure rule implementation, CFPB, United States</li> <li>• Volcker Rule, United States</li> </ul> |

In order to set context for this study (which explores the viewpoints of UK based compliance officers), Table 4 represents some of the major pieces of legislation/regulation impacting the UK sector at this time. It should be noted that this list is far from exhaustive, but represents the diversity of regulations that compliance officers face in everyday practice.

Certain pieces of legislation will only apply to more complex organisations, being dependent on specific type of banking institution. It should also be considered that the roles of compliance officers vary across organisations. In some organisations there will



be compliance officers devoted to specific pieces of legislation (for example, specific roles focussed on areas such as anti-money laundering). However, in other organisations, the compliance officer's role may require engagement with numerous pieces of legislation. However, irrespective of the organisational structure, there is an expectation from the regulator that the compliance personnel within the financial service organisations are competent and able to navigate, and interpret, the provided regulatory guidelines, whilst also being "on the alert at all times" (Gelemerova, 2009, p. 40).

A conscious decision was made early within the research process, that no specific piece of legislation<sup>30</sup> would be explored during the literature review, or later during data collection with participants. The reasons behind this were that a focus on one piece of regulation would not reflect the practical realities of most individual participant's work environment (as compliance is a wide ranging role within a organisation covering a broad range of country, region and international regulation in practice<sup>31</sup>, which is discussed further in Sections 4.1 and 4.2). Instead the focus is on the experiences of compliance officers when facing their roles within the organisations they serve.

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<sup>30</sup> An initial interest in FATCA (Foreign Account Tax Compliance Act) promoted the early direction of the literature search, and considerations of 'how' to comply. This was then reconsidered in light of the extensive range of new country specific and international regulation facing the sector (on further review of the literature).

<sup>31</sup> Another example of cross border legislation would be that of Suspicious Activity Reporting, which would form one of the duties of compliance within an organisation.



**Table 4 Summary of some significant pieces of legislation/directives impacting UK financial services**

| Legislation   | Requirements/Compliance impact  | Overall summary of changes  |
|---|---|---|
| Financial Services Banking Reform Act 2013 <sup>32</sup>        | Meaning of “compliance failure” defined in Section 71, with directions to comply in Section 54, and requirements in Section 55 and 56.  | Including ring fencing, and the framework for communication between the Bank of England, the PRA, and the FCA in relation to payment systems (Edmonds, 2013; Haynes 2015).  |
| The Money Laundering (Amendment) Regulations 2012 <sup>33</sup> | No specific reference to compliance in amendments. Money Laundering Regulations 2007 <sup>34</sup> set out requirements within Part 4, and enforcement activities in Part 5. With specific reference to compliance duties for due diligence (Section 13.2.b.ii), and policies and procedures (Section 20.1.f).                    | Amendments to Money Laundering regulation (alongside updates in 2015 ongoing to the original 2007 regulations). Ryder (2008) discussed the risk based approach adopted by the FSA, which has continued under the FCA <sup>35</sup> (primarily through internal monitoring policies and procedures, and submissions of suspicious activity reports). |
| Financial Services Act 2012 <sup>36</sup>                       | Directions of Financial Policy Committee set out in Section 9H, and compliance thereon set out in Section 9I. Rule-making powers set out within Section 24.   | Including the changes to regulatory body (Murphy and Senior, 2013).   |
| Capital Requirement Directive IV <sup>37</sup>                  | This falls under the scope of BASEL III <sup>38</sup> , with minimum capital requirements including quality and level of common equity, a capital conservation buffer (common equity of 2.5% of risk weighted assets, and total common equity standard of 7%), and a countercyclical buffer ranging from 0-2.5% of common equity. | Representing implementation of capital requirements of BASEL III. BASEL III is not legislation but rather a set of standards developed by supervisors/central banks, which is transposed within EU law.   |
| Solvency II <sup>39</sup>                                       | Falls under scope of the Financial Services and Markets (The Solvency 2) Regulations 2015 <sup>40</sup> .   | Impacting UK Insurance Industry, and aligned to the three pillars of BASEL III, to develop consumer solvency protection with  |

<sup>32</sup> See <http://www.legislation.gov.uk/ukpga/2013/33/contents> accessed October 2015.

<sup>33</sup> See <http://www.legislation.gov.uk/uksi/2012/2298/contents/made> accessed October 2015.

<sup>34</sup> See [http://www.legislation.gov.uk/uksi/2007/2157/pdfs/uksi\\_20072157\\_en.pdf](http://www.legislation.gov.uk/uksi/2007/2157/pdfs/uksi_20072157_en.pdf) accessed November 2015

<sup>35</sup> See <http://www.fca.org.uk/about/what/enforcing/money-laundering/approach> accessed November 2015.

<sup>36</sup> See <http://www.legislation.gov.uk/ukpga/2012/21/contents/enacted> accessed October 2015.

<sup>37</sup> See <http://www.bankofengland.co.uk/pr/Pages/crdiv/default.aspx> accessed October 2015.

<sup>38</sup> See summary at <http://www.bis.org/bcbs/basel3/b3summarytable.pdf> access November 2015

<sup>39</sup> See <http://www.bankofengland.co.uk/pr/Pages/solvency2/default.aspx> accessed October 2015.

| Legislation   | Requirements/Compliance impact   | Overall summary of changes   |
|---|--|--|
| FATCA <sup>41</sup>   | Foreign financial institutions (FFIs) to provide annual reports to IRS on US clients. Non-compliance results in 30% withholding tax on all US sourced payments i.e. dividends/interest (Brodzka, 2013). An intergovernmental approach is now to be adopted.  | minimum capital requirements, and solvency capital requirements (Doff, 2008; Eling, Schmeiser and Schmit, 2007). Enacted as part of the US Hiring Incentives to Restore Employment (HIRE) Act 2010, in order to target those evading US taxes (Brodzka, 2013). This is discussed in further detail in Section 5.1. |
| Markets in Financial Instruments Directive II <sup>42</sup> | A consultation on the transposition of the MiFID II is underway <sup>43</sup> . Transposed in FSMA 2000 in “Part 4 (now Part 4A) authorisation for investment firms, Part 18 recognition for regulated markets and Schedule 3 for EU passporting of investment services and activities” (HM Treasury, 2015, p. 3). | Aim is to strengthen investor protection framework, and increase competition.  |
| Central Security Deposits Regulation <sup>44</sup> (CSDR)   | EU legislation <sup>45</sup> , which is under consultation.  | Involving mandatory securities settlement discipline, including mandatory buying-in and mandatory cash penalties for failed settlements.   |

<sup>40</sup> See [http://www.legislation.gov.uk/ukxi/2015/575/pdfs/ukxi\\_20150575\\_en.pdf](http://www.legislation.gov.uk/ukxi/2015/575/pdfs/ukxi_20150575_en.pdf) accessed November 2015.

<sup>41</sup> See <http://www.fca.org.uk/firms/being-regulated/meeting-your-obligations/firm-guides/systems/fatca> accessed October 2015.

<sup>42</sup> See <http://www.fca.org.uk/firms/markets/international-markets/mifid-ii> accessed October 2015.

<sup>43</sup> See <https://www.gov.uk/government/consultations/transposition-of-the-markets-in-financial-instruments-directive-ii> accessed November 2015.

<sup>44</sup> See <http://www.fca.org.uk/firms/being-regulated/meeting-your-obligations/firm-guides/csd> accessed October 2015.

<sup>45</sup> See <http://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32014R0909&from=EN> accessed November 2015.

## 2.4 Underpinning theories – why comply?

There are fundamental questions over why management comply with regulation (May, 2004), when the costs of compliance are seen to be so high (see Section 3.5). The theories and empirical studies reviewing this area of the literature are discussed in Section 4.4.

### 2.4.1 Institutional considerations – the banks

As discussed in the Introduction (Chapter 1), the literature review has been performed under the lens of institutional theory. Under this premise, organisations find social reward in legitimacy, resources, and survival, subject to acceptance of coercive, normative, and mimetic institutional pressures (DiMaggio and Powell, 1983). Under institutional theory, rational firms may be seen to act in a similar manner to other firms under the three isomorphic processes - coercive (formal and informal pressures exerted by other organisations), mimetic (firms modelling themselves on other organisations) and normative (resulting primarily from professionalisation). Putting this into the context of compliance in the banking sector:

“Organizations are prone to yielding to coercive and normative pressures arising from their institutional context (for example banks adhering to capital base requirements or to a corporate governance code) as these are likely to confer social privileges from their stakeholders” (Fashola, 2014, p. 2)

Interligi (2010) proposed a conceptual framework which links (Neo) institutional theory (DiMaggio and Powell, 1983) and the competing value model (Quinn and Rohrbaugh, 1983), which is used as a model for measuring culture. The framework introduces core dimensions of legitimacy (organisations response to stakeholder expectations), permeability (openness to stakeholder influences) and control style (the way in which stakeholders expectations are implemented) (Interligi, 2010, p. 243). The justification for this model was to combine the strengths of institutional theory and competing value model to explain “culture, organisational performance and regulatory compliance” (Interligi, 2010, p. 246) to inform “policy makers, regulators and compliance practitioners” on how cultural change can impact compliance performance. These concepts can be linked to the evolution of the compliance function that has been discussed during the literature review (see Section 4.1 and 4.2). Compliance is now viewed in practice as a “core function within organisations” (Perezts and Picard, 2014), hence, the association with institutional theory for the purpose of the literature review.

#### 2.4.2 Personal ethics – the compliance officers

However, the literature may also be linked to the theory of moral reasoning, as regulation and compliance is “actually performed by *someone*” (Perezts and Picard, 2014). Moral reasoning relates to the process in which an individual applies moral principles to determine a course of action (Myry, Siponen, Pahnla, Vartiainen and Vance, 2009). Kohlberg’s model, based on three broad levels of moral development (Pre conventional, Conventional, and Post Conventional), was first developed in a non-business environment (research was developed in a study of young American males). Many academics have developed the theory further and applied this across a range of business disciplines. The literature related to this theory is discussed further in Section 4.4.2.1.

Whilst exploring the issue of the global financial crisis, other studies have considered wider ethical theories such as virtue theory (Graafland and Ven, 2011; Racelis, 2014). These studies extend beyond personal (morality) perspectives and regard banking as a collective, with virtues communicated and evidenced within “codes of conduct” (Graafland and Ven, 2011). Others have argued evidence of personal ethics through signing of “oaths” may also “enhance” compliance (de Bruin, 2014). However, there is limited empirical research as yet relating to oaths, so the impact of these mechanisms (as opposed to codes of conducts) is viewed as uncertain (de Bruin, 2014).

Overall, the focus of these ethics studies indicate that there is a public expectation for further “professionalization of those who work in the financial sector” (Graafland and Ven, 2011), with clear evidence<sup>46</sup> of ethical banking required to restore public trust. Consequently, this provides the overlap between ethical theories which are studied in the literature review, with the wider exploration of institutional theory, as it is argued that the “conduct of the individual is strongly influenced by their immediate environment” (Graafland and Ven, 2011, p. 606).

Posner (2009, p. 284) argued that “capitalism is Darwinian”, and stated that it would be “as unfair” to blame<sup>47</sup> financiers for their actions in the build-up and during the crisis, as to blame lions for eating zebras (indicating a complete disregard for personal ethics). This also disregards the issue of accountability within the sector (which was discussed in relation to UK Banking Reform Bill in Section 2.3, and also revisited in Section 8.3.4).

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<sup>46</sup> Through oaths (de Bruin, 2014), ethical code adherence and competence testing (Graafland and Ven, 2011), a reassessment of virtues of the profession (Racelis, 2014)

<sup>47</sup> Although Posner (2009) does acknowledge that financiers had “primary responsibility” for the crisis, they could not be blamed.

This underpins the importance of encompassing ethical theories within this thesis through the review of the literature, and the resulting analysis of data.

### **2.4.3 Stakeholder considerations – the regulator and wider society**

When discussing the motivations for compliance, the relationship with stakeholders may also be considered. Freeman's 1984 work is most often used to define stakeholders within the literature (Mitchell et al., 1997; Cuganesan and Khan, 2008). However, it is acknowledged that managers will have varying levels of consideration for different stakeholder group, across different industry groups, and jurisdictions. Mitchell et al. (1997) developed the stakeholder salience model to theorise this phenomenon. In this model stakeholders may be positioned by organisations, in accordance with factors of power, legitimacy and urgency, which are described as:

“(1) the stakeholder's power to influence the firm, (2) the legitimacy of the stakeholder's relationship with the firm, and (3) the urgency of the stakeholder's claim on the firm” (p. 854)

The reason behind theorising the model was a criticism of existing stakeholder literature and theories, where the authors contended:

“Among the various ways of identifying stakeholders, as well as in the agency, behavioural, ecological, institutional, resource dependence, and transaction cost theories of the firm, we have found no single attribute within a given theory that can guide us reliably on these issues” (Mitchell et al., 1997 p. 854)

This same criticism may apply within this study of compliance in the financial service sector, in that grand theories are too abstract to reliably guide us on models for compliance (which will be developed further in Chapters 8).

Cuganesan and Khan (2008) consider the stakeholder salience model in a review of the banking industry in Australia. They also consider Clarkson's 1995 (pp. 106-7) discussion of primary and secondary stakeholders, where primary stakeholders' participation is considered essential to maintain the organisation as a going concern, and the secondary group wield considerable influence, whilst not being directly engaged in the transactions of the firm (Cuganesan and Khan, p. 87). They contribute to the literature by performing content analysis on Australian banking organisations annual reports, and websites. The study specifically discusses the relationship with the regulator, whereby the findings of the study indicated and 11% contribution of “total

non-financial KPIs reported”. From these findings the authors concluded that there was:

“...a strong focus on regulatory compliance and cost efficiency. Concurrently, the absence of reporting of the contribution of regulators to organisational wants and needs limits the reporting to this stakeholder group” (p. 97)

So although the regulators are considered to be an important stakeholder they are not acknowledged to have primacy (in terms of disclosures provided by banking organisations), where customers and shareholders were considered to hold most importance. Cuganesan and Khan’s 2008 study was not focused specifically on the compliance function itself. However, this does provide some context to this thesis when considering motivations of compliance officers towards stakeholders. In addition, the authors themselves acknowledged limitations in the study, contending that further research was required to assess the differences in “stakeholder measurement and management practice” across the industry, to include “community banking organisations” (p. 98).

Other authors review the issue of primacy from other angles. Although not explicitly focused on the role of the compliance officer, Fashola (2014) offers a conceptual framework in the form of the “customer legitimacy model”, in response to discussion on “strategic choice, institutional theory and legitimacy” when considering the banking sector. In this model they contend that primacy should be given to the customer in the relationship between the regulator and the banks (which although not explicitly stated in the article, may be seen as the compliance officer in practice due to their intermediary role between the regulators and the banks).

Using these theories (i.e. institutional theory, Kohlberg’s moral reasoning (with overlap to wider ethics literature base), and stakeholder salience), the focus during the literature review has been that of relational issues between the role of the regulators and the role of the compliance officers. This study explores experiences of compliance personnel whilst facing new regulation, hence the overlap between the different theories covering personal ethics (the compliance officers), institutional impact (the banks), and stakeholder relations (the regulator, and wider society). Institutional theory may be used to frame decision making within the banking organisations; Kohlberg’s moral reasoning to frame the personal motivations (of the individual compliance officers); and finally, stakeholder salience to consider the relational issues between the regulator and the individual firms.

## 2.5 Chapter summary

The purpose of this short chapter was to provide background to the UK regulatory environment in which this study has been undertaken. In addition, underpinning theories around motivations for compliance have been discussed, in order to set the scene for the following literature review. In the following chapters, the regulatory compliance literature is presented, which has been written across a range of disciplines and geographic perspectives.

As discussed in Section 2.3.1, this thesis has not focused on any single piece of legislation. Instead, there has been an exploration of the issues faced by practicing compliance officers in their everyday roles within the financial service industry, whereby the compliance officer's role within the organization may cover a diverse, and ever changing regulatory environment.

Therefore, this sets up the framework for the literature review, where a number of theoretical and practical perspectives are considered in Chapters 3 through to 5. The literature in the area of regulation and compliance is wide and involves cross over between disciplines of political economists, legal scholars, finance theorists and social scientists. Therefore, the focus of the literature review has been to broadly consider models of compliance, whilst addressing a more specific question of: What are firms complying with and why do firms comply? Coupled with this overriding question, is the exploration of whether there are credible alternatives to the current broadly accepted best practice models. This follows on from the context that has been set out within this chapter, which has discussed the historical and current UK regulatory environment. This literature will then be contrasted to the findings of this UK study in Chapter 8. A summary of legislation impacting compliance officer (from both an International and UK perspective) is provided in Section 2.3.



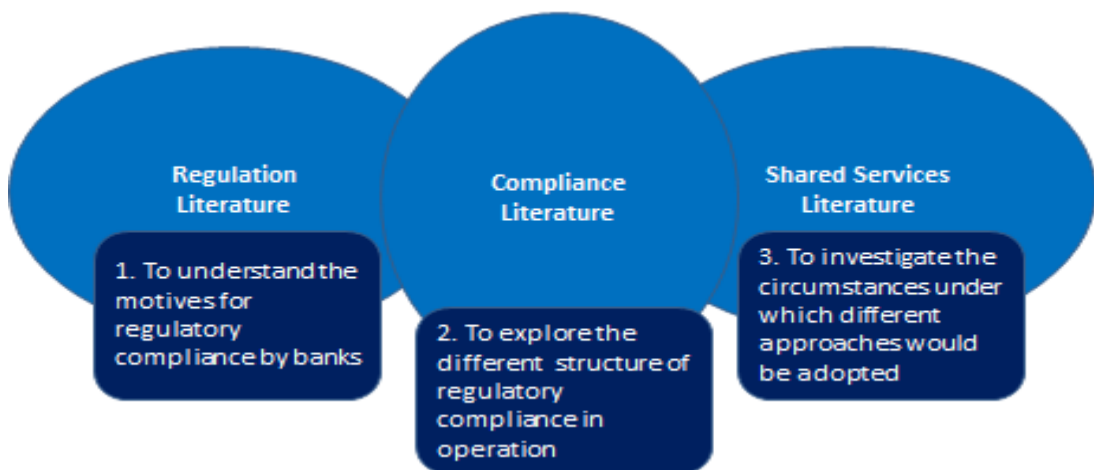
## Chapter 3 Literature review – Regulation: What are we complying with?

“More than a sword is needed to achieve the objectives of the ruling classes of regulatory capitalism. Both the regulators and the regulatees who command the economy need civility that is not dependent on iterated encounters, yet that is secured by smoke curling from a benign gun.” Braithwaite and Hong (2015)

### 3.0 Introduction

As will be seen in the following chapters the literature has been reviewed in three broad areas of regulation, compliance and shared service/outsourcing. In Figure 5 the overlap between the literature domains is summarised and the positioning of the research objectives are proposed.

Figure 5 Summary of literature review topics with links to research objectives



### 3.1 Literature review framework

As illustrated in Figure 5, the academic literature reviewed during the course of the research project can be categorised into topic areas of regulation (with what do officers comply); compliance (models and motivations); and shared services. Norman (2011, p. 44) commented that “it may be helpful to look at the realm of beyond compliance obligations through the lens of regulation or self-regulation”, and this supported the initial direction of the literature review.

Therefore, this review has taken distinct lines which feed into the overall knowledge of models of compliance:

- Chapter 3: Regulation literature – including a review of regulatory theory literature, academic literature pre and post crisis, and literature reviewing costs of regulation and compliance therewith;



- Chapter 4: Compliance literature – including a review of the history or compliance, a review of qualified officers and responsibilities of compliance officers, and compliance models and approaches, including compliance tooling; and in the final section ‘Why management comply’ which explores the literature reviewing the motivation of managers towards compliance;
- Chapter 5: Exploring Alternatives - The first two section reviews the limited literature which is available regarding the relationship of the compliance function with consultants, and how the compliance function deals with new mandatory items of regulation; and the remaining sections review the concepts of outsourcing, looking at the literature relating to shared services and outsourcing, which may be considered an alternative to in house compliance.

Further background on aspects of the UK regulatory environment, and underpinning theories on motivations for compliance, was included in the previous chapter.

### 3.2 A history of regulation

Under a capitalist system, the banking sector is subject to inherent financial instability with “financial crises” plaguing “our history” (Minsky, 1976, p. 1). Regulation is necessary to “establish reasonable constraints” over the banking industry (Minsky, 1976, p. 11). There is a wealth of literature available relating to regulation. A smaller proportion of the literature is directed specifically to banking or financial service regulation<sup>48</sup>, which provides an indication of the broad discussion and application of regulatory theories by academics. Figure 6 was developed by the author during the literature review to summarise the theories and models feeding into regulation literature, and this mind map forms the outline for the content of the literature review of regulation. There are three main sections to the mind map which summarises the concepts discussed in the following literature review: the underpinning theory, pre and post crisis critique of regulatory models, and finally an overriding concern of cost benefit analysis.

Underpinning regulatory theory is discussed in Section 3.3. Since the most recent financial crisis there is a renewed interest in the area of regulation amongst academics. Some key literature has been categorised as pre/post crisis within Section 3.4 with a review of new academic models, updated theory and critical review of the regulatory structure post crisis. An area of continued focus by academics (and indeed

<sup>48</sup> A Google Scholar search on “regulation” indicated approximately 1.8 million results. When this was specified to “banking regulation” this decreased to approximately 28,000 results, and if the search term “financial service regulation” was used this reduced down to 186 results (as at June 2015).

practitioners) is that of cost benefit analysis, and the literature reviewed in this area is discussed in Section 3.5.

**Figure 6 Author developed mind map of regulatory literature**

| Underpinning Theories and Models   | Post Crisis Critique   |
|--|--|
| <b>Microeconomic Theory</b> <ul style="list-style-type: none"> <li>- public choice</li> <li>- Regulatory capture (Stigler, Baker, Omarova)</li> <li>- Agency theory (Ross, Fullenkamp &amp; Sharma, Alexander)</li> <li>- Rent Seeking (Krueger, Krawiec)</li> </ul>   | <b>New Academic Models</b> <ul style="list-style-type: none"> <li>- Regulatory Academy (Fullenkamp and Sharma)</li> <li>- Complement vs. substitution theory (Becher and Fyre)</li> <li>- updated PIG model (Omarova)</li> <li>- 'Sentinel' (Levine)</li> <li>- Regulatory Ambassadors (Braithwaite and Hong)</li> </ul>   |
| <b>Macroeconomic Theory</b> <ul style="list-style-type: none"> <li>- avoid market failure (Keynes)</li> <li>- macroprudential policy (Galati &amp; Moessner)</li> </ul>  | <b>Updated Theory</b> <ul style="list-style-type: none"> <li>- Updated responsive regulation (Braithwaite)</li> <li>- 'embedded' self-regulation (Omarova)</li> <li>- Meta regulation (Gilad)</li> <li>- Technological (Ford) vs. Relational (Braithwaite)</li> </ul>  |
| <b>Models</b> <ul style="list-style-type: none"> <li>- Responsive regulation (Ayres and Braithwaite)</li> <li>- enforcement pyramid, tripartism and PIGs</li> <li>- Command and control regulation</li> <li>- Outcome orientated regulation</li> <li>- Process orientated regulation (Stefanadis – self regulation, Coglianese and Lazer – management based)</li> <li>- Open Corporation (Parker)</li> </ul> | <b>Critical Academic Review</b> <ul style="list-style-type: none"> <li>- Crotty (NFA and VAR)</li> <li>- Jameson (VAR)</li> <li>- Wilson (lit. review)</li> <li>- Ford (lit. review)</li> <li>- Bartle (RIA)               <ul style="list-style-type: none"> <li>- Baker and Young (Regulatory Capture)</li> <li>- Trust and Ethics (Davies, Llewellyn et al.)</li> </ul> </li> </ul> |
| <b>Cost Benefit Analysis</b><br>(Included for context in literature review, however not forming part of research questions)  |  |

### 3.3 Regulatory theory

The rationale for regulation under economic theory is the desire to avoid monopoly inefficiencies (Baldwin and Cave, 1999). However, from a societal (public) viewpoint the objective of regulation is to protect the consumer from monopoly exploitation (Crew and Kleindorfer, 2002).

Some significant economic literature was developed by academics during the 1970s (regulatory capture theory, Stigler, 1971, Posner, 1974; agency theory, Ross, 1973; rent seeking behaviour, Krueger, 1974) which has shaped today's regulatory

landscapes. Microeconomic theory developed from the end of 1970s is thought to have supported deregulation during the latter part of the 20<sup>th</sup> Century (Crew and Kleindorfer, 2002; Winston, 1993). Posner (1974) argued that there were two broad streams to the economic regulation literature at the time: the first “public interest” theory, and the second stream exploring “capture” theory.

Public interest theory encompasses “what motivates policy makers”, and in contrast capture theory discusses regulatory actors with “narrow, self-interested goals” (Levine and Forrence, 1990, pp. 168-169). Under public interest theory (Keynesian macroeconomic theory) regulators were required to correct for market failure, however, from 1960s onwards public interest theory was subject to increasing criticism, as the regulation had not brought about the “desired” stability (Crew and Parker, 2006). Academics sought explanations and reasons for regulatory failure, and so public choice and the theory of regulation was developed further.

Regulatory capture theory was developed by George Stigler (1971), and this mechanism has been cited by some authors as one of the main causal factors of the most recent financial crisis of 2007-2009 (Baker, 2010; Omarova, 2012). However, due to the complexity of the financial sector there is a strong reliance by the supervisors and regulators on the industry itself, due to the industry’s superior technical expertise and resources, so regulatory capture is considered an on-going issue.

Other authors have considered the self-regulatory mechanisms within the markets. Mayer (2008) discusses the evolution of financial markets in “an absence of formal systems of regulation” where reliance was placed on “informal relations of trust”:

“There comes a point at which trust mechanisms appear to break down and more formal investor protection is required. Is regulation then inevitable?”  
(Mayer 2008, p. 631)

This point supports earlier discussion of “regulatory creep”, whereby there is a “trade-off between trust and confidence on one hand, and regulation on the other” (Llewellyn, 2005). This concept of trust and self-regulation, contrasted with formal regulation can be linked back to the theories around agency. Ross developed the economic theory of agency (1973) which has been extended further by numerous authors under the heading of principal agent theory. Fullenkamp and Sharma (2012) refer to this “current” issue whereby “regulators are sandwiched between politicians to whom they are agents responsible for rulemaking and law, and the financial sector, to which they are principals in charge of regulation and supervision” (p. 4).

The investment of resources in attempts to divert income from other people through the political and regulatory process was termed “rent seeking” by Krueger in 1974 (Crew and Parker, 2006). Krawiec (2005) suggested that rent seeking behaviour of powerful interest groups, may have influenced the development of the US legal system towards a compliance based regime. She suggested that legal compliance professionals such as lawyers, compliance and ethics consultants, and in-house compliance, all have a stake in, and benefit from, internal compliance based liability regimes. Krawiec went on to suggest that there is also an over reliance on agency cost explanations for organisational misconduct by legal academics and legal decision makers.

Much of the regulatory compliance literature also broadly refers to the concept of culture. However, Meidinger (1987) criticises this phenomenon whereby:

“One important reason for the rise in discussions of regulatory culture seems to be the inability of scholars to comprehend large parts of regulatory activity without reference to such a construct” (p. 356)

The concept of the “regulatory community” is introduced, and linked to the concept of culture. It is argued that in order to action change, the “developed culture of regulation” requires adjustment (p. 372). This has relevance to the context of this study, in that alongside the regulatory communities, compliance communities may also co-exist.

More recently specific research on culture has been performed from the regulatory viewpoint (O’Brien et al., 2014; Ring et al., 2014). O’Brien et al. (2014) contend that “open, ongoing dialogue” is essential to maintain sustainability within the market via mechanisms of co-regulation. This is essential in order for understanding and evaluation of the “calculative, social and normative reasons” governing behaviours within the market (p. 122).

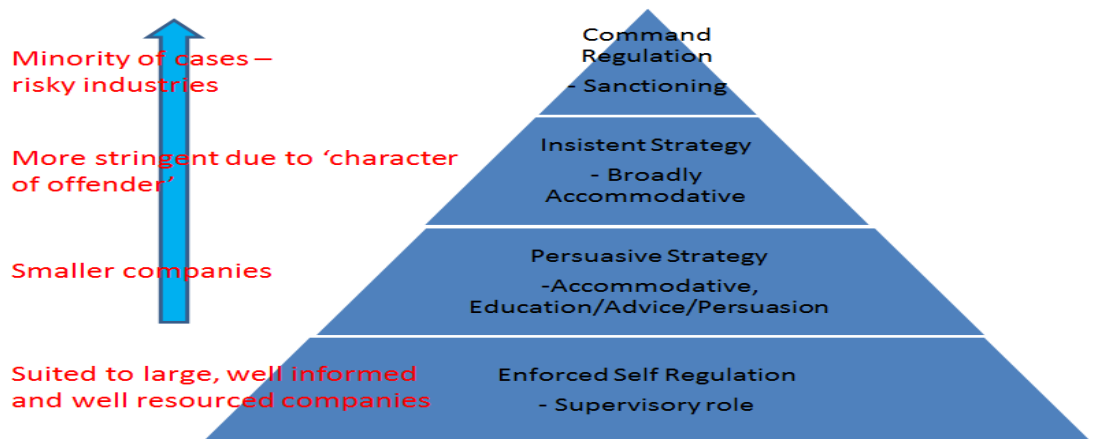
Empirical data is presented by Ring et al. (2014) in the form of a qualitative review of regulatory announcements (from the FSA/FCA). The authors contend that there needs to be clearer signposting by the regulator with regards to culture issues in order for “lessons” to be taken on board by firms in the market (p. 20).

Therefore, there appears an obvious interest in the subject of culture from both an academic and practice based viewpoint. A discussion now follows of the mechanisms and models within the literature, for regulators to respond to regulatory issues.

### 3.3.1 Responsive regulation and “the enforcement pyramid”

Ayres and Braithwaite summarised models of regulation in their 1992 publication “Responsive Regulation”. This publication is widely cited in academic literature (most notably under the legal discipline) and underpins further research and resulting models to regulatory approaches (which will be reviewed in the following section). Indeed, an entire special edition was devoted to the topic of “Responsive Regulation” (Regulation and Governance, 2013). Ayres (2013) commented on the phenomena of citations steadily increasing year on year (between the years 1993 to 2011) for responsive regulation and the “pyramid of enforcement” (see Figure 7). Under the notion of responsive regulation, it is argued that rather than the period (i.e. 1980s onwards to point of publication) being viewed as an era of vast deregulation, it should be viewed as “regulatory flux”.

Figure 7 Pyramid of enforcement (summarised from Ayres and Braithwaite, 1992 and Hutter, 1997)



Ayres and Braithwaite (1992) revisited concepts of ‘deterrence’ versus ‘compliance’ models of regulation (terms coined by Reiss, 1980) and introduced the theory of the “enforcement pyramid” (Figure 7). The theory states that the successful pursuit of cooperative regulation is predicted by “tit for tat strategy”, use of sanctions and interventions (under hierarchical range). Following the 1992 publication, the financial service sector has witnessed the “deregulation-crisis-reregulation” cycle around the 2007-09 Global Financial Crisis (Parker, 2013). Many academics have focussed on the concept of the enforcement pyramid (Parker, 2013, p. 4). Some academics have characterised the regulatory response to the latest Global Financial Crisis as a

“Minsky” moment (Kregel, 2010), to correct the instability caused by weak regulation in the markets in the build up to the financial crisis (Crotty, 2011).

Within the responsive regulation model it is considered that regulatory bodies would be able to concentrate their efforts and resources on the riskier firms. Ultimately, this would align to the goal of compliance with law/policy/regulation whilst minimising compliance costs of regulatory bodies (efficiency/cost reduction). Gossum, Arts and Verheyen (2010) specifically comment that the “main advantage of compliance specific response is the reduction in the regulators compliance cost”, through a varied approach of persuasion through to interventionist and enforcement (p. 248).

The theory of tripartism, and the ideas of public interest groups (PIGs) becoming fully fledged players in the regulatory game between the regulatory agencies and the firm to deter regulatory capture, were also proposed by Ayres and Braithwaite (1992). Responsive regulation was developed during a time of focus on national regulation, and of course regulation (and associated problems) has increasingly shifted towards a transnational level (Abbott and Snidal, 2013). Responsive regulation has been developed further in more recent publications (Omarova, 2011), which will be discuss further under Section 3.4.3.

### **3.3.2 Self-regulation and responsive regulation critique**

Ayres and Braithwaite (1992) originally discussed the idea of enforced self-regulation, as a form of subcontracting regulatory function to private actors. They linked the idea of self-regulation, to earlier theory developed by Ronald Coase in 1937 (whereby firms would be organised to produce goods and services when internal production was cheaper than external market transactions). They distinguished this from “co-regulation” which they stated to mean “industry association self-regulation with some oversight and/or ratification by government”, and under which they considered the contemporary British system for regulating financial services to sit under<sup>49</sup>.

In summary the strengths of enforced self-regulation stated by Ayres and Braithwaite (1992) include: flexibility of rules/regulation to changing business environment; commitment to rules (due to participation in setting rules, and bearing costs of own regulation); focusing on offenders (resulting in higher disciplining rate). Overall this route would result in compliance becoming “the path of least corporate resistance”.

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<sup>49</sup> Please refer to Section 2.1 for the history of the UK regulatory regime.

The concepts of deregulation in the form of self-regulation reflect neoliberal ideology, which was supported by advocates such as Alan Greenspan<sup>50</sup> (Mason, 2009). However, following the crisis in 2008, Greenspan “admitted a flaw” in the (neoliberal) worldview that he had been practicing for 40 years (Mason, 2009, p. 118). Pre- and post-crisis, a number of authors have explored the ideas of enforced self-regulation further (Stefanadis, 2003; Coglianese and Lazer, 2003; Ford, 2008 and 2011; Gilad, 2010), whose work is discussed further below under Section 3.4. Also, following the crisis Braithwaite has proposed a “clarification” and evolution to the original theories set out in their 1992 founding work (see Section 3.4.3, reviewing evolution of regulatory theory). Although the literature presents a “black and white picture of competing models of regulation” of command and control and self-regulation (Sinclair, 1997, p. 531) this is not realistic in practice, and policy makers may choose to cherry pick the best elements of regulation models. Baldwin and Cave (1999) provides a summary of the different regulatory strategies i.e. command and control, self-regulation, incentives, market harnessing controls, disclosure, direct action, rights and liabilities law and public compensation, with exemplars from industry, including a critique of strengths and weaknesses of each strategy.

Nevertheless, barriers still remain to develop the ideal model or system of regulation in the complex and rapidly changing world of financial services. Norman (2011) discusses self-regulation, in relation to business ethics, specifically commenting on compliance whereby “the most powerful way to have historically made corporations more socially responsible, or better corporate citizens, is through state regulation (including the pervasive threat of tort law)” (p. 48). Braithwaite’s (2002) earlier discussion of reward/punishment would apply in this instance. Whilst promoting “persuasion” reinforced with “punishment”, Braithwaite contends that to “manifest a desired behaviour” reward is a more successful strategy than punishment. This is difficult to apply to the financial service industry as how can we measure reward in an (historically) profit driven market. The reward in this instance may be considered then to be promotion of reputation or “informal praise” (Braithwaite, 2002, p. 24).

Although many authors have discussed Ayres and Braithwaite’s responsive regulation model, there seems to be limited empirical evidence regarding the model. Nielson (2006, 2009) discusses the lack of empirical evidence, and offers an empirical analysis of regulatory inspectors’ actions (and how responsively they react) across four regulatory areas. Few authors have empirically tested responsive regulation due to the

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<sup>50</sup> Chairman of the US Federal Reserve from 1987-2006.



“complex, ambiguous and all encompassing” mix of strategies upon which there are inherent difficulties to form hypotheses (Nielson and Parker, 2009; Parker, 2013, p. 3). Nielson and Parker (2009, p. 377) empirically tested “tit for tat” responsive regulation and “restorative justice” responsive regulation. The findings are “not consistent” and they call for further research stating:

“If a responsive regulatory strategy is the most effective strategy, a future research question is: How do we design regulatory agencies that promote such behaviour?” (Nielson, 2009, p. 413)

Parker (2006) specifically reviewed responsive regulation ‘in action’ within the Australian Competition and Consumer Commission (ACCC). This is a development on her earlier work in the book “The Open Corporation” (Parker, 2002), in which a wide scale empirical study (unstructured interviews) of regulators and self-regulation profession was undertaken. Parker (2006) suggests that there are inherent pitfalls faced by regulators in the form of the “deterrence trap” and the “compliance trap”. The deterrence trap (where penalties are not sufficient to deter misconduct) is considered manageable through “skilful” use of responsive regulation (Parker, 2006, p. 593). However, the inherent issues of the compliance trap (whereby political support for the “moral seriousness” of law enforcement is lacking) are only resolved via political action:

“This is the heart of the compliance trap dilemma. In the absence of authoritative, broader political and cultural support for the regulator’s view of the law the regulator is trapped. There is no technique, style, or approach the regulator can utilise to improve compliance where the meaning of compliance is politically contested” (Parker, 2006, p. 611)

Other academics contend that responsive regulation is not suitable in instances where the regulator does not have sufficient resources to detect non-compliance, as a relationship between the regulators and the regulated becomes impossible (Smith, 2011). The Australian financial service sector is used as an example to demonstrate where the regulator cannot “escalate” through the pyramid effectively. Criticism is directed at the regulator when reactive “compulsory investigative powers” are employed (which is implicated as a resourcing issue), as this sets the context of the relationship as “adversarial” (Smith, 2011 p. 722). This contrasts to the context of a persuasive strategy that could be adopted in the case of more regular and proactive monitoring/surveillance.



Since the latest crises there has been a returned focus by governments, regulators and academics to macroeconomic theory, with some commentators linking the latest financial crisis to macro imbalances within certain economies (FSA, Turner Report, 2009, p. 13), and calling for a “macro prudential” focus to be applied by regulators (IMF, 2010). The regulatory approaches pre-crisis were largely based on the intellectual assumption of theories of efficient and rational market (FSA, Turner Report, 2009), and the report contends that there needs to be critical reflection on these theories in the wake of the crisis. Within the UK, the Financial Policy Committee was created in interim form in 2011 (and statutory form in 2013) in order to address macro prudential regulation, with responsibilities of “identifying, monitoring and taking action to remove or reduce systemic risks” with the UK financial system (Murphy and Senior, 2013).

There have also been calls for further research in the area of macro prudential policy in academic literature (Galati and Moessner, 2010). They concluded that the current drive for decisions on macro prudential policy has occurred “against a background of limited research, and analytical tools and data available so far that could inform these policy decisions in a meaningful way” (p. 25). Baker (2010) also argues for the case of macro prudential regulation, and states this philosophy leads to intellectual independence from industry. In their review of macroeconomic literature, Galati and Moessner (2010) consider that more research is required on effectiveness of macro prudential tools. They also conclude that there needs to be further study on how monetary policy and macro prudential policy should be coordinated. This proposal does not form an area of research in this thesis, however, this provides meaningful context to the continuing changes within UK financial service regulation.

### **3.4 Academic literature pre- and post-crisis**

There is a divide in the direction and commentary of academic research relating to regulatory approaches, pre- and post 2007-2009 financial crisis. There appeared to be support of deregulation and the self-regulating profession pre-crisis. However, post crisis there has been criticism by some authors of the regulatory approach, and use of risk based approaches to regulation.

For example, pre-crisis, Stefanadis (2003) illustrated some of the benefits of self-regulation, although it was not implied that formal regulation should be abandoned. The author considered the main advantages to self-regulation to be faster access to information about new, efficient technologies and their adoption in the financial sector. Coglianese and Lazer (2003) discuss the ideas of management based regulation (a

form of process orientated regulation). This approach seeks to take advantage of private sector understanding, compelling regulated parties to conduct their own evaluation, find their own control solutions and document all the steps they take. They argue that management based regulation gives firms flexibility to develop their own approach, and the underlying assumption is that effective management based regulation is also relatively cost effective as management plan around the lowest costs solutions available.

Hutter (2005, p. 4) in her research based on agency websites of regulatory initiatives, discusses the Financial Services Authority's "self-consciously signalled approach" to risk based regulation, and links this into the British Government's "adoption of risk management". Hutter calls for further research to understand how different organisations (regulators, domains and countries) understand risk, and also to investigate further the extent to which rhetoric and ideas of risk based approaches translate into action. Alexander (2006) argued that regulators are uniquely positioned to balance the relevant stakeholder interests in devising governance standards for financial institutions, whilst achieving economic development objectives and minimizing the externalities of systematic risk. Alexander considers that regulators and supervisors are acting as agents on behalf of broader stakeholder interests in the economy, and regulation is necessary to align incentives of all parties. They consider a proactive approach is necessary by regulators, due to the "special risk that bank and financial firms pose to the broader economy" (p. 34), a statement clearly demonstrated during the financial crisis of 2007-2009.

In the "immediate aftermath" of the crisis Ashby et al. (2013) collected data via semi structured interviews with 20 risk management and financial service professionals. The interviews were held in July/August 2009 and focussed on: the cause of the financial crisis; the role of risk management and its implementation; and how organisational factors (culture and governance) contributed to the crisis. This qualitative analysis provided rich insights into the perceived "conflict between risk management and other business functions" (Ashby et. al, 2013, p. 6). In conclusion the authors comment that despite the multiple causes of the financial crisis, that there were key factors which explain the actions of certain institutions choosing high risk approach:

- "human and cultural weaknesses at the institutional, industry or society levels;
- Communication weaknesses within some financial institutions, where boards and senior managers either did not receive .... or failed to understand this information;

- Weaknesses in the prudential regime for banks and the investment firms coupled with flawed supervision.” (Ashby et. al, 2013, p. 11)

Post crisis there is critical assessment of the regulatory approach “New Financial Architecture” (NFA) by Crotty (2009). Crotty describes NFA as “light regulation on commercial banks, even lighter regulation of investment banks and little, if any, regulation of the shadow banking system” (p. 564). The author contends that regulation of the financial markets will not be effective unless it “substantially reduces the perverse incentives that pervade the system” (p. 566). The article continues to criticize tools employed by regulators/financial institutions including VaR (value at risk), which is described as “one of many possible examples of totally ineffective regulatory processes with the NFA” (p. 572). Value at Risk is a statistical measure which was widely used to assess levels of risk within firms/investment portfolios, and represents maximum loss not exceeded with a given probability, over a defined period of time. There are various assumptions and variations in application, but the most common assumption used is that historical market data is the best predictor of future change, maximum loss not exceeded with a given probability defined as the confidence level, over a given period of time. Jameson (2008) also discussed the failures of VaR, and comments that “the choice of methodology, underlying statistical data, and the modeller’s implementation skills are all extremely important in determining whether the resulting VaR numbers are useful or misleading” (p. 9). Perignon and Smith (2010) performed a quantitative study which reviewed both the level of VaR disclosure and the accuracy of the figures provided over the period 1996-2005. They argued that historical simulation was the most popular method, whilst noting that this method had limitation in forecasting the volatility of future trading revenues. They concluded whilst the quantity of VaR disclosure had increased over time, the actual quality of reported figures had not improved, whilst commenting that VaR’s are “excessively conservative” and that there was a “disconnect between historical simulation VaR and future volatility” (p. 29).

Bartle (2008) discusses the models of risk regulation and governance and describes two models, of a “scientific technocratic” approach and a “social political” approach. The conclusion on the two models is that there appears to be an emphasis on quantitative techniques at the expense of qualitative techniques. This has specific ramification in the use of Regulatory Impact Assessment, which at that time focused more on quantitative techniques. There was also criticism levelled specifically at the FSA, who had “pursued quantitative techniques more than most regulators, but had been forced to admit that it had made significant mistakes in risk assessment over the problems of the bank Northern Rock” (Bartle, 2008, p. 15).

Some academics have summarised the literature following the crisis, for example, Wilson et al. (2010) comments on the increased focus on regulators and calls for improvements in regulation. They conclude that further research was necessary to investigate the overall impact of securitisation and other risk management practices on financial sector efficiency, and on allocation of risks, in order to propose and design “the most appropriate regulatory blueprint” (p. 33). Ford (2011) also discusses the literature post crisis, and argues that enforced self-regulation and other process based regulatory approaches would benefit from greater attention to both macro forces (background influences of power) and micro forces (such as form, natures and drivers of incremental changes). The article goes on to discuss the work of other scholars in development of meta-regulation theory (Gilad, 2010), and updates to responsive regulation theory (Braithwaite, 2010) discussed under Section 3.4.3. A number of reasons for regulatory failure during the crisis are discussed, including the comment that “the SEC and the FSA arguably embraced innovation to such a degree that industry innovation utterly outstripped regulators ability to stay abreast of developments within their remit” (Ford, 2011, p. 623). The article concludes that responsive regulation is now built on mechanisms of learning through experience, and so has evolved into a meta-regulatory approach (see also Section 3.4.3).

However, despite the criticisms of ‘light touch’ regulation within the literature there are still some authors who still promote models of self-regulation. Omarova (2011) provides a “thought experiment” of the merits of a new model of “embedded self-regulation” within the financial sector, focusing on systemic risk prevention and “imposing the responsibility of protecting the public from the financial crisis directly on the financial service industry” (p. 438). However, in comparison with the current financial regulatory structure, to the successful self-regulatory systems in nuclear and chemicals industry, the article argues that under the current structure the financial industry “lacks meaningful incentives to develop this new type of more publicly minded and socially responsible self-regulation” (p. 413). Omarova (2011) suggests that one of the most important obstacles to self-regulation in financial industry is the lack of a “community of fate” mentality, due to the security of “public safety net and the near certainty of government bailouts” (p. 420). The article also concludes that financial institutions, whose profitability depends on the acquisition and application of information not available to competitors, would find difficulties in cooperation and sharing of knowledge with their peers in the industry. Norman (2011) supports this discussion in relation to business ethics commenting on a lack of:

“principle based guidance for when exactly firms in competitive markets must constrain themselves from pursuing profitable opportunities [...] that are legal but possibly unethical or irresponsible” (p. 47).

Other contemporary models are discussed further under Section 3.4.3.

### 3.4.1 Critique of “regulatory capture”

“is regulation simply an arena in which special interests contend for the right to use government power for narrow advantage?” (Levine and Forrence, 1990)

A number of articles post crisis have explored the ideas of regulatory capture, and its impact within the context of the regulatory crisis. In case of regulatory capture, it is observed that regulations evolve which meet the needs of groups (including the regulated parties) rather than that of public interest (Etzioni, 2009). Yackee (2012) contends that such groups highly influence the “pre-proposal stage” of regulations.

Baker (2010) also discussed the four mechanisms of regulatory capture: lobbying, degree of political salience, institutional design/revolving door and intellectual capture and then comments on the pro-cyclicality of regulatory capture, and how capture is “relatively easy during boom periods, but becomes much harder when regulation is re politicized in the context of a crisis” (p. 652). Young (2012) has a counter argument to scholars who rely on the concept of regulatory capture to explain regulatory oversight, and regulatory failures. Within his research article he demonstrates that despite extensive lobbying efforts, the private sector influence did not always manage to weaken regulatory standards (utilizing methods of process tracing analysis for three case studies). After providing a number of specific arguments in his article, he concludes:

“the line between public and private was drawn with the word discretion: regulators had discretion to choose unpopular decisions; discretion to say no to bankers demands; discretion to pick and choose which information to utilize from private sector groups and which to reject” (p. 20)

Young calls for a change in focus towards research on regulatory capture, to pursue an approach to investigate the conditions under which private sector groups are successful in their lobbying effort and those where they are not successful.

Further empirical evidence is provided by Harvey and Bosworth (2013), which supports the concept of a “captured model of regulation” within the UK. Through a review of FSA data on fines, they contend that “sanction avoiding compliance” is in place, with a

tendency of box ticking culture rather than a focus on unearthing the underlying compliance (and criminal) issue (p. 9). In conclusion they point to the regulators' tendency towards "maintaining public confidence" and compliance officers over consideration of "commercial sensitivities" in exposing non-compliance/criminal activities.

In response to academics criticising regimes for light touch regulation (which Davies (2010) contends is a phrase almost never used by the regulators themselves), and citing "risk based approach" and "regulatory capture" as significant factors impacting on the most recent financial crisis; new models have been proposed by academics to avoid the pitfalls encountered in the past. The concepts around regulatory capture within the literature reviewed here may indeed have implications for this study into compliance. If these powerful groups could be used and harnessed by compliance officers with the emphasis on "discretion" as highlighted by Young (2012), then useful knowledge transfer may be possible between these groups, compliance officers and the regulators. Yackee (2006, p. 728) commented (pre-crisis) on the advantages on use of such groups by agency officials, due to the variety of "tools and resources" that they offer.

### **3.4.2 Models of risk regulation and governance**

There have been a number of studies focussing on the relationship between risk regulation and governance. Fullenkamp and Sharma (2012) argue that policy makers seem to lack an awareness of how earlier crises were resolved and the most effective strategies to deal with the crisis. They propose a model for "regulatory academies" whereby policy makers could access an archive of the evolution of rules and regulations, historical information on regulatory and legal failures, financial scandals and systematic crisis. They consider that by making regulatory agencies both financially and intellectually independent this would transform the regulatory cycle, and improving the quality of supervision, regulation and enforcement.

Helleiner and Pagliari (2011) comment on the interaction between each of the policy arenas, interstate, domestic and transnational following the financial crisis, and propose that academic researchers may now need to consider reanalysis of the previous concept of strengthening of official international standards, towards a weakening in the post crisis world. A counter "global" view is suggested by Moshirian (2011), who called for a "new global framework that should create an independence and partnership between international institutions and national authorities" (p. 511). These ideas were developed further in Moshirian (2012) in which the paper concluded



that the “gradual emergence” of a world central bank could result in “less regulatory arbitrage, more successful implementation of international rules and agreements and a more stable global financial system in the future” (p. 2679). The author comments on the emergence of the European Central Bank, which has theoretically reduced the burden of national regulation and allowed for more efficient and stable economic activities (whilst recognising the current financial turmoil). Therefore, questions appear to remain over the influence such ‘macro’ communities have towards regulatory compliance.

Another view of governance is offered by Becher and Frye (2011), who performed multivariate statistical analysis, providing empirical evidence to review the relationship between regulation and governance. Within their review of literature they comment on the concentration by academics on the “notion of substitution of regulation for governance” (p. 26) (substitution theory), despite mixed empirical evidence. They test various hypotheses with regard to substitution theory, and conclude instead that regulated firms do not have significantly lower monitoring, and following periods of deregulation firms appear to decrease monitoring. They suggest the notion that regulatory pressure may encourage greater monitoring. They state that their findings support the hypothesis that regulation and governance are compliments, and may work together to ensure an effective governance structure.

### **3.4.3 Contemporary models/Evolution of regulatory theory**

Given the enormity of events of the most recent financial crisis, academics and practitioners have questioned the validity of concepts and models pre-crisis. Arnold (2009) reviews the role of accounting research in the most recent global financial crisis. On review of the publication record of the “premier” accounting journals both pre crisis and post in relation to discussion of structured investment vehicles (SIVs), including special purpose entities (SPEs), and qualified special purpose entities (QSPEs), securitisation and off balance sheet entities (mortgage bank securities – MBSs, and collateralised debt obligations – CDOs), Arnold (2009) argues that the dangers of such practices were not highlighted until the credit crisis was already underway. Haynes (2015) concludes that new UK legislation (the Financial Services (Banking Reform) Act 2013), and the separation of retail and investment banking, would have been unlikely to prevent the crisis.

However, given the global nature of the crisis, it appears unclear how to explore the phenomena, and which criteria to use to measure success or failure. Davies (2010), commented that only two countries (Canada and Australia) appeared to fair well during

the crisis. A number of academic articles following the crisis highlighted the apparent lack of understanding of the dynamics of systematic risk accumulation, by both the regulators and the firms themselves (Omarova, 2012; Galati and Moessner, 2010; Arora, 2010). Langevoort (2012) contends that “sophisticated financial actors from both buy and sell side” continued to transact despite the awareness of risks within the portfolios – “a manifestation of agency cost and moral hazard” (p. 498). There is also now a spotlight in accounting research on the financial reporting rules over off balance sheet structured investment vehicles (SIVs) and the consulting services offered by some of the international accounting firms in the lead up to the crisis (Arnold, 2009). These discussions of ‘lack of understanding’ correlate with the issue of how financial service firms should implement effective compliance strategies to deal with new and improved regulation that is being proposed following the crisis.

Following the financial crisis, Braithwaite (2010) revisited his founding work (Ayres and Braithwaite, 1992). He summarised and reformulated the model under nine principles. He commented on reactions to responsive regulation approaches whereby some criticism on its complexity had been levelled from some scholars, and counter argued that the principles of responsive regulation should be likened to “good parenting” describing responsive regulation as a “natural social process”. To summarise, the nine principles under responsive regulation were re-clarified as: “Think in context; Listen actively; Engage those who resist fairness (whilst showing respect); Praise those who show commitment; Signal preference to achieve outcomes via support and education, to build capacity; Signal (but not threaten) a range of sanctions which you can escalate; Network pyramidal governance by engaging wider networks of partners (as you move up the pyramid); Elicit active responsibility; Learn, and communicate lessons learned.” (p. 476). This work reinforces the importance of the relational elements and communication, between regulator and the regulated.

As discussed earlier in Section 3.3, the responsive regulation model is widely cited and there is ongoing critique within the literature between Ford (2013) who calls for technological strategies, and Braithwaite (2013) who calls for relational strategies to resolve “scalability challenges”<sup>51</sup> in regulation (Braithwaite and Hong, 2015, p. 25). An

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<sup>51</sup> Whereby, effectiveness of regulation and monitoring are impacted by size and complexity of the industry i.e. relationships between the regulator and the regulated become more difficult with size. Ford (2013) defines scalability as a “measure of whether and how well a regulatory strategy operates in environments characterized by greater levels of logistical complexity, workload, and scope” (Ford, 2013, p. 17).



alternative suggestion of “regulatory ambassadors” is offered, in which the relationship between ambassadors and the firm is likened to “meeting diplomats”.

Omarova (2012) introduced a new model of the “Public Interest Council” which draws on the ideas of tripartism from the original Ayres and Braithwaite models for regulation (and the ideas of Public Interest Groups, or PIGs). The ideas were set out for the US, but the theory was considered transferable to other financial service regimes. The Public Interest Council’s main function would be to impose structural checks on regulatory capture and to diffuse the industries power to control the regulatory agenda by maintaining constant and intense public scrutiny (Omarova, 2012). The author was critical of the Dodd Frank Act (see also Section 2.3), and stated “the act does not directly address the issue of regulatory capture and agencies failure to act in a publically minded manner” (p. 631). This work echoes ideas put forward by Levine (2012), who calls for a “Sentinel”, an institution which would be politically independent and independent of the financial markets. The Sentinel would need to be expertly staffed with a “coordinated team of well-informed financial economists, lawyers, accountants, regulators and individuals with private sector experience” (p. 41). Omarova refers to Levine’s proposed solution of the Sentinel, and considers that this falls short of a “truly tripartite approach”, and the “mission of guarding the public interest against captured or corrupt regulatory agencies would become entrusted to yet another agency” (p. 638).

Although not related specifically to the financial crisis, one area of concern for practitioners globally is that of Suspicious Activity Reporting. The normative and ethical approach to regulation is considered by Ryder and Turksen (2014) in relation to regulatory response following the terrorist attacks in the US in 2001. They discuss that whilst ethical approaches to regulation may not be seen as “salient to some”, the importance of “enlightened moral judgements” is essential to support “sustainable, legitimate and ultimately effective counter terrorism strategy” (p. 6). Ryder and Turksen (2014) argue that despite changes to legislation, there is limited evidence “that the ‘international’ response to 9/11 is working” (p. 43). The additional burden<sup>52</sup> of such regulation (and the knee-jerk reactions of policy makers and regulators to crisis) impacts the compliance officer’s role directly. The same argument could be applied to new legislation (and whether it is ‘working’) following the most recent financial crisis,

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<sup>52</sup> In an earlier paper, Ryder (2008) highlighted the British Banking Associations claim of AML compliance costs approximating to £250 million each year.

and whether anything has been achieved by new regulatory requirements and banking reform.

Other authors also try to develop existing regulatory models further, following the crisis. Baldwin and Black (2008) comment on a number of the academic models of regulation: responsive regulation (Ayres and Braithwaite, 1992), smart regulation (Gunningham, Grabosky and Sinclair, 1998) and risk based regulation (Hampton's 2005 Report). The authors offer criticism of these models (notably on the practical problems faced by regulators i.e. resource constraint, unclear objectives, changes in regulatory landscape), and suggest an alternative "really responsive regulation" which they apply to the UK Environmental and Fisheries control. Under a really responsive framework the regulators are:

"to be really responsive regulators have to be responsive not only to the compliance performance of the regulatee, but in five further ways: to the firm's own operating and cognitive frameworks (their attitudinal settings); to the broader institutional environment of the regulatory regime; to the different logics of regulatory tools and strategies; to the regime's own performance; and finally to changes in each of these elements" (p. 61)

Trying to draw the literature together, Gilad (2010) discusses regulatory approaches that she considered to be "one family of process orientated regulation" (p. 485), and which had been labelled separately by various scholars in recent literature "system based regulation", "enforced self-regulation" (Ayres and Braithwaite, 1992), "management based regulation" (Coglianese and Lazer, 2003), "principle based regulation" (Ford, 2008) and "meta regulation (Parker, 2002)" (p. 488). Meta regulation is an approach proposed to hold the regulatee and regulator accountable for continuous improvements in regulation, and compliance, through a learning orientated approach to regulation. A useful comparison of meta-regulation (as a subset of process orientated regulation) is made with prescriptive regulation and also outcome orientated regulation, and is provided in tabular form. An important observation is made that "real life regulatory regimes" are likely to combine more than one regulatory model in their approach, and provided the example of the British financial regulation regime whereby "outcome orientated regulation stipulates firms to provide retail customers with suitable investment advice, while prescriptive rules detail the type of information and documents that firms should provide to clients" (Gilad, 2010, p. 489). In a review of the literature, and empirical examples provided the conclusion as drawn that "current research, although limited and inconclusive, indicates that process orientated regulation

institutions tend to have a positive, albeit highly varied, impact on the fulfilment of regulatory objectives” (Gilad, 2010, p. 502). There are calls for further research to investigate whether meta regulatory approach can support organisation capacity building.

There has also been some empirical research performed to support new models. Klomp and Haan (2012) applied principal component analysis to examine the impact of bank regulation and supervision on bank fragility. They comment that prior research had provided mixed results on effectiveness of bank regulation and supervision in reducing banking risk. They concluded that supervisory control, capital regulation and market entry regulation had significant effects on capital and asset risk. Further, they found supervisory control on activity restrictions, private monitoring, market entry restrictions and liquidity had a significant effect on liquidity and market risk.

Using research questions of why did nobody notice the financial crisis, and what were the causes? Cabral (2012) proposes a quantitative model, based on the development of an “Industrial Organisation” type banking model. The paper concludes that as a result of the combined changes to the regulatory framework for capital requirements (Dodd Frank Act, Basel III, and existing policy of the FDIC Improvement Act) that the US regulatory framework will be more robust than imposing BASEL III alone. Therefore, this paper is limited due to its focus towards the US market and the impacts thereon, rather than considering the effects of international regulatory requirements (or indeed, the impact of the focus of this study, UK compliance officers facing these international standards).

Ongoing empirical evidence into trust in financial services is presented by Devlin (2014), with data collection on a six monthly cycle from 2009 onwards. Measures on trust are presented in a series of waves, with indications of improved overall “trust ratings” since 2013. The author contends that “fading memories” of the financial crisis account for the results. However, this evidence contrasts with evidence provided in publications issued by the FCA relating to ongoing scandals relating to culture within the sector (FCA, 2013; FCA, 2014).

As can be seen from these papers there is wide commentary on the broad regulatory initiatives in place by national and international regulatory bodies (from both an academic and practical literature base). However, Llewellyn et al. (2014) contend that trust is still lacking, despite the ongoing focus on regulatory and prudential reforms in response to the crisis. To counter the lack of trust, the banking sector needs to fulfil the

distinctive needs of customers. Reference to virtue theory<sup>53</sup> and “advocating more virtue” within the sector is proposed (p. 6) to ensure the “long term prosperity of customers”. The authors contend through improvements to internal governance (professionalism and ethics), competition (customer led and directed), and market diversity (through range of business models), the banking sector may become more “virtuous”. Racelis (2014, p. 29) adds to this argument, with survey research indicating attributes of; honest and competence, kind-heartedness, self-confidence, innovativeness, ambition and security as essential virtues for the financial service sector to move forward following the crisis. However, compliance officers may argue that they have been working towards this virtuous purpose previously, and ultimately they are inhibited by conflicting motivations to comply i.e. economic, in competition with normative aspects within the firms they serve. Graafland and Ven (2011) earlier commented on this whereby:

“a renewed sense of virtues in the financial sector alone will not be sufficient to restore the internal goods in financial sector. Institutional changes will also be needed to allow banks to put their mission into practice” (p. 616)

A further discussion of motivations for compliance and compliance culture is presented in Section 4.3.1.

Given the evident interest in the regulatory cycle within the academic literature and the regulatory body’s commissioned reports both preceding and following the financial crisis, this highlights a potential research question with regard to compliance functions within financial service sector. In an environment where “regulatory structures have been flexed and reformed with little rationale for one method or another” (Harvey and Bosworth, 2013, p. 2), it is unclear how compliance officers are supposed to make strategic decisions over compliance approaches. It is not obvious whether compliance officers and management would proactively monitor the regulatory cycle when strategizing compliance functionality within the organisation. Research objective 1/research question 1 emerged from this discussion. The identified gap is summarised in Table 5 at the end of this Chapter.

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<sup>53</sup> An interrogation of Google Scholar (under search terms “virtue theory” and “regulation” and “financial services”) indicated only a limited number of other authors have considered this topic under the lens of virtue theory (82 references as at 28 July 2015). More general discussion of ethics has been applied by other academics as discussed in Section 4.3.1.

Objective 1 -To understand the motives for regulatory compliance by banks

RQ1 To what extent does the regulatory cycle influence managements' decision making over compliance approach

Although there is an abundance of academic critiques and 'solutions' in the aftermath of the financial crisis, there seems to be little empirical evidence for alternative approaches to regulation.

### 3.5 Cost benefit analysis (CBA) and cost of compliance reviews

A review of the literature around regulation and compliance would not be complete, without due consideration of the costs and benefits of regulatory compliance. Despite a wealth of general commentary on cost of regulation and compliance by scholars, there appears to be limited empirical evidence within academic literature available on cost benefit analysis in relation to financial service regulation and compliance. Attempts have been made more recently in the US literature to reopen cost benefit arguments (Sunstein, 2015; Coates and John, 2014), with a critique that case study research "show that precise, reliable, quantified CBA remains unfeasible" (Coates and John, 2014). The lack of empirical evidence may indicate the complexity in measuring both the costs of regulation and compliance, and the benefits of regulation. There is also on-going criticism of the cost of regulation and compliance in more commercial literature. For example Green (2005) commented that the "immeasurable costs are the opportunities that are lost because management is worrying about compliance and not running the business" (p. 41). Therefore, regardless of its complexities, this appears to be an area meriting future academic research, due to the ever present interest by practitioners in cost analysis.

#### 3.5.1 Cost benefit analysis

Using "cost benefit analysis" and "financial services" and "compliance" as keywords yields many potential articles within broader literature searches<sup>54</sup>. However, on further review, many of these articles are not related to financial services, or have not been subject to peer review. There are two older academic articles which specifically review cost benefit analysis in relation to UK financial services. Alfon and Andrews (1993) consider cost benefit analysis (CBA) essential to review whether the benefits of regulation are proportionate to their burden, and that regulation does not undermine innovation and impede competition unnecessarily. They conclude that the main

<sup>54</sup> As an example 6,390 plus recorded in Google Scholar in June 2015.

problem with CBA is lack of data, which is partly as a result of difficulties in identification of incremental compliance costs.

Franks, Schaefer and Staunton (1998) review costs in their study (via mixed method analysis) and concluded that the direct cost of regulation were substantially higher than predicted at the time of the Financial Services Act. However, they also concluded that direct costs of regulation for the “securities and derivative trading and broking sectors are substantially lower for the UK, than the US and France” (p. 1547). They also commented on the “dearth of studies” which reviewed the benefits of regulation, in light of the significant costs imposed by regulation in the financial service sector.

More recently, Coates and John (2014) and Sunstein (2015) have reopened arguments in the academics literature on financial services regulation (from a US perspective). Coates and John (2014) reviews a number of cases (including Sarbanes Oxley, SEC reforms and BASEL III impacts) and argues that:

“the capacity of anyone – including financial regulatory agencies, OIRA, academic researchers, CBA/FR proponents, litigators or courts – to conduct quantified CBA/FR with any real precision or confidence does not exist for important representative types of financial regulation” (Coates and John, 2014, p. 89)

This indicates that ‘guesstimated’ CBA is performed, and this is not a desirable underpinning to policy setting. Whilst arguments are provided as to why cost benefit analysis is complex (including the macro impacts on the economy and the “non stationary” relationships in the sector), Coates and John (2014) does not offer solutions to the issue. Sunstein (2015) critiques the review by Coates and John, and argue that despite “knowledge problems” within the domain, that there is no reason that CBA should be dismissed or ignored within financial service regulation. Instead the financial regulators are encouraged to perform and publish CBA with caveats, and in the absence of important information breakeven analysis should be performed (Sunstein, 2015, p. 279).

### **3.5.2 Compliance costs**

Irrespective of CBA performed at governmental level, prior to implementation of new regulation, the majority of organisations are more interested in understanding the costs to their own business of complying with regulation. Therefore, this area of research provides a stream of academic research which has direct links to practitioners’ immediate concerns to understand the cost of compliance. Elliehausen (1998)



reviewed a number of studies on cost of regulation in banking. The article concluded that the majority of costs are related to labour i.e. the amount of time spent by bank officers and managers on compliance related activities. This is supported by other academics (Bamberger, 2010). The observation was made that small banks have cost disadvantages compared to larger banks, and this may discourage market entry of new firms into the banking sector. In addition the article concluded that “frequent minor revisions to regulation might be more costly to banks than making infrequent major revisions” (p. 452). Garcia (2004) discussed IT spending and challenges faced by financial institutions to comply with regulations. The author contended that an analysis of total IT spending on compliance is not a “tangible or purposeful metric” for strategic planning, and those executives should take the opportunity to strike a balance between immediate tactical results of compliance and longer term strategic values of business improvement. The attitude of some executives of “close your eyes and pay up” without giving thought to the longer term strategic values and opportunities to create business value is criticised (Garcia, 2004). Krause (2008) also discuss the issues faced by global business in light of a “bewildering tide of new regulation”. They argue, however, that in choosing the right management software, management can benefit from improved performance throughout the organisation. This of course requires careful balance of strategic vision and cost awareness.

Interview data has been presented as empirical data within a number of papers. A mixture of representatives from the FSA and the banking sector discussed the “cost of compliance” (Goodhart, 2004). There was some apparent difference in opinion even within this small group over the question of whether it is possible for firms to benefit significantly from being able to demonstrate compliance excellence. Comments from the participants ranged from “if you’re above the minimum standard, I don’t believe it makes much difference at the moment” to “questions do get asked about compliance and customers take a lot of comfort from knowing that you have a robust compliance system” (Goodhart, 2004, p. 30).

The method of interviewing compliance staff and the regulatory body was also adopted by Harvey (2004), who defined costs of compliance as the “tangible operational costs that relate to investments that institutions make in the form of physical and human capital required to perform the compliance function” (p. 335). The benefits of compliance were defined as costs that are otherwise avoided, so avoidance of penalties imposed by regulators for non-compliance, and the intangible benefits to reputation (loss of reputation results in direct costs via loss of income, indirect costs via

loss of custom, or legal costs, and opportunity costs via foregone opportunities). This study reviewed and commented on the views of costs and benefits of compliance within UK financial institutions (focused on money laundering compliance costs). In conclusion the author called for further research, and proposed a full cost benefit study.

A case study approach (using methodology of analogy cost estimation) was adopted by Sathye (2008) to estimate costs of compliance for AMLCTF Regulation (Anti Money Laundering and Counter Terrorism Funding) in Australian financial institutions. The author compared the results to other studies, and concluded that the cost of compliance “per capita” was significant, and could affect the overall competitiveness of Australian institutions due to the small size of the economy in terms of population. The author considered their methodology to be transferable to other jurisdictions.

### 3.5.3 Commercial research

In addition to academic research in the area of compliance costs, there has also been specific research performed by ‘commercial’ researchers (which has been directed specifically at an audience of practitioners). This research contributes to the overall literature (as although not specifically academic within the articles that follow, the methods employed have been justified in the same way that one would expect from academic research). In addition, these reports have been commissioned and paid for by the industry, which reflects the ongoing concern of this topic to practitioners.

The FSA released a briefing note in 2006 announcing the release of the “Cost of regulation report” undertaken by Deloitte, and “The benefits of regulation” report undertaken by Oxera Consulting. The purpose of the Deloitte report was to examine the incremental costs attributable to individual FSA rules by firms over three sectors. A major conclusion of the report was highlighted as “much of what regulation requires is in fact regarded by firms as good business practice” (p. 1), whilst the highest incremental costs were the direct fees collected by the FSA. The purpose of the Oxera report was to set out a framework for identifying and measuring the benefits of regulation.

The Deloitte (2006) report explains the sampling and methodology employed very clearly, whilst highlighting the difficulties in the review. This method could be adapted and employed in future similar studies by academics. One of the major findings was that across all three sectors the direct FSMA related fees, collected by the FSA (comprising levies funding the FSA, the Financial Ombudsman services and the Financial Services Compensation Scheme), were the highest incremental cost. The



report was clear that the estimated incremental costs of regulation differed markedly between firms (even within the same sector) and the report attributed this to different views of firms about what activities are deemed to be incremental, and also the different view of firms as to what constitutes acceptable compliance.

The Oxera report (2006, p. 1) sought a framework to establish “What to measure?” and “How to measure?” when assessing the benefits of financial regulation. The report commented that although there was a significant body of literature on regulatory impact assessment and cost benefit analysis available for review, the existing studies did not provide “a comprehensive overview of the dimensions of benefits that regulation may be delivering, or contain little discussion of how different types of potential benefits can be measured” (p. 1). The report provides a number of diagrammatic summaries of concepts, including a summary of relevant measures for each dimension of market outcomes that should be examined in the measurement exercise, as well as the main empirical approaches available for quantifying impact of the regulation. The observation was made that “benefit measurement should aim to directly quantify improvements in market outcomes that flow from regulation or specific rules” (p. 30). The report also recognised the difficulty in practice of direct measurement, and, consequently, sometimes indirect measurement (benefits evaluated indirectly by identifying and measuring suitable proxies) are a necessary alternative.

As discussed earlier in Section 2.3.1, Thomson Reuters has also recently undertaken survey research on costs of compliance (English and Hammond, 2012; English and Hammond, 2015). The results of these publications highlight “red flags for the future of regulated firms, and their compliance officer” (English and Hammond, 2015, p. 19). The most recent survey concluded that there appears to be a gap between the “current compliance challenges” and the “compliance budgets and availability of skilled resources” (English and Hammond, 2015, p. 19).

Whilst a dearth of academic literature exists around this topic (perhaps due to access issues to data), the area of cost/benefit continues to be an area of concern for practitioners. More recently in the media, practitioners have raised concerns on the rising costs of regulation (in light of a six per cent increase in fees by FCA during 2015). Quoting Mr Richards of the Personal Finance Society:

“Regulatory fines were originally intended to influence behaviours and ultimately help fund regulation. They should also be providing a dividend for the most compliant, who should pay the least.” (Fantano, 2015)

This statement raises a number of questions, including the difficulties in measurement (and rewarding) compliant behaviour (which is discussed further in Section 4.3.2).

A potential area to research further would be the extent to which internal compliance officers monitor cost of complying with regulation, and whether there is any adoption of cost benefit analysis internally when assessing compliance strategy to emerging regulation. As costs of compliance are generally considered to be difficult to quantify, this would form an area for future research following completion of this thesis, as this question falls outside the overall research objectives.

### 3.6 Chapter summary

As evidenced within this element of the literature review, a diverse range of scholars contribute to the regulatory literature. However, much of this literature has been written from the perspective of the regulators themselves, and from the perspectives of societal need, rather than the implications on those trying to comply. Much of the literature is fairly conceptual, with only limited empirical evidence offered to support regulatory models. This is most likely a reflection of the diversity in regulatory fields and regimes across different jurisdictions.

It should be noted that the literature on cost/benefit has also been included in this review, although this does not then lead to any specific research questions for this thesis. The reason for inclusion is to acknowledge the wide range of literature in this domain, and also to link into practitioner concerns over compliance costs during the resulting interviews (discussed in the Methodology, Chapter 6). Indeed the overarching supplied construct that was discussed with participants when considering their compliance experiences, was whether 'cost or benefits' were incurred (when comparing personal constructs around the participants experiences).

An initial summary of the regulatory literature gap is summarised in Table 5. Further discussion of the specific gaps, and links to the research objectives and questions is presented in Section 5.4.

**Table 5 Summary of regulatory literature review and associated gap, with link to research objective and research question**

| Literature review       | Section Discussed  | Authors calls/criticisms  | Remaining gap   | Research objective  | Research question/Potential future RQ   |
|-------------------------|--|---|---|---|---|
| <b>Regulation</b>       | Section 3.3/Section 3.4.3 Contemporary models/Evolution of regulatory theories | Proposals for alternative regulatory structure: coherence (Arora, 2010); responsive regulation/enforced self-regulation/meta regulation (Ford, 2011; Braithwaite, 2010, Gilad, 2010); Public interest council/Sentinel (Omarova, 2012; Levine, 2012). | Limited empirical evidence/research performed to test regulatory models. No research to review 'compliance strategy' to deal with regulatory cycle. | Objective 1: To understand the motives for regulatory compliance by retail banks. | RQ 1: To what extent does the regulatory cycle influence management decision making over compliance approach?   |
| <b>Compliance costs</b> | Section 3.5 Cost benefit analysis and cost of compliance reviews               | Empirical academic reviews 1993/1998/2008. Empirical practice based reviews 2006.   | Limited empirical research over compliance costs.   | Outside the research objectives of this thesis.                                   | Future RQ <sup>55</sup> : To what extent do compliance officers monitor cost of compliance? (Future research as ultimately cannot be answered in timeframe/methodology chosen). |

<sup>55</sup> For clarity, although this area is seen as a gap within the literature, this research question will be reserved for future research into the topic. This is seen to as a question that sits outside the overall objectives of this thesis and cannot be explored under the chosen research method.

## Chapter 4 Literature review – What is compliance?

The use of the word compliance in academic literature is widespread. However, the concept of the compliance function receives more limited attention by academics. During the course of the literature review it became clear that the compliance function has a number of input factors, namely regulations (to which it must comply), compliance tools, and theoretical and practical models (of how to comply). The outputs (and effectiveness) of the compliance function are viewed (from a personal and practical perspective) to be influenced by the organisational factors including attributes of compliance staffing; culture, governance and relationships; and ultimately the amounts that management are willing to invest within the compliance function. A mind map to summarise the related compliance literature is presented in Figure 8.

Figure 8 Author developed mind map of compliance literature

| Practicalities of compliance<br>(new regulations, and role attributes)  | Compliance models and IT tooling   | Outputs of compliance<br>(compliance culture and effectiveness)   |
|---|--|---|
| <b>Regulations</b><br>FSMA<br>Basel II/III<br>MiFID<br>Proposed FATCA<br>- Impact of new regulation (Gebhardt and Novotny-Farkas, Hussein and Hussan)<br>- Regulatory approaches (Hutter) | <b>Models</b><br>- Jackman (value and culture, compliance competence model)<br>- Woods (partnership/ethics framework)<br>- Edwards and Wolfe (combined partnership and culture model)<br>- Malloy (deterrence and normative model)<br>- Crump (active and passive compliance)<br>- Calcott (cosmetic compliance)<br>- Rossi (centralised model)<br>- Carter (CSA)<br>- Barraquier's ethical vs perceived profitability | <b>Culture and Governance and Relationship</b><br>- management tone<br>- Relationship with auditors,<br>- Relationship with regulators<br>- Relationship with consultants   |
| <b>Compliance Officer Attributes</b><br>-skill set<br>-authority<br>-independence<br>(Taylor, Stoneman, Gable, Somerville, SEC Commissioner speech)                                       | <b>Tools</b><br>- Mainelli and Yeandle (pilot Phophezy)<br>- Doyle<br>- Bamberger  | <b>Key Outputs (SIA Report)</b><br>-advisory, policy and procedures, education, monitoring and surveillance, licensing, culture<br><br><b>Effectiveness</b><br>- Edwards and Wolfe<br>- Demircic-Kunt & Detragiache |
| <b>Compliance cost and benefit literature (outside scope of research questions)</b>   |  |   |

In Section 4.1, the history of how the compliance function has developed in recent years is reviewed. This is further developed in Section 4.2 where the attributes of compliance officers and the role of chief compliance officers are discussed. In Section 4.3 the literature relating to compliance models, measuring compliance effectiveness, compliance approaches to new regulation, and compliance tooling is reviewed. Finally consideration of 'why management comply' is presented in Section 4.4.

#### 4.1 The role of compliance

Hutter (1997) considered that compliance with regulatory legislation should be regarded as a much as process as an event. As regulation has evolved in practice, and has become more complex, so too has compliance and thus the role of the compliance officer. Parker (2000) discusses the growth in employment of "specialist compliance professionals", to advise organisations on regulatory and ethics programs. Edwards and Wolfe (2005), state that "compliance is core to the operation and wellbeing of the financial service sector and the consumer" (p. 49). This supports, Barry's (2002) earlier argument in that an essential attribute to maintaining an ethics and compliance culture is "a shared set of values and standards" (p. 39). Therefore, the central role of compliance and the importance of ethics were apparent within the literature prior to the financial crisis. Hardouin (2011), comment that dimensions of "regulatory quality and government effectiveness are also critical to the quality of compliance" (p. 152).

A discussion document by the Securities Industry Association (SIA, 2005) also looks at the role of compliance in organisations, and consider the primary role of the compliance function is to; identify problems, deter misconduct, and potentially reduce penalties and liabilities in the event that wrongdoing has occurred. They recognise whilst ultimate responsibility remains with management to comply with laws and regulation; there is a reliance on the compliance function to play an "integral support role in helping management to address the problems and develop remediation plans" (p. 9). The report proposes a comprehensive listing of typical compliance activities, which is fairly generic, including: advisory capacity; policy and procedures; education/training; monitoring and surveillance; business unit compliance reviews; centralised compliance function (control room function/anti money laundering programme function); licensing, registration and employment related functions; internal inquiries and investigation; regulatory examinations, reporting and investigation; fostering regulatory relationships; promoting a culture of compliance; programme assessment; chaperoning (SIA, 2005, Section B, p. 6). The core compliance tasks are also confirmed by Taylor (2005) who reviewed the evolution of compliance, and

comments on the increasing cost of compliance, due to extension of regulations such as MiFID (Markets in Financial Instruments Directive). These papers act as a background summary to the concepts of compliance within an organisation. However, they are not 'traditional' academic articles and as such this is representative of wider issues within the compliance literature.

Much of the literature is practitioner focused, indicating a lack of academic influence or specific empirical research into the compliance function. This may well be due to the difficulties in accessing compliance functions (a phenomena which has been experienced during the course of completing this thesis); or indeed it may indicate a lack of generalisability which is possible across different compliance sectors (due to complexities in individual regulated sectors).

#### **4.2 Qualified officers and the responsibilities of the chief compliance officer**

“Good self-regulation professionals should see themselves both as citizens of the corporation and as citizens of a broader ethical community of compliance professionals, regulators and stakeholder” (Parker, 2002, p. 195)

The role of compliance officers has become more prominent in recent years, with attractive benefit packages being provided by employers. This means that compliance officers can be recruited direct from university, or recruited from other professions such as legal or accounting (Taylor, 2005; Stoneman, 2005). However, there does not appear to be a clearly recognised professional body<sup>56</sup> for compliance officers at present (in the UK) and no specific examinations need to be taken to act as a compliance officer (Taylor, 2005). Nevertheless, there are a number of organisations which bring professional compliance officers together and advise on suitable learning and networking opportunities (for example Professional Risk Managers International Association – PRMIA, the International Compliance Association – ICA, and the Chartered Institute for Securities and Investment - CISI). In a recent regulators/governments report, they also discuss this issue of “financial market qualification”<sup>57</sup> with a comparison to the US examination and CPD requirements (HM Treasury, Bank of England, FCA, 2015, p. 68). However, the comment of the report (which is specific to the Fixed Income, Currency and Commodities (FICC) markets) is that:

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<sup>56</sup> Although there are ‘trade bodies’ of compliance consultants which are endorsed by the FCA (for example, the APCC, see <http://www.apcc.org.uk>), these are pre-dominantly directed towards compliance officers providing consulting services.

<sup>57</sup> Note the proposals for qualification were not compliance specific.

“One option is for regulatory authorities to impose training and qualification requirements on FICC market participants, as is currently the case for certain retail market activities. However, the diversity of FICC markets means it would be challenging for a regulator to apply and maintain a qualifications framework that was appropriately calibrated to the range of different roles that FICC market participants perform.” (HM Treasury, Bank of England, FCA, 2015, p. 67)

This quote represents the difficulties in application and maintenance of examination and CPD requirements from a regulatory viewpoint. Therefore, this would stress the need for this oversight to remain at a professional body/or community of practice level (similar to the way in which chartered accountants are regulated via the Institute of Chartered Accountants of England and Wales (ICAEW), or equivalent professional membership, under the umbrella of the regulator the Financial Reporting Council (FRC)).

There are also other resources available to compliance officers. A simple interrogation of the internet, found the “Compliance Exchange” website<sup>58</sup> which was started in 1995 and is edited and compiled by an individual, to provide an online research facility for compliance officers, directors and those who study, service or regulate financial services in the UK. However, it must be noted that this website is offered by those with a vested interest in consulting. Another similar website is the “Compliance Consortium”<sup>59</sup> website which brings together consultants with financial service industry experience, offering advice on ‘compliance headaches’. This service promotes itself as being members of the Association of Professional Compliance Consultants (as a professional body recognised by the FCA) and “The Compliance Institute”. Again this service is provided by consultants, and it could be argued that these sites are primarily to market their own expertise and services.

The literature acknowledges the broad skill base required by compliance officers (Taylor, 2005; Stoneman, 2005, Gable, 2005). Taylor (2005) reviewed the roles and responsibilities of compliance officers and commented that “mere technical knowledge is not sufficient in a modern compliance role” (p. 56). Stoneman (2005) discusses the “modern compliance officer” in a more commercial article, but makes some fundamental points including the difficulties that bankers now face in light of the “torrent of information” that is available from regulators. The observation is made that due to

<sup>58</sup> See <http://www.compliance-exchange.com/> accessed initially during 2012, and available December 2015.

<sup>59</sup> See <http://www.complianceconsortium.co.uk/> accessed initially during 2012, and available December 2015.



the apparent increase in regulation, management are led to rely on compliance consultants who are “typically former bankers or former examiners”, to aid them with interpreting regulation, writing and developing policies and procedures, and then following the established procedures.

Compliance officers often have a diverse background (Gable, 2005). Compliance officers tend to be recruited from the legal and accounting communities, although specialist education in compliance and compliance qualification is emerging given the specialist nature of the role of compliance officers. Haynes (2005) is critical of the overlaps of roles in some organisations, arguing that roles of “risk management” and “risk based compliance” (and other control functions) should not be blurred (p. 150). Langevoort (2012) broadly discusses the role of in house lawyers and their relationship to chief compliance and chief ethics officers, within financial service organisations. The difficulties of knowledge management, where complex information is too “diffused throughout the organisation” (p. 508) adds increased complexities to these roles. Questions are raised within the article over the complex issues faced by these roles, asking for further research into the career progression of chief legal officers and their suitability to combine roles of ethics and compliance (p. 518).

The focus and links between ethics and compliance is not a new phenomenon. Within her 2002 speech, the then SEC Commissioner Cynthia Glassman suggested that although not specifically required, she thought it was essential nonetheless:

“A company should have an officer with ownership of corporate compliance and ethics issues” (SEC, 2002)

The speech clearly states the importance of the Chief Compliance Officers whilst also highlighting the importance of: sufficient seniority and authority; full support of CEO, ability to report directly to the board, and sufficient time and resource to implement corporate responsibility programme. Haynes (2005) also argues these points, claiming that “the compliance function can only operate effectively” if compliance personnel are suitably senior; can act independently; and have access to senior management (p. 154). There are also links to be made between the roles of compliance officers with the recent focus on accountability by the regulator (which is discussed further in Section 8.3.4).

Despite a number of blogs and commercial articles on the roles and responsibilities of Chief Compliance Officers (Volkov, 2012; Reichert, 2011; Somerville, 2010; Stoneman, 2005), there appears to be a dearth of academic literature in this area. Somerville



(2010) comments on the “origin” of the chief compliance officer, as fuelled by the savings and loans crisis of the 1980s, and also attributes management buy in to compliance with reference to comments on the speech by the SEC commissioner in 2002. An astute comment is made in this short article of “the CCO has to come to the position with knowledge acquired performing senior roles within the industry. You have to know what the secrets are before looking for where they are buried” (Somerville, 2010, p. 1). This endorses the theoretical model of seniority and authority required by the role. Hoffman (2010), in a short article, also comments on the “great strides” in business ethics in recent history, whilst also reviewing the limitations. This article comments specifically on the “Corporate Ethics Officer” role (and the restrictions of the role), whilst also likening this to the role of the chief compliance officer in mutual funds in the US. The role of a corporate ethics officer is not well advertised in the UK, so the argument can be made that this also falls under the remit of the chief compliance officer (supporting the model proposed by Jackman in 2001 and 2002 which is discussed in the following Section 4.3.1).

Given the broad roles and responsibilities a number of questions arise over what constitutes the most effective qualified officers for compliance: academic background (legal, finance or other) and whether this role should be professionalised. There appears a gap in the literature reviewing this area. As a result, it would be interesting to review a sample of job specifications and CVs of compliance officers to see how these vary across a nature of financial institutions, to conclude if there are any patterns or models to be seen (although, this will be restricted to future research as this falls outside the scope of the research objectives).

#### **4.3 Compliance approaches, methods and tools**

The challenges which face those with research interests in regulatory compliance are highlighted by Parker and Nielson (2009). They contend that there are two streams of research performed in the area. The first stream focuses on social construction, to “create understanding of compliance, and on the power relations between the actors involved” (p. 50). The second stream uses “predefined” understandings of compliance and purports to “explain what causes compliance (as predefined), or what effect compliance (as predefined) has” (p. 50). Irrespective of which ‘stream’ the research is categorised<sup>60</sup>, it is argued that the ultimate purpose of such research is to enable an

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<sup>60</sup> As elaborated within the research methodology and analysis developed in the following chapters, it may be argued that this thesis is actually a blend of these two streams. The focus within the resulting conceptual model is around relational element (or power relations between actors), whilst also contributing to the discussion of what causes (or creates barriers) to compliance.

evaluation of whether individuals or organisations are complying with the regulation, and if this then leads to the “substantive goals” of regulation (Parker and Nielson, 2009, p. 57).

#### 4.3.1 Compliance Models

There is a large body of commercial literature available regarding compliance methodology and IT tools, on which practitioners rely to develop their compliance approaches. However, there has been thoughtful development of models of compliance prepared which would be of benefit to practitioners (Jackman, 2001; Parker, 2000; Woods, 2002; Edwards and Wolfe, 2004/5).

Jackman (2001) raised the question of: Why comply? He discussed the idea of “getting by”, and “keeping the regulators happy” proposing that regulators needed to bear some responsibility to discourage the “tick box approach”. He contended that as ethical behaviour develops, less regulation is required. This supports Parker’s (2000) argument that good compliance involves engagement and persuasion within the organisation so that the “ethically and legally responsible action is consistent with business goals” (p. 345). Jackman (2001) also proposed that regulation is most effective when individuals and firms buy into the principles, and, therefore, would be committed to delivering good quality service and advice. In order for this to be achieved he commented on a commitment to simplicity:

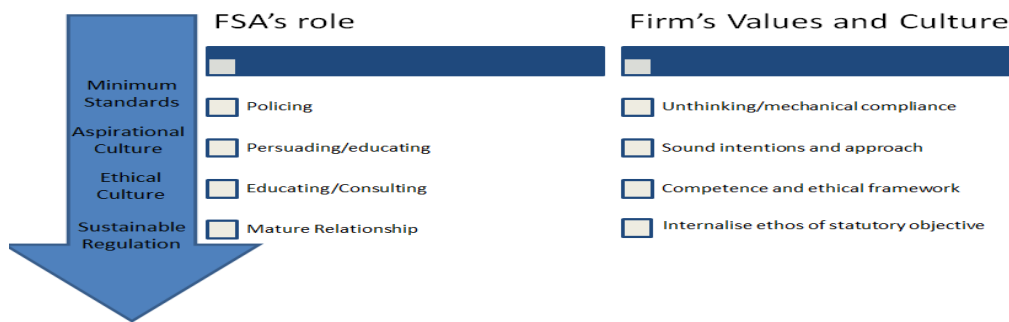
“It is likely that five rules that matter (and can be understood and remembered) are more effective than 50 that confuse” (p. 215)

This supports earlier statements of Newton (1998, p. xv) who argued that those connecting ethics to compliance find this a “substantially more useful guide than a four-inch-thick rulebook” when applying professional judgement. However, awareness of compliance culture is not considered sufficient. Compliance culture may indicate adherence with letter of the law rather than the spirit, and, therefore, this would not prevent individuals behaving in a manner which avoids the principles of regulations (Newton 1998).

Under Jackman’s model the commitment to training is also vital; with an emphasis on ensuring people understand what is expected of them, rather than compliance out of a sense of fear or a need to tick boxes. This concept of competence is supported by Edwards (2003). The emphasis of working in partnership was highlighted (using the FSA as an exemplar, and portrayed within Figure 9).

Jackman’s model has limited citations within academic literature, however, it should be noted that the model was also discussed within FSA publications due to the relevance to practitioners relationship with the regulator (and thus impact is difficult to measure). The linear nature of Jackman’s model (describing the relationship and actions of the regulator and the firms) has clear links to responsive regulation and Ayres and Braithwaite’s (1992) enforcement pyramid (Figure 7).

**Figure 9 A summary of Jackman's model (adapted from Jackman, 2001, p. 213)**



Jackman revisits this model in a later paper published by the FSA, to discuss “where ethics and regulation meet” (FSA, 2002, p. 8). The author offered the model as a framework for the development of values and culture within individual firms, or the sector as a whole. The author encouraged individual firms to think proactively about “an ethical framework” within the compliance function. The discussion paper sets out a number of everyday questions and scenarios to provoke a wider discussion of ethical behaviour within financial service firms. Jackman’s model assumed that the concepts of business ethics were already embedded within the financial service sector. However, many would contend that given the events and causes around the most recent financial crisis, that there is still a huge progress to be made in relation to business ethics within financial services. The “ethics – free zone business schools” were critiqued following the crisis (Davies, 2010, p. 34). Brenkert (2010) also reviewed the progress of business ethics and contended:

“Even if we are certain we know what they should be doing, unless we can relate this to how businesses can come to operate in those ways, the normative arguments lack power, persuasiveness and effectiveness.” (p.

709)

The support for high ethical standards has more recently been promoted by Mark Carney, Governor of the Bank of England (BBC, 2014a). Links to virtue theory<sup>61</sup> have been made by Llewellyn et al. (2014) reemphasising the ability to understand the spirit and not the letter of the law.

Edwards and Wolfe (2005) refer to the Jackman's model in their review of compliance. They consider the ideas of developing compliance competence and "an appropriate ethical culture in partnership between the regulator and the regulated" (p. 52). They liken the shift of an over regulatory approach to the more relaxed regulatory style since the inception of the FSA to the "regulatory pendulum", a term attributed to Sparrow (2000). They also consider that the regulators need to align their approach to ideas of responsive regulation (Ayres and Braithwaite, 1992, discussed under Section 3.3.1), and mirror the regulatory approach to the specific circumstances of the regulatory issue under consideration. Calcott (2010) also reviews the concept of induced self-regulation, arguing that firms may implement compliance in a "perfunctory or cosmetic fashion". However, the advantages of firms choosing their own approach is also recognised, whereby they can draw on their own experience and reflect on individual circumstances to approach compliance.

Other academics have studied compliance models in relation to organisational structure and strategy within the firm. Rossi (2010) looked at the merits of self-regulation and how the concepts could be embedded within an organisation. The paper contends that the value of compliance analysis ex post to implementation of regulation is limited, and that compliance should be used to shape strategy (which links back to the cost benefit arguments, with concepts presented by Garcia, 2004 presented under Section 3.5.2). Prorokowski and Prorokowski (2014), performed semi structured interviews in order to explore best practice in the rapidly changing compliance landscape, contending that clear structures of accountability within risk ownership should be measured against strategy (p. 76). However, these findings also promoted the concept of "clear lines of communication" with regulator to avoid sanction, within is in line with other studies (which are discussed further in Section 4.4.1).

The link to an ethical framework put forward by Jackman (2001) and Edwards and Wolfe (2005) are echoed in more commercial papers. Duska (2011) discusses the conflicts of ethical as opposed to compliant behaviour, and contends that being ethical

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<sup>61</sup> See also previous Section 2.4.2, for a discussion of underpinning theories around personal ethics.

and following the law are not the same. Duska quotes Richard Breeden (Chairman of SEC) who stated:

“It is not an adequate ethical standard to aspire to get through the day without being indicted” (Duska, 2011; p. 22)

Harvey and Bosworth-Davies (2013) review the relationship of regulation and ethics in their empirical study of regulatory intervention by the FSA. The authors describe Jackman’s model as “paternalistic” whereby “guidelines become redundant, as the ethics of compliance is embedded within the moral fabric of the regulated organisation” (p. 5). Based on their review of cases of regulatory intervention, the authors conclude that the “high pressured culture” within the financial sector, produces a “captured model of regulatory compliance” where deviant behaviour is often overlooked by both internal audit/compliance and regulators, who “steer clear of criminalising fellow employees” and inflicting disrepute on the financial service sector (p. 14). In such an environment Jackman’s model would fail to offer an appropriate regulatory solution, where compliance is seen as a box ticking exercise and a barrier to operations (rather than the proposed ethical framework).

However, other authors concentrate on economic factors, in contrast with normative factors to understand compliance models. Checkel suggests the literature is divided into two distinct lines:

“Rationalists emphasize coercion, cost/benefit calculations and material incentives, whereas constructivists emphasize social learning, socialization and social norms” Checkel (2001)

Malloy (2003) describes two visions of firms; one of a rational profit maximisers, obeying laws and regulations, only when it is in the firms best economic interest, and the second where the firm is a law abiding actor who complies in good faith despite struggling with increasingly complicated and contradictory laws and regulation. This view is supported by Gilad (2011) who contends managers analyse “regulation via a prism of costs and gains” whilst appreciating the “commercial and reputational gains that can be extracted from effective compliance systems” (p. 310). Gelemerova (2009, p. 53) comments on compliance with money laundering regulations, and the difficulties in practice of “how to strike a balance between the profit-orientated nature of reporting institutions, the need to keep the financial system clean, and the fear of being punished by regulators”. Malloy (2003) goes on to discuss models of compliance including the deterrence model, and the firm as a rational actor, and the normative model, with the

firm as a good faith actor. The article recognises the limitation of the normative model and states:

“proponents of the normative model pay little attention to the role that compliance costs play in causing violations...if the costs of complying with social norms are greater than the costs of violating, the individual will ignore the norm...even a manager driven primarily by normative concerns, will make compliance decisions by engaging in instrumental decision making akin to that assumed by the deterrence model” (p. 471)

Malloy’s article, therefore, highlights the importance of cost of compliance in consideration of management strategies to compliance. May (2004) presents a similar concept in the form of “affirmative motivations” (good intentions and a sense of obligation to comply) and “negative motivations” (fear of consequences) when reviewing empirical data of compliance with social and environmental regulations. Nielsen and Parker (2012) also build on Malloy’s concepts (in an empirical study focused on business experience of Australian TPA law). Whilst reviewing the theories behind compliance motives they argue that the compliance literature instead identifies three “interests of commitments” which motivate compliance behaviour; Economic (maximising economic utility), Social (earning approval and respect) and Normative (doing the right thing). Nielson and Parker (2012) suggest that each business would be holding a “plural of motives” along this basis.

This develops earlier considerations of “states of compliance culture” summarised as “non-compliance, negative or anti compliance, and positive or pro compliance” (Jenkinson, 1996, p. 42). Whilst links to normative model and culture can be made (in terms of the “law abiding actor”) the complexity of compliance culture is clear. The variables of “values, attitude and behaviour” are cited (Jenkinson, 1996). Compliance culture reflects the individual firm’s approach to regulation (Alfon, 1996, p. 20), and is clearly linked to the strategy and goals of the firms in terms of a positive (best practice) or negative “management of regulatory risk” approach. The complexity of the firm’s structure is also important with choices of ‘top down’ or ‘bottom up’ to consider (Jenkinson, 1996). Morton (2005), comments on the Securities and Exchange Commission (SEC) emphasis on “culture of compliance”. The observation that compliance culture cannot be bought “or taught by a high priced management consultant” (p. 60) confirms the complexity of the concept. In addition the difficulties in measuring compliance culture are also apparent – despite the provision of the culture framework by the SEC, this model clearly failed in the most recent financial crisis.

Compliance competence is inextricably linked to culture and a commitment to partnership with the regulators (Edwards, 2003). Carretta, Farina and Schwizer (2005) contend that language used in documentation can be used to observe and measure cultural implications (whilst referencing Schein's (1985) and DiMaggio's (1997) identification of language as an "artefact" of corporate culture, whereby analysis of text/documentation can yield an understanding of culture). Utilising text analysis they reviewed "culture compliance" within Italian banking sector and identify significant cultural gaps between banks and supervisors, which although pre crisis, also supports the importance of alignment between banks and regulators.

More recently, Kenny (2014) offers qualitative empirical evidence to examine the issue of "dependence corruption" within the financial service sectors. Data is presented to explore the phenomenon of why societal impact, and "rules and regulation were compromised" during the most recent financial crisis. The struggle of compliance officers facing dependence corruption (when dealing with regulator and within their own firms) conflicts with the literature on partnership models with the regulator (Wood, 2002; Jackman, 2001). The dependence corruption and relationship models could be linked via literature on barriers to compliance, for example, the conflicting balance of economic, social and normative aspects discussed by Nielson and Parker (2012).

There is a range of more practical literature on compliance, which provides linear models of minimal, to beyond compliance scales (which echo the linear models set out by Jackman/Edwards and Wolfe). Crump (2007) refers to the concept of "passive and active" compliance approaches. Passive compliance is considered to be auditor driven, reactive to requirements with purpose to seek minimal compliance at minimal expense, with no improvement of conduct of business. Active compliance allows for "business promotion and transparency, and is intervention focussed, enabling companies to remove defects in processes and install automated controls for compliance" (p. 46). Links back to the literature discussed under Section 4.2 regarding responsibilities of the Chief Compliance Officer can be made, whereby essential to active compliance is review of abnormal transactions by an individual "who cares and is held accountable for the conduct of business and the success of transactions" (p. 48). This indicates rather than a tick box process to resourcing compliance, the staffing and attitudes of the compliance function staff outweigh the importance of any model and tools available.

Control Self-Assessment (CSA) techniques are promoted by Carter (2007). Whilst commenting on the increasing costs of compliance, he suggests:



“Costs associated with internal auditing, external auditing, management, staff employees and outside consultants have increased significantly since SOX (Sarbanes-Oxley Act) became law<sup>62</sup>. According to a 2006 study by law firm Foley and Lardner LLP, the costs of being a US listed public company with annual revenue under US \$1 billion increased 174% from fiscal years 2001 to 2005” (p. 70)

Key elements of CSA are; CSA planning, management buy in, auditor buy in, training, testing, and execution of workshops and results evaluation (Carter, 2007). The article concludes “a well-planned carefully implemented CSA programme ultimately helps shape compliance work into an effort that all stakeholders can agree is truly value added” (p. 72).

However, “compliance theorists” have received criticism for the “multiple frameworks and models” offering only partial theory of increasing complexity, with incompatible assumptions due to the multiple motivations for compliance (Etienne, 2011, p. 306). Instead, Lindenberg’s “goal framing” approach was instead proposed to explore compliance based on the three broad categories of: hedonic goal (to feel good); gain goal (to preserve or increase resources); and normative goal (to do the right thing) (Etienne, 2011, p. 311). This ‘goal’ approach bears similarities and consistencies to Malloy’s 2003 deterrence as opposed to normative discussions, May’s 2004, affirmative contrasted with negative discussion, and supports Nielson and Parker’s 2012 economic, social and normative discussion.

An important point for this study is the concept of a ‘lack of attention’ to certain goals, and the ultimate dominance of certain goals (to the detriment of other goals), and thus the resulting impact on compliance. This is linked to the financial service sector during the most recent crisis, whereby the dominance of the ‘gain’ goal for salaries/bonuses outweighed other goals of normative/social acceptance which resulted in non-desirable behaviour of individuals (Etienne, 2011, p. 312). The difficulties in interpreting compliance models and data sets are clear for both academics and practitioners studying financial service compliance. This supports Checkel’s earlier argument that:

“Empirically, can one disentangle compliance driven by persuasion and social learning from that driven by calculating self-interested strategic adaptation or that driven by passive, cognitively simplifying imitation” (Checkel, 2001, p. 566)

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<sup>62</sup> The Sarbanes-Oxley Act was enacted in 2002. See [www.sec.gov/about/laws/soa2002.pdf](http://www.sec.gov/about/laws/soa2002.pdf) (accessed December 2015), and earlier Footnote 8.



One of the main issues, therefore, in both the literature and in practice, is how compliance effectiveness may be measured, and how well compliance officers deal with new regulations when different goals exist. An issue in measuring effectiveness would arise when assessing compliance officers' actions in the cases of sanctions issued by the regulator i.e. the sanction may cost the business less than the act of modifying systems and processes to comply. Difficulties in 'quantifying' communication effectiveness (and to whose benefit) would also be a problem. For example, there would be problems measuring compliance officers' effectiveness in dealing and communicating issues to the regulators i.e. if they communicate effectively this may be to the detriment of the business, but the benefit of wider society. Some academics have attempted to quantify compliance effectiveness which is discussed further in Section 4.3.2.

#### **4.3.2 Measuring compliance effectiveness – empirical studies on compliance approach and tooling<sup>63</sup> in dealing with new regulation**

In instance of good compliance the regulators may adjust their response to the firms they regulate (as discussed in Chapter 3). Parker (2002, p. 241) discusses the issue of "liability incentives" including sentencing incentives, reactive liability, corporate probation and regulatory incentives (i.e. forms of responsive regulation), however, this does not fully reflect how good compliance is measured in the first place.

Edwards and Wolfe (2004) considered that the success of a compliance function can be measured by its ability to minimise or eliminate: a bank's exposure to legal or regulatory sanctions; negative impacts on the banks reputation; and, financial loss; incidences of detection of non-compliance. There are a limited number of other studies attempting to measure compliance effectiveness utilising a range of methodologies.

A case study approach was adopted by Edwards and Wolfe (2007) providing a detailed account of evaluating compliance competence. Template analysis was used within the organisation to demonstrate to regulators and stakeholders that; analysis has been performed, highlight current strengths and weakness, and provide a basis for future development and improvement in compliance competence and ethics within the organisation. The authors adopt the practical internal compliance competence model proposed by Jackman (2001), and the ethical framework for financial services proposed by Wood (2002), as a basis for their template development.

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<sup>63</sup> 'Tooling' is used here in reference to IT software used to enhance compliance within organisations. An example would be to facilitate interrogation of large volumes of data, to highlight anomalies in routine transactions.

A significant element of a compliance officer role will be to embed new regulation. Although, there appears to be limited number of studies in how the compliance function specifically prepare strategies for changes to regulation; the literature does offer some high level studies on the impacts of new regulation on organisations. Hussein and Hussan (2008) commented on the limited number of empirical studies undertaken by academics about the application of BASEL II, which may indicate the difficulty that academics often encounter when trying to collate data on compliance. Demircuc-Kunt and Detragiache (2011) performed a quantitative review of bank Z scores to see if there was an association between compliance with global standards (specifically BASEL Core Principles - BCP) and bank soundness. The authors concluded (with a number of caveats) that there was no support for the hypothesis that better compliance with BCPs resulted in sounder banks as measured by Z score.

A questionnaire based study (restricted geographically to UAE) was performed by Hussein and Hussan (2008). They concluded that UAE banks were ready for the implementation of BASEL II. The findings were supported by the level of capital resources required for implementation for BASEL II, and the importance of training and education on BASEL II. Gebhardt and Novotny-Farkas (2011) statistically reviewed the impact of mandatory IFRS adoption (IAS39 Financial Instruments: Recognition and Measurement) on European banks. They concluded that tighter rulings of IAS39 significantly reduced discretionary behaviour. They also found that the effect of the IFRS ruling was less apparent in stricter supervisory regimes, and in countries with more dispersed ownership of banks (as the principles of the ruling were already being applied in these scenarios). This finding was evidence in cross listed banks, who appeared to have “smoothed their income” to lesser extent prior to the IFRS ruling.

Other studies have focused more on the tooling involved in dealing with new regulation. Mainelli and Yeandle (2006) reviewed the results of a pilot of a specific application (Phophezy, a commercial application of a support vector machine) which was introduced to deal with new regulatory initiatives of MiFID, and utilised an automated process to identify a set of anomalous trades for individual reviews. The authors concluded that the future of risk based compliance may be to develop an acceptable framework process of “sift and investigate”. They called for further (specific) research on SVM/DAPR<sup>64</sup> applications to provide practical approaches to compliance models.

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<sup>64</sup> To clarify SVM represents, support vector programme (statistical and information technology approach) and DAPR represents, dynamic anomaly and pattern response, which are evident in such applications to assist with monitoring.

In depth interviews were performed by Doyle (2007) to investigate tools and methods used to manage compliance, and indicated a general conclusion that respondents were concerned about the lack of systems to proactively manage compliance. This seems to counter results of other academic reviews, whereby results have shown that there has been successful implementation of compliance tools and methodology incorporated within organisations. However, the author did recognise limitation in the research methodology of semi structured interviews, with potential for interviewers attributes to influence respondents replies. The article also reviewed the influence of European Information centres, via survey method, and considered the benefits to be opportunities for the sharing and adoption of best practice (which is considered to link to the literature on shared services). Bamberger (2010) performed a more general review of the use of technology within compliance, and points out the benefits and pitfalls of a reliance on technology. He quoted that in 2008 the total market for governance, risk and compliance software systems and services was estimated at \$52 billion. The article recognises the consultancy angle whereby major players such as Deloitte and IBM have documented studies showing the economies gained by automating risk management controls. However, there is a clear message that traditional methodology, with “reliance on manual controls and stove piped compliance responses cannot keep pace with the increasing complexity of compliance burdens and evolving levels of risk” (p. 685).

It is not clear within the literature to what extent organisations apply the theories of ‘assessing effectiveness’ of compliance in practice, especially when combined with theories proposed regarding organisations’ choice of tools and methodology within the compliance functions. Therefore, this research may bridge this gap within the literature, as the methodological tool chosen of repertory grid (see methodology chapter), will explore practitioners’ views on a range of compliance scenarios from ‘worst compliance experience’, to their views on ‘aspirational compliance’. The constructs explored with practitioners will provide empirical evidence to add to this gap within the literature, and will address objective 2, research question 2a and 2b. This gap in the literature is summarised in Table 6.

Objective 2- To explore the different structures of regulatory compliance in operation

RQ2a What are the key constructs that influence managers’ decisions over the compliance function approach?

RQ2b How do compliance officer's personal constructs align to academic models of compliance?

#### **4.4 Why management comply? Theoretical and empirical Studies**

As can be concluded from the literature review on regulation, there are a number of theoretical approaches to regulation. As such the reaction of an organisation and the compliance officer will ultimately depend on the approach of the regulatory body, in the relevant jurisdiction they are serving. Interactions with stakeholders and regulators are discussed further under Section 4.4.1.

Following earlier discussions (including underpinning theories), of 'why firms comply?' (Section 2.4), the literature exploring the relationships between compliance officers and the regulator, and the firms that they serve will now be studied, alongside considerations of motivations for compliance.

##### **4.4.1 Relationship with regulator and other control functions**

In a review based on the former regulatory regime, Thomas (1997) provides a viewpoint of a compliance officer in their dealings with the regulatory body PIA (Personal Investment Authority). The article discusses the costs of compliance in relation to training and disclosure compliance, and comments that costs have to be balanced against the benefits achieved. The article is critical of the contemporary feedback received from regulators, and concluded that lessons can be learned from both the regulators and the compliance officers: "compliance officers can learn on an on-going basis from the PIA, but equally there are learning points for the PIA from the practices which the compliance officers have put in place in their own companies" (p. 241).

These concepts are developed further in a model based on commitment and partnership (Wood, 2002). Although based specifically on corporate Australia and a means of enabling "inherent ethical" behaviour within organisations, the concept is considered transferable to other domains. The partnership model must be mutually beneficial to all parties and society, otherwise a contest of wills develops between government and corporation which costs society as a whole. The ideas of "tone at the top" are considered, and the observation is made that ethical behaviour should be pursued for "the altruistic desire to be ethical, and not for the mercenary desire to profit from the latest strategic initiative" (Wood, 2002, p. 63). The concept of the model and the interrelationship between compliance, regulator and ethical behaviour is summarised below in Figure 10.

Edwards and Wolfe supported Wood's partnership model and linked this to Jackman's model, whereby the partnership approach should incorporate the development of the organisations values and culture. The approach is considered essential to achieving a viable and meaningful compliance function (Edwards and Wolfe, 2004, Carretta, Farina and Schwizer 2010a).

**Figure 10 Summary of Wood's partnership model (summarised by Edwards and Wolfe, 2004)**



It should also be recognised the importance of the partnership approach to avoid excess compliance requirements, due to the negative correlation of shareholder returns to increasing compliance function costs (Edwards and Wolfe, 2004). Carretta et al. (2010a) provide some empirical evidence to support the concepts of the partnership model in their research (utilising text analysis and development of a cultural survey). They argue in the changing pattern of supervision solutions, with more and more orientated towards self-regulation mechanisms, this determines the need for an increasing degree of cooperation between supervisory authorities and banks. Moreover, they consider that the new relationship models between supervisors and banks need to be supported by organisational tools which enable sharing of information between parties, to promote the advisory function of supervisors.

Case study research is presented by Weaver, 2013 to discuss barriers to compliant behaviour including: perceived incentives to comply (incentives and sanctions, monitoring problems, and enforcement problems); willingness to comply (information and cognition problems, attitude and belief problems and peer effects); and capacity to comply (including resource and autonomy problems). Although this study is not specific to financial service compliance, the concepts presented are transferable. The willingness to comply may be embedded within organisation culture. The capacity to comply may be associated with the cost and benefit arguments for compliance. The link to relationship and partnership with the regulator will be made through incentives to comply and willingness to comply. Recent empirical evidence suggests, however, that

a culture of “dishonesty” within the banking sector in comparison to other industries (Cohn, Fehr and Marechal, 2014) which further complicates the relationship of capacity and willingness to comply.

The relationship and willingness to comply may also be related to the concept of negative media publicity and enforcement action by regulators. This has been linked empirically to positive adjustment to corporate compliance (Yeung, 2002; Zubic and Sims, 2011). Although not directly connected to the compliance function or financial services sector, Fearnly, Hines, McBride and Brandt (2002), reviewed the impact of the Financial Reporting Review Panel (FRRP) on auditors (via interview technique). Analysis of her findings supported the use of legitimacy theory whereby “personal embarrassment, possible career damage and risk of ICAEW disciplinary inquiry” (p. 109) were major sources of concern for audit partners. The similarity in professional standing of auditors and bankers could indicate that these concepts of embarrassment, career damage and disciplinary inquiry will also impact bankers’ relationship and actions of compliance to regulation in the same way. Although the compliance officers may not be subject to ‘discipline’ via a specific compliance professional body (as discussed under Section 4.2), they may be subject to disciplinary/career damage as discussed by Fearnly, Hines, McBride and Brandt (2002) if their background stems from professions such as an accountant, lawyer or police/law enforcement (and they still form part of a membership of a regulated body, for example the ICAEW).

There is also necessity for coordination between the compliance function and other control functions of risk, internal audit and legal (Securities Industry Association, 2005). Within academic literature there appears to be a general consensus that the relationship of compliance function with top management and the board is vital, and the compliance function needs to act independently with clear communication channels to the board. Doyle (2007) through interview techniques concluded that there was a “lack of faith” felt by top management in compliance management within organisations, due to the inability to provide reliable and comprehensive overviews of compliance risks. This was felt to be due to systems lacking capability to pro-actively manage compliance, allowing organisations to deepen and sustain their competitive positioning.

A number of studies have reviewed management approaches to overall governance and compliance with mixed findings. The methodology and findings are varied in this area; however, in general the main conclusions of academics support the theory that improved governance approach by management may result in lower risk ratings for audit, reduced audit fees, and improved financial reporting. Hanson and Stephens

(2009) performed a review of internal auditors' views, via surveys, and concluded that internal auditors are aware of their ability to influence the tone of the organisation, and appear to be working toward improvements of tone at the top. Altamuro and Beatty (2010) concluded that improvements to the internal control monitoring and reporting, led to improvements in the quality of financial reporting in the banking industry. However, internal control regulations results in both direct and indirect costs, and measuring of indirect costs is especially difficult (Altamuro and Beatty, 2010), which supports the view of other academics in their review of compliance cost measurement (discussed under Section 3.5). However, these costs of compliance may also result in offset benefit of reduced audit fees when a company discloses relatively high levels of compliance risk management (Knechels and Willekens, 2006).

#### **4.4.2 Management tone and governance – empirical evidence within the literature**

There has been a general movement by practitioners to improve management tone at the top and governance structures within firms since earlier crisis of Enron, WorldCom, and Arthur Andersen at the start of the millennium. Various academics have reviewed the implementation of effective management governance and control structures and tried to correlate this to firms' valuations to provide evidence for the motivation behind practitioners' actions. Academics often refer to concepts of 'legitimacy' and 'improvements to reputation'. Therefore, the author has explored the literature under the lens of institutional theory (DiMaggio and Powell, 1983), as discussed in Section 2.4.1.

The impact of reputation gains is explored quantitatively by some authors. Hendricks and Singhal (1996) performed event study methodology research to review the impact of quality awards on firms' market values, and found a positive correlation between stock market reactions and announcements of firms winning quality awards. Akhigbe and Martin (2006) also performed a quantitative study to review the valuation effects of implementation of Sarbanes Oxley in financial service industry firms, and found positive benefits to adoption and compliance (with the exception of securities firms). Henry (2008) performed a similar analysis in Australia, using sampling and statistical modelling to review whether a firm's adoption of corporate governance structuring impacted the valuation of firms. The study concluded that voluntary adoption of corporate governance structures was found to "significantly, both in statistical and economic terms, enhance firm valuation outcomes" (p. 938). Adams, Mansi and NishiKawa (2009) provided quantitative evidence linking board characteristics and performance. The study reviewed the relationship between boards of directors and



shareholders through examination of a sample of mutual index funds, using three benchmarks to measure the index fund performance (expense ratio, return differential and alpha). The authors found an inverse relation between board size and fund performance. However, they commented that “there may not be a single optimal structure that is applicable to all funds” (p. 1261). These studies all focussed quantitatively on the impacts of compliance decisions, and ignore how the compliance function has evolved, and reacted to regulatory change over time (Michael, Falzo and Shamdasani, 2015, p. 8).

The concepts of over-complying to gain reputation, has been suggested by a number of authors, although not specific to the compliance domain (Arora and Gangopadhyay, 1995; Oliveria, Rodrigues and Craig, 2011). Companies may include voluntary risk reporting disclosures (RRD) which is evidence of “over complying”, however, public visibility is a crucial factor in promoting legitimacy strategies through RRD (Oliveria et al., 2011). However, Arora and Gangopadhyay (1995), provide a different perspective in their review of the environmental industry regulation and compliance. They considered that “over-meeting” the regulation requirements is intentional and not incidental, and could serve as a signal to policy makers to tighten restrictions for the industry as a whole (thus, influencing policy makers regulatory formation). Shimshack and Ward (2008) also reviewed relationship of the environmental industry regulation and over compliance, with an alternative focus on enforcement. They concluded that credible enforcement significantly increases statutory over-compliance with regulation, noting that enforcement not only improves behaviour of non-compliant plants, but also provokes typically over-compliant plants to reduce discharges further below permitted levels. This literature has been written from the perspective of other sectors (environmental industry). Although this literature base offers concepts around motivations for compliance or over compliance (and reporting thereon), the incentives for regulatory compliance within these industries will be different to those within the financial sector.

There are some alternative views on management approaches to governance within the literature. Kempf Jr (2008) comments that management push forward with “proposals advance in the name of good corporate governance” (p. 130) without reviewing whether the proposals are really sound. The article provides some specific examples and criticises academic review stating “because the results of these studies don’t fit with the views of the players, they have been ignored by them” (p. 118). The article is not criticising the principles of good governance, but rather suggesting that

management and academic take a step back and consider the effectiveness of certain governance techniques and strategies. Others have related governance more generally as a “bundle of practice” (Filatotchev and Nakajima, 2010, p. 598), arguing that best practice should be viewed in terms of “combination of practices rather than as individual good corporate governance drivers”.

In addition the image of good governance is often misleading (Laufer, 2006). In a study employing a method of policy analysis on regulatory reforms Laufer commented that despite “images of firms committed to doing the right thing in spite of lost profits, and choosing the path of compliance for reasons of integrity, not risk management, conveys a strong message of ethical self-regulation” (p. 246), that these images are “all too often illusionary”. Laufer also comments on the difficulties in assessing the actual effect of corporate compliance programmes on firm behaviour, and how this “adds to the sceptics and pessimists account”. These concepts are supported by Carretta, Farina and Schwizer (2010b), in their literature review of the roles and effectiveness of boards and directors. Their review included consideration of directors’ self-evaluation, with the advantage of devoting time to looking at “routines of behaviour” which they do not normally stop to examine. The argument against self-evaluation, and internal assessment was stated in the lack of transparency and capability. They concluded that a “one size fits all” approach to board evaluation does not apply, and so it is necessary to establish adaptable assessment procedures.

This view on self-evaluation is not supported by Nijhof, Cludts, Fisscher and Laan (2003). They reviewed the implementation of code of conduct within four case studies, utilising an assessment method based on EFQM (European Foundation of Quality Management) model, intended to support the implementation (with the review more focussed on the implementation process rather than the outcome of the code implementation). The research involved management self-evaluation of the process, and the different participants in the research project concluded that following the process approach provided, the indicators formed a “coherent and comprehensive set to measure to what extent a code of conduct is embedded within a company” (p. 76).

#### ***4.4.2.1 Managements’ moral and value development***

Moral development was first defined by Piaget, and then further refined by Kohlberg, and represents the “transformations” which occur in an individual’s structure of thought (Kohlberg and Hersch, 1977). In a review of the theory (and application to practice of teaching) Kohlberg stated:

“other variables come into play such as emotion, and a general sense of will, purpose of ego strength. Moral judgement is the only distinctive moral factor in moral behaviour, but not the only factor in such behaviour...” (p. 58)

Although there were no studies found which related specifically to financial service compliance and Kohlberg’s moral development<sup>65</sup>, it is considered that the concepts introduced in other (non-compliance specific) studies may be transferable to the compliance domain. In terms of methodology development, Weber (1991) adapted Kohlberg’s moral judgement interview and scoring, and applied this to a study of managers’ moral reasoning. The purpose of Weber’s study was to enable future researchers to apply an adapted methodology to measure and understand moral reasoning within management decision making processes.

Abdolmohammadi and Baker (2006) reviewed the relationships between accountants’ personal values and moral reasoning. In this study the authors introduced the theory developed by Rokeach (the influence of values on behaviour) and linked this to moral reasoning. The study combined the methodology of the ‘Rokeach Value Survey’ (RVS) and the popular instrument to measure moral development of ‘Defining Issues Test’ (DIT). Given the professional status of many compliance officers (and thus similarity to accountants in this study) this methodology is considered transferable to compliance literature. Myyry et al. (2009) again integrated moral reasoning and values within their study, but used an alternative motivational type of value model proposed by Schwartz (1992). This study reviewed the association between moral reasoning and compliance/adherence to information security policies.

Combining a number of ethics related theories (i.e. Kohlberg/Rest/Trevino), and empirical data from interviews with compliance professionals, Barraquier (2011) proposes a conceptual model to explore levels of compliance contrasted against perceived profitability of business transaction. The proposed model considered the strategic implications of compliance decision making, and contends that all organisation will operate in each of the four quadrants in the model (see Figure 11).

Although this model is based on empirical data from the fragrance and flavouring sector, it may be considered in other compliance settings. However, this model has received only a limited number of citations to date<sup>66</sup>. When considered in relation to financial services one may consider the most recent financial crisis. Under correlation

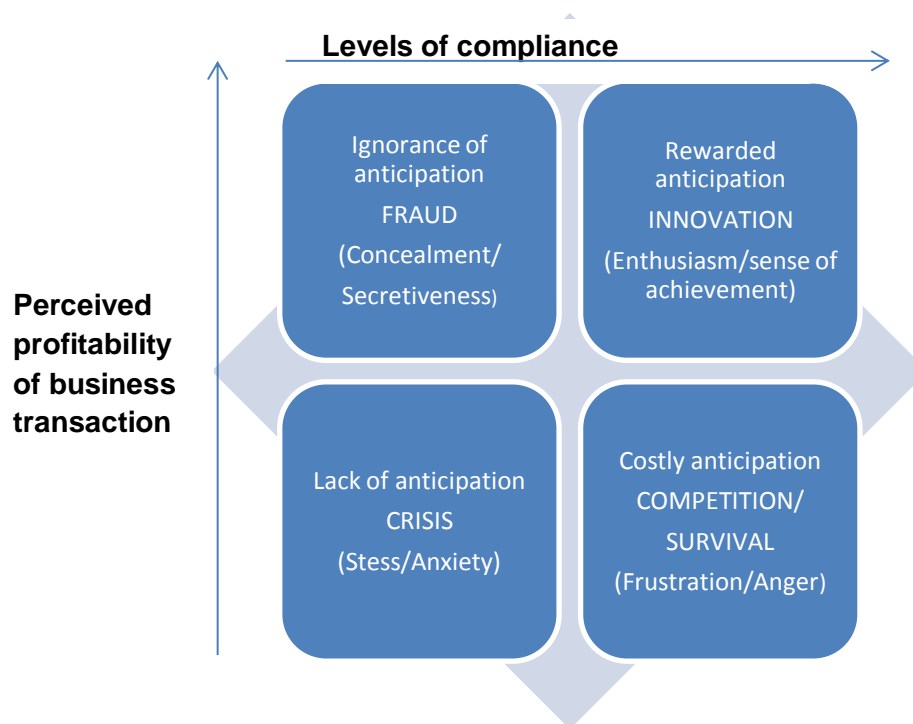
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<sup>65</sup> Using search terms “financial service compliance” and “Kohlberg” yielded no results in Google Scholar.

<sup>66</sup> As an example Google Scholar, indicates only 24 citations at November 2014.

within this model, instances of behaviour where levels of compliance may have been consider low, and perceived profitability were high, this would fall under the fraud quadrant. Compliance professionals in the financial service sector may not appreciate this categorisation; however, the model does attempt to correlate managers' behaviour and decision making, compared to competitive environment (Barraquier, 2011). The relation to ethics in this model echoes earlier models discussed under Section 4.3. Acknowledgement is made that compliance decision making is made across the entire grid.

**Figure 11 A model of ethical behaviour, decision outcomes and associated emotions (Barraquier, 2011, p. 39)**



The context of Barraquier's model to this study is revisited in Section 8.1.1., where there is further discussion of the opposing behavioural motivations of profitability, as opposed to compliant behaviour (given the high profitability of the sector, compared to fines issued by the regulator).

#### 4.5 Chapter summary

The compliance literature is often written from a practical perspective, although there are clear links made to underpinning theories in terms of motivations to comply. As evidenced in the review of the regulatory literature there is limited recent empirical evidence in place to support models of compliance. Given the restricted number of studies, and lack of empirical data focussed on compliance this may indicate issues

obtaining access<sup>67</sup> to compliance professionals for this type of empirical research. There is significant correlation to ethics and culture presented in the literature (albeit in a rather abstract way, which has been criticised by Meidinger (1987), from a regulatory perspective).

In the preceding chapters, the regulatory literature and the compliance literature domains have been explored in order to review questions around what compliance officers are complying with, and how, and why compliance officers may achieve regulatory compliance. The next chapter explores the literature which offers potential alternatives to the traditional in house compliance functions (in order to add to the how to comply discussions).

Further discussion of the specific gaps, and links to the research objectives and questions is presented in Section 5.4. A summary of the compliance literature gap is presented in Table 6.

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<sup>67</sup> Pérezts and Picard, 2014 comment on difficulties obtaining access with ‘months of negotiation and exploitation of interpersonal networks to succeed’. This has also been a difficulty in this study as discussed in Section 6.4.6 and Section 6.5.1.

**Table 6 Summary of compliance literature review and associated gap, with link to research objective and research question**

| Literature review        | Section discussed  | Authors calls/criticisms  | Remaining gap   | Research objective  | Research question/Potential future RQ  |
|--------------------------|--|---|---|---|--|
| <b>Compliance roles</b>  | Section 4.2 Qualified officers and the responsibilities of the chief compliance officers | Roles and responsibilities/modern compliance officers/risk managers/legal counsel (Taylor, 2005; Stoneman, 2005; Gable 2005; Langevoort, 2012). | Limited empirical research.   | Outside the research objectives of this thesis.   | Future RQ: What are the educational and career attributes of financial service chief compliance/risk managers? (Future research as ultimately cannot be answered in timeframe/methodology chosen). |
| <b>Compliance models</b> | Section 4.3.1 Compliance models, Section 4.3.2 Measuring compliance effectiveness        | Jackman's value and culture model, passive as opposed to active compliance, cosmetic compliance.  | Limited empirical research on measuring effectiveness/benefits of one approach above another. | Objective 2: To explore the different structures of regulatory compliance in operation. | RQ 2b: How do compliance officers' personal constructs align to academic models of compliance?   |

## Chapter 5 Literature review – The alternatives: consulting, outsourcing and shared services

“You can't delegate the responsibility for compliance to another party, but you can get help to ensure your controls are appropriate” FCA<sup>68</sup>

### 5.0 Compliance relationship with consultants

The purpose of this short chapter is to explore the alternative ways in which the firms, and the compliance officers may choose to achieve regulatory compliance. The chapter has been split into four main sections. The first section discusses the literature around relationships with consultants, and how compliance officers deal with new regulation. The second section looks at the concept of shared services. In the third section outsourcing is considered. In the final section the outcome of the literature review is summarised (including the review of the regulation, and compliance literature in Chapters 3 and 4).

Based on the commercial and academic literature available on compliance tooling<sup>69</sup> it can be deduced that the market for compliance consultancy is very lucrative. Arnold (2009) highlights the “thriving” consultancy trade in the major accountancy firms (despite the restrictions of SOX and the independence rules), and this is seen by the author to be an area for future empirical research.

One could question the over reliance on consultants by organisations, and whether consultants feed off regulatory and compliance uncertainty, given recent events in the financial crisis. Gable (2005) comments on the fact that certain white papers and presentations are produced by those with a vested interest in selling compliance related products and services. This concern is echoed in an online press article following the governance scandals by Gullapalli (2005). This looked specifically at the auditing profession and the data available on the increase in audit fees and other services, following the collapse of WorldCom Inc., Enron Corp., and Arthur Andersen. Whilst commenting on the “avalanche of work” generated by the Sarbanes Oxley corporate governance bill it was noted that “there is no shortage of work for the accounting profession as it tries to fix a tarnished reputation” (p. 1). Krawiec (2005)

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<sup>68</sup> Extract from the FCA website <http://www.fca.org.uk/firms/being-regulated/meeting-your-obligations/using-external-support/compliance-consultants>, accessed July 2015.

<sup>69</sup> In the context that a large professional literature base exists (in the form of magazine articles and webpages) devoted to discussions of compliance processes, and IT software as tooling, to enhance compliance within organisations.



also comments on the rent seeking<sup>70</sup> behaviour of some professionals in relation to regulation setting, and consulting thereon. The benefits to be gained, both financially and through improved status and reputation, are seen to be enormous.

The motives of individuals procuring such services are also to be explored. It may be queried whether such services are procured to transfer accountability, or whether it is simply an issue of resourcing effectively within organisations. Michael, Falzon and Shamdasani (2015) model the way in which consultants improve a financial firm's profitability, and comment on how "few economists have studied this segment of the larger market for professional services" (p. 4). However, this quantitative paper is driven from an econometric literature base which does not fully explore individual decision making within organisations.

### 5.1 Compliance function strategies to deal with new regulations

On review of literature there does not seem to be any recent empirical research in the area of use of consultants (specific to financial services)<sup>71</sup>, and so this is seen as area where this research project can contribute to knowledge.

At the inception of this research project in 2012, Alkan (2012) discussed the implications of FATCA (Foreign Account Tax Compliance Act) in *Economia*<sup>72</sup>. The article indicated that many companies were hiring accounting and law firms to help ensure compliance with FATCA, due to "weariness" of implementing new regulations. Via website review, it was found that each of the Big 4 accounting firms had dedicated pages for FATCA (along with a plethora of other consulting firms). This phenomenon of consulting firms advertising their products and services to deal with emerging regulation is not new. The interest in this specific piece of legislation continued within the media<sup>73</sup>. Therefore, the literature review on consulting followed this specific piece of legislation, as an illustration of new regulation that is under development at the same time as this thesis is completed.

Due to the ongoing development of the intergovernmental approach for FATCA, the value of the contributions that consultants can offer to compliance officers is subject to

<sup>70</sup> See earlier definition as per Krueger (1974) in Section 3.3, whereby, rent seeking relates to the investment of resources in attempts to divert income from other people through the political and regulatory process.

<sup>71</sup> Google Scholar search March 2015 revealed 12 hits under search terms "compliance consultant" and "financial service".

<sup>72</sup> A publication issued by Institute of Chartered Accountants of England and Wales for its members.

<sup>73</sup> Ongoing interest in this piece of legislation has been demonstrated in *Economia*, for example 2012 <http://economia.icaew.com/technical-update/tax/fatca-attack>, and 2014 <http://economia.icaew.com/news/november-2014/fatca-costs-on-the-rise> accessed December 2014.

question. Therefore, the topic of how compliance officers intend to deal with the requirements of FATCA, including their relationship with consultants is seen to be an interesting area to focus the research project, with respect to RQ 3.

There appears to be limited academic literature in relation to the topic of FATCA, which may be due to the ongoing implementation of the legislation. However, this appears to be a controversial item of legislation in practice, given the continued media scrutiny. An earlier article by Dizdarevic (2011) highlighted how FATCA reporting and withholding provisions depart from the norm of using withholding as a tax enforcement mechanism, and instead use it as a coercive compliance measure. The tax withheld is not for the purpose of securing payment of the taxpayer's liability, but rather a penalty for failing to report. The issue of fairness was also highlighted in this article, due to the allocation of burdens, whereby FATCA imposes a great burden on foreign financial institutions (FFIs) who do not necessarily assist the tax payer from evading US tax. Whilst acknowledging that there are "few carrots, mostly sticks" in the FATCA regulation, Dhanawade (2014) argues that it is unfair to discuss the flaws in the legislation without "crediting the law for its innovative push towards increased transparency in international tax reporting and information exchange" (p. 157).

Wise and Baker (2012) reviewed the proposed regulation, and discussed the intergovernmental framework, in which they raised the question of how FFIs should be proceeding to prepare for FATCA:

"Should they ignore FATCA and wait for the intergovernmental agreement with their home country? Or should they be ready to comply with FATCA in case the framework falls apart?" (p. 38)

There seems to be a high level of criticism of FATCA, within the limited literature which is available (Dizdarevic, 2011; Wise and Baker, 2012; Morse, 2012; Brodska, 2013). Morse (2012) contends that the introduction of FATCA "cannot solve the problem of US taxpayers' offshore accounts without the cooperation of non US governments" (p. 529). The difficulties in enforcement are also highlighted whereby local audit firms will be allocated responsibility for ensuring that FATCA requirements are met – but of course the US does not generally exercise any control over these agents. In conclusion, the authors indicates that the US administrators of FATCA may be required to use "tactics based on simplicity, reciprocity and side payments" to encourage support for FATCA by non US governments (Morse, 2012, p. 550). Brodska (2013) highlights that the main criticisms around the legislation revolve around costs, and implications on existing data

protection legislation in certain jurisdictions. Behrens (2013) also adds to the criticism of FATCA stating “the cost of compliance imposed on private parties simply outweighs the benefits” (p. 217). The author contends that the predicted revenues of FATCA at \$800 million annually, are dwarfed by the estimated costs of approximately \$5-10 million per FFI, which amounts to \$1-2 trillion globally (p. 223). The three choices proposed for FFI are: firstly, to disclose required information to the IRS (or follow intergovernmental reporting requirements); secondly, to impose the thirty per cent withholding tax related to US/non US payments; or thirdly, to completely avoid US investments and client (p. 208).

Snyder (2015), comments on the wider effort of the US “crackdown on tax evasion”. In cases of non-cooperation/compliance, there has been successful prosecution. Snyder (2015) presents the high profile case of the US Department of Justice against Credit Suisse, in which Credit Suisse submitted a guilty plea, resulting in a settlement of approximately \$2.6 billion. However, Snyder (2015) also argues that some institutions<sup>74</sup>, who had previously cooperated with legislation, are adopting a more confrontational stance and withdrawing, indicating:

“withdrawing FFIs may have concluded that there was no tax violation to disclose, or that the enormous costs of investigation and disclosure simply outweigh the risks of prosecution” (Snyder, 2015, p. 603)

This may suggest that financial institutions consider that costs of compliance exceed the benefits of compliance, and the threats of prosecution are viewed as a business risk, or cost to the business operations.

As indicated in the discussions above, there were unanswered questions for compliance officers when approaching the legislation (specifically echoing Wise and Baker, 2012). Compliance officers were encouraged by commercial and consultant based literature to drive forward to comply with FATCA. However, a large amount of uncertainty remained on the direction of FATCA in the UK due to the intergovernmental approach. This problem could be linked into objective 2 and objective 3/research questions 2a and 3 to review how managers should approach new regulation, which models and strategies to adopt, and whether use of consultants is inevitable. This gap in the literature is highlighted and linked to the objectives in Table 7.

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<sup>74</sup> This study was focussed on Swiss based entities.

Objective 3 - To investigate the circumstances under which different approaches to compliance would be adopted.

RQ3 In cases of new regulation, how do compliance functions rely on external expertise (consultants) or is there proactive promotion of in house knowledge and expertise?

## 5.2 Use of shared service arrangements

There also appears to be limited academic literature linking financial services to shared service arrangements. Of the shared service literature that is available, many of the authors focus on the 'motives and drivers' of shared service or outsourcing arrangement, rather than providing empirical evidence, or insights into how management can actually implement and manage the arrangement in their organisation (McIvor, McCracken and McHugh; 2011). For example Marshall (2001) discussed the Bank of America shared service arrangement with Exult, with a focus on the motivating factors of "cutting costs", and making "technology spending more efficient", and, reduction in headcount.

Previous studies have involved review of other administrative functions such as finance, and human resources. In addition, the methodology employed has generally been of a qualitative nature, with many academics choosing to study via case study of specific organisations and functions (Herbert and Seal, 2012; McIvor et al., 2011). Lindvall (2011) followed the case of Ericsson's transformation of their decentralised global finance and accounting function to a global network of shared service centres. Recent studies have also focussed on the concept of "offshoring" (outsourcing outside UK) (Evans, 2005; Clark and Monk, 2013), and an alternative concept (mainly used relation to global IT outsourcing industry) of "knowledge process outsourcing" (Currie, Mitchell and Abanishe, 2008).

The traditional head office and shared service approach is compared by Herbert and Seal (2009). The article briefly discusses the corporate restructuring phases of centralisation (1950 to mid-1980s), decentralisation (1980 to end of 1990s) and shared service centres (SSCs - mid 1980s to end of last century). They comment that for SSCs to be successful and add value to an organisation management should not view them as "back door centralisation or a milestone on the road to outsourcing" (p. 46).

**Figure 12 Comparison of traditional head office and shared service centre (SSC) summarised from Herbert and Seal (2009, p. 45)**

|  | Traditional Head Office          | Shared Service Centre  |
|--|----------------------------------|--|
| Output Focus                                   | Self-serving<br>(top management) | Customer centred<br>(business divisions)                         |
| Input Focus                                    | Functional<br>(role focused)     | Process centred<br>(centres of excellence)                       |
| Location                                       | Within HO                        | Physically remote<br>(separate site)                             |
| Governance                                     | Hierarchical                     | Arm's length<br>(quasi market)                                   |
| Objectives                                     | Coordination and control         | Process efficiency<br>Divisional focus on core activities        |
| Cost recharge                                  | Central cost apportionment       | Units charged per activity/output or traceable captive resources |
| Information Technology/<br>Information Systems | Main focus consolidation         | Enterprise wide (ERP),<br>Standardisation of processes           |

Schulz and Brenner (2010) perform a literature review to try to determine a common understanding of the basic terms and definitions of “shared service centres” used by authors. They provide a useful insight on the background of the authors which they reviewed during their study of shared service literature. They comment that earlier papers were written by authors with a professional background, however, in more recent years there has been increased interest in the topic of shared service centres by “scientist/academics”.

Whilst recognising that definitions vary across the literature, Ulbrich (2006) contended that there was common idea that shared services are a “way of optimising corporate resources and processes in a new organisational entity” (p. 196). The author summarised the goals of shared service as:

- “cost reduction through providing services to a diverse set of business units;
- An accumulation of intellectual and capital assets;
- A centre of excellence providing services with customer and process focus; and
- A place to deploy new technology” (p. 200)

Problems usually encountered when implementing shared services are recognised as “business relations, interfaces and location” (Ulbrich, 2006). The author, whilst recognising the limitation of the research, recommended complementary research utilising in depth case studies. Lindvall (2011, p. 286) supports the Ulbrich’s argument of these goals, through their case study of Ericsson commenting on vision of global shared service organisation around the “four C’s”; Cost, Control, Consistency and Competency.

Contributing to calls for “case led” research into shared services, Herbert and Seal (2012) performed a qualitative case study on shared service organisations (SSO). Consultants claim that SSO can reduce costs and improve service quality, and this research investigated these claims from a management accounting perspective. They called for further research on the SSO model, to survey the views of internal customers of the SSO model. They also called for research on the implications of the SSO model in terms of threats and opportunity for individual accountants and their professional bodies. This could be viewed as an avenue for new research in relation to the compliance function in financial service institutions. Mclvor et al. (2011) also review the concept of outsourcing (from the perspective of the public sector) via a longitudinal case study methodology. During the course of a 3 year review they performed semi structured interviews, and commented that the strength of this approach was the ability to “triangulate data from multiple informants” (p. 451) to analyse the key lessons from the outsourcing experience.

However, other methodologies have also contributed to the shared services/outsourcing literature. Spekle, Van Elton and Kruis (2007) modify an earlier study using transaction cost economics by Widener and Selto (1999), to review why firms outsource internal audit activities. The authors found their modified study in the Netherlands were supportive of the earlier study by Widener and Selto (which was based in the US). The findings indicated that asset specificity and frequency were strongly linked to sourcing decisions. The transferability of the questionnaire design between regions may also indicate a possibility of methodological transfer to other function sourcing decisions such as compliance. Lindvall (2011) although not referencing to “transaction cost economics”, makes the same links to the advantages of efficiencies of shared service function over transactional work which is “standardised, less complex, and consisting of frequent work with high volumes” (Lindvall, 2011, p. 282).

### 5.3 Outsourcing<sup>75</sup> within financial services

The former UK regulator, the FSA provided some guidance on outsourcing of compliance, and maintained links with the Association of Professional Compliance Consultants. An important message was that whilst it may be appropriate for firms to outsource compliance they stress that firms “cannot outsource that responsibility” (FSA, 2008, p. 13). The regulator acknowledged working with organisations responsible for compliance consultancy, but clearly stated that “we do not regulate them and it would not be appropriate for us to list or approve firms we don’t regulate” (p. 13).

Specific to financial service sector, Evans (2005) provides a practical guide to outsourcing in the context of MiFID and the contemporary guidance from the UK’s regulator. This article was focussed heavily towards the practitioner, discussing compliance with regulation, rather than development of academic theory. Musile Tanzi, Gabbi, Previati and Schwizer (2013) also review the compliance function following MiFID, and provide empirical evidence including: the positioning of the compliance function; the roles attributed; the methodologies applied within the function; and the interaction with the rest of the organisation (p. 51). However, Musile et al. (2013) study does not address the gap/link to outsourcing/shared services literature.

An earlier case study highlighted the “mixed results” achieved by outsourcing, highlighting the importance of performance management monitoring (McIvor, Humphreys, McKittrick and Wall, 2009). The authors contend that organisations often assume that using external service providers will result in lower costs, at higher performance levels than internal functions (McIvor et al., 2009, p. 1027). Measures are often set concentrating on cost, whilst ignoring the importance of other dimensions such as “quality, flexibility and service” (McIvor et al., 2009, p. 1027). This importance of cost factors relates to Coase<sup>76</sup>’s theory of the firm (in sourcing, as opposed to outsourcing and ‘make or buy’) and is discussed in depth in a more recent study by Clark and Monk (2013), with direct reference to financial service firms. The issue in financial service firms is the embodiment of assets is largely the knowledge, talents and expertise of employees (Clark and Monk, 2013, p. 283). Thus, by outsourcing of such talent, the firm’s assets are depleted. The relationship of offshoring, and the

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<sup>75</sup> Guidance on outsourcing is provided in SYSC8 of the FCA handbook, available at <https://www.handbook.fca.org.uk/handbook/SYSC/8/> accessed December 2015.

<sup>76</sup> Also discussed earlier in Section 3.3.2 with reference to self-regulation, whereby, firms would be organised to produce goods and services when internal production was cheaper than external market transactions.



“global hierarchy of financial centres”, is also considered to be intrinsically linked (Clark and Monk, 2013, p. 295). Currie et al. (2008) contend that the option of knowledge process outsourcing (KPO) is attractive to firms who “do not possess all the capabilities and skills in house”, with the KPO industry reliant on the “demand for business intelligence and expertise” (pp. 94-96). This results in organisations potentially paying premium wages in order to capture the services and intellectual decision making of the highly skilled workforce offered by these service providers. However, understanding “current performance and the degree to which sustainable superior performance in a process can be maintained” is necessary in order to align the outsourcing process (and decision) to the overall organisation strategy (McIvor et. al, 2009, p. 1045).

It should also be considered at this point that Rossi (2010) concluded that “the compliance function should ideally not be decentralised, at least on initial inception” (p. 826). In earlier literature, Haynes (2005, p. 160) expressed no preference for centralised/decentralised as long as the “responsibilities of the compliance function are clearly defined” and it is “independent”. No empirical evidence has been provided to date (as far as this author is aware) to analyse the advantages or disadvantages of shared services for financial service compliance. Therefore, one could question whether the theory of centralisation of compliance proposed by Rossi, and the counter findings of Herbert and Seal regarding shared service organisation could be combined and developed for further in academic review of the compliance function. This can be linked to objective 3/research question 3. This gap is highlighted in Table 7.

Objective 3 - To investigate the circumstances under which different approaches would be adopted

RQ3 In cases of new regulation, how do compliance functions rely on external expertise (consultants) or is there proactive promotion of in house knowledge and expertise?

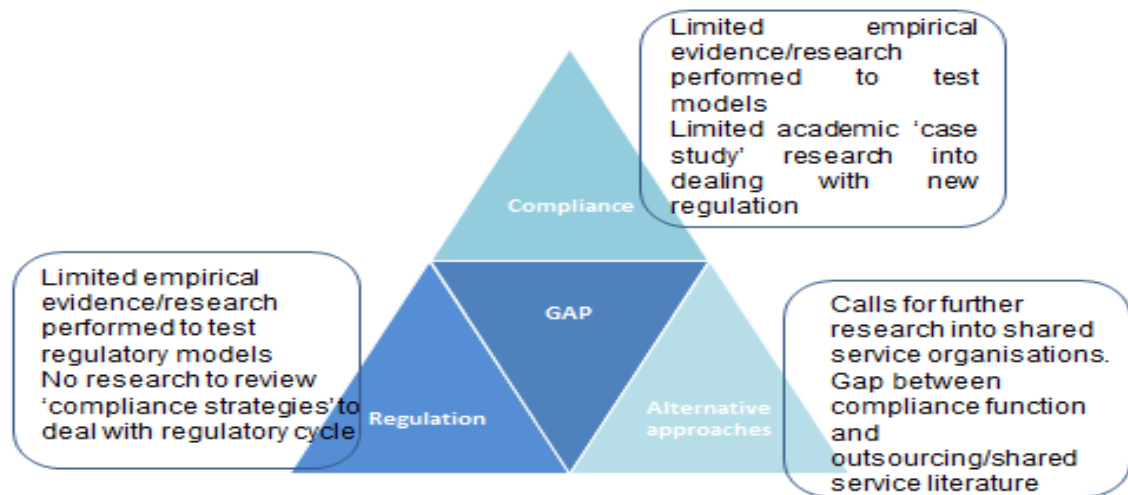
#### **5.4 Summary of overall literature review - gap analysis**

Under each area of the literature review (regulation, compliance and shared services), links have been made to the research objective and research questions, within the narrative (see Table 5, Table 6 and Table 7). This section summarises the identified gaps and the link to the research objective and research question in tabular format.

The main gap is considered to be the lack of recent empirical evidence within the compliance literature. This seems indicative of wider issues of engaging with financial service compliance professionals, given the resulting access issues that have been

encountered during the course of this thesis. Figure 13 summarises the information presented by each literature area in Table 5, Table 6, and Table 7, to indicate the gap between the streams of literature studied in this review.

**Figure 13 Theoretical positioning within literature, and research gap/overlap**



Chapter 6, which follows, sets out the approach to data collection to meet these gaps and to answer the specific research questions. However, it must be noted alongside the specific research questions that are set out in Table 5, Table 6 and Table 7 respectively, that there were overarching themes of discussion with participants during interview (as a result of the literature reviews). These are referred to further in Chapter 6 (specifically Section 6.2) and are summarised below:

- What are the effects of changing regulation? (this question theme stems from the literature review in Chapter 3 and 4)
- When/How are consultants used? (stems from literature review in Chapter 5)
- When/How are outsourcing/shared service options considered? (stems from the literature review in Chapter 5)

Following data collection, the literature is revisited and triangulated to the findings of this study in Chapter 8.

**Table 7 Summary of alternatives literature and associated gap, with link to research objective and research question**

| Literature review                | Section discussed  | Authors calls/criticisms  | Remaining gap  | Research objective   | Research question/Potential future RQ  |
|----------------------------------|--|---|--|--|--|
| <b>Compliance/new regulation</b> | Section 5.1 Compliance function strategies to deal with new regulation | FATCA (Dizdarevic, 2011; Wise and Baker, 2012)  | Limited academic case study of practitioners' strategies to deal with new regulation   | Objective 2: To explore the different structures of regulatory compliance in operation<br>Objective 3: To investigate the circumstance under which different approaches would be adopted | RQ 2a: What are the key constructs that influence manager's decision over the compliance function approach?<br>RQ 3: In cases of new regulation, how do compliance functions rely on external expertise (consultants) or is there proactive promotion of in house knowledge and expertise? |
| <b>Shared service</b>            | Section 5.2/5.3  | Motives and drivers of shared services/outsourcing (Marshall, 2001; Herbert and Seal, 2009; Ulbrich, 2010; Mclvor et al., 2011; Schulz and Brenner, 2010; Lindvall, 2011; Clark and Monk, 2013): transaction cost economics (Widener and Selto, 1999; Spekle et al., 2007): case study research (Mclvor et al., 2009) | Calls for further research on Shared service organisations (SSO) (Herbert and Seal, 2012)<br>Gap between the compliance function and the outsourcing/shared service literature | Objective 3: To investigate the circumstances under which different approaches would be adopted  | RQ3: In case of new regulation how do compliance functions rely on external expertise (consultants) or is there proactive promotion of in house knowledge and expertise?   |

## Chapter 6 Methodology

“Choice of method is not a stand-alone decision reached at an early stage in the research process but evolves as a project unfolds, as the researcher’s understanding of the issues and also of the organizational research setting develops.” (Buchanan and Bryman, 2007, p. 496)

### 6.0 Introduction

The purpose of this chapter is to explain the development of the research design around the research objectives. Epistemological and ontological considerations are discussed in Section 6.1. This leads to the second discussion, where the adoption of repertory grid and ethical considerations are summarised (Section 6.2 to Section 6.3). A technical discussion of use of repertory grid technique is then presented (Sections 6.4 to Section 6.6). These sections detail the adaptation of research method design from pilot stages through to final data collection, reflections on the data collection, and finally the analysis of data. In Section 6.7, reflections on the limitations of the methodology are made, with discussion of problems encountered (and resolved) during the course of the thesis.

Systematically, the methodology chapter addresses the overall aim of this thesis which is to explore whether it is possible to identify a best practice model of compliance within the banking sector (given ongoing changes to regulatory design). The development of research objectives and questions to address this overall aim, are detailed within Table 8.

### 6.1 Philosophical considerations and research design - The author’s personal ontological and epistemological orientation

“The field [Organisational Research] is fragmented, with no central core of traditions, frameworks and concepts, no unified theoretical or practical proposal” (Buchanan, and Bryman, 2007, p. 487)

A personal affinity toward general science and mathematical topics in earlier academic studies, led to initial considerations of positivist research design. However, the focus of research questions around decision making in compliance approaches, aligns with the concepts of inductive research and constructed knowledge embedded within humans. Humans learn, and develop (construct knowledge) through experience so this directly impacts on their strategic approach for compliance to regulation. Therefore, a pragmatic approach has been adopted. Specifically, this thesis is centred on the fundamental concept of constructive alternativism underpinning Personal Construct

Theory (Kelly, 1955), utilising the methodological tool Repertory Grid. Personal construct theory, and the repertory grid technique originates from the field of psychology, and is discussed in depth in Section 6.4

A crucial part of development as a researcher is the ability to defend the terms of analysis and justify the steps taken “to a sceptical friend or questioning colleague” (Krippendorff, 2004, p. xxi). This scepticism towards the research methodology has been experienced whilst at conferences and research seminars. In certain cases, advice/feedback received involved simply “setting up a huge questionnaire, and mail off to a list of compliance officers”<sup>77</sup>. However, it was considered that this method would not provide the depth of data required to meet the objectives of understanding and exploring compliance officers’ selection of compliance approaches<sup>78</sup>. The discussion, which follows in Section 6.2 through to Section 6.4, will justify the chosen method of repertory grid, to gain insight on the tacit knowledge of participants, in order to meet the research aim and objectives.

Kelly (1963) indicates that constructive alternativism does not fit in either the objectivism or constructionism domains. Due to the emphasis on ‘testing’ of constructs, links to positivism/objectivism are apparent. However, the reliance on man’s approach to the world through construing falls back to links with “rationalistic thought”, and through the ability to construct “alternative approaches to reality” which then conflicts with traditional realism (Kelly, 1963, p. 17). This has been translated within this thesis as man learning on a continuous basis, and adapting their approach, through interpretation of individual experiences (under a pragmatic logic).

McWilliams (2004, p. 291) succinctly describes his own draw to Kelly’s philosophy as “coming home to a well-articulated perspective” which aligns to a uniformed way of thinking about human interaction. McWilliams (2004) discussed the concept of “accumulative fragmentation” with knowledge progression through additional “pieces of truth to the puzzle”; whereby, once we verify our conclusions there is “no point” in further exploration of the truth. This is in direct contrast to Kelly’s concept of constructive alternativism, which contends knowledge/truths are invented from alternate interpretations of the same events. Under constructive alternativism, we also revise and replace our knowledge in light of future interpretation of events – and hence there is no final truth. This strongly correlates to the chosen research topic of

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<sup>77</sup> Comment from a session chair at the BAFA Doctoral Conference 2013.

<sup>78</sup> In terms of choices to adopt strict adherence to letter of the law, or more ethical approaches. See Section 4.3 for discussion of compliance approaches.

compliance, given the current flux within the regulatory framework within financial service.

Constructive alternativism strives for individuals to “take personal responsibility for creating meaning” (McWilliams, 2004 p. 291). This philosophy links seamlessly into a personal desire for contribution to practitioners’ knowledge creation, where there is a constant ambition using buzzwords to ‘improve, become more efficient, transfer knowledge and expertise’.

As discussed within the Introduction, Chapter 1, this is a complex topic which has been scrutinised in depth<sup>79</sup> by academics and practitioners alike, and ‘an answer’ may not exist to rectify the problem. Crisis research, or studies of “extreme events” (Buchanan and Denyer, 2013) often involves the application of case study design. Within the literature review, there has been a variety of “authoritative accounts” produced with the aim of silencing alternative and critical perspectives of crises (Buchanan and Denyer, 2013). Therefore, this research has been designed to enable a new data set (from the compliance officers’ viewpoint) to be explored to contribute to academic theory (see Section 6.6 for analysis of grid/interview data).

A summary of the ontological and epistemological underpinnings, and how they have been defined and applied in this thesis, is summarised in Figure 14.

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<sup>79</sup> The literature has been covered in depth from a regulator’s viewpoint, but less so from a compliance officer’s perspective.

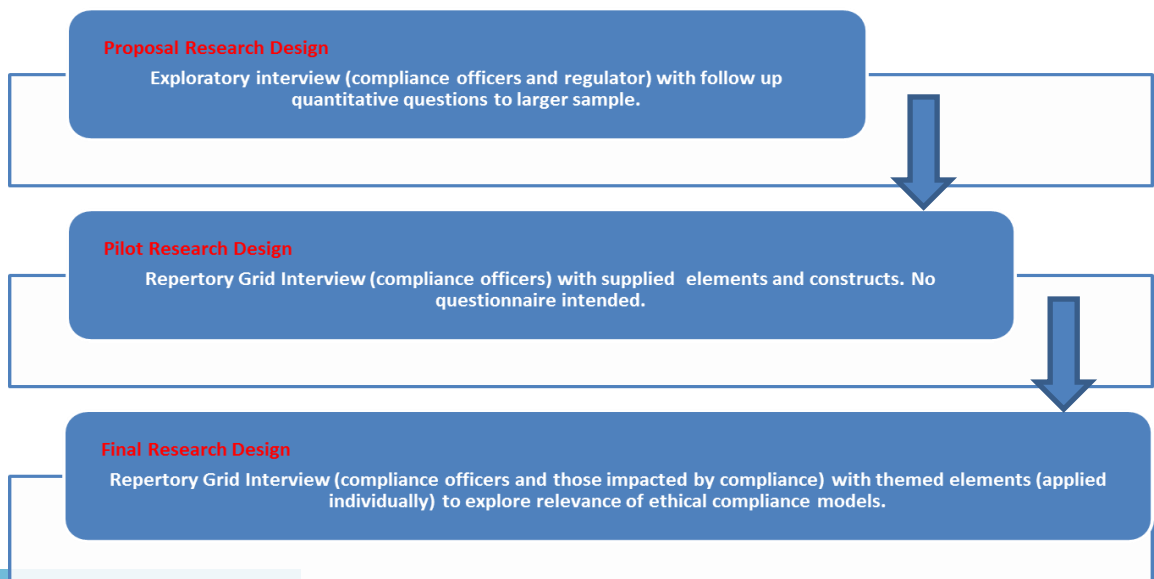
**Figure 14 Summary of ontological and epistemological underpinnings, related to methods employed**

|              |   | Application in this research  |
|--------------|---|---|
| Ontology     | The nature of reality                     | Pragmatism/Relativism - there are many truths, facts depend on viewpoint of observer  |
| Epistemology | The nature of knowledge                   | Humans learn and develop (construct knowledge) through experience so this directly impacts on their strategic approach when deciding on compliance approaches     |
| Methodology  | The nature of research design and methods | Qualitative - Inductive and exploratory discourse, during personal, repertory grid. Qualitative and quantitative analysis on constructs through content analysis. |
| Methods      | The means of collecting data              | Repertory grid/unstructured interviews<br>Personal construct analysis<br>Interview transcription analysis (Story telling)   |

A summary of the iterations in the research methodology design is set out in

Figure 15 from the proposal stage of the project, through to the pilot stage of the project, and then to the final research design adopted in this thesis. This provides some context to the explanation of methodology set out from Section 6.2 onwards.

**Figure 15 Iterations of research methodology design**





## 6.2 Summary of methodology

The final methodology has been designed to explore objective compliance models within the literature using subjective data sought from the individuals at the ‘front line’ dealing with financial service regulation – the compliance officers and risk managers themselves. Under this context, the research questions have been refined to the final version that is presented within Table 8.

To explore the research questions (Table 8), the repertory grid tool (see details in Section 6.4) has been used to facilitate sessions with individuals impacted by compliance within financial service organisations (an overview of participants can be seen in Table 11). Unlike traditional interviews a major part of the session with the participants involves preparation of a grid which is used to compare and contrast experiences. This then facilitates ‘story telling’ by participants which draws on tacit knowledge. At the end of the session a mixture of unstructured, open and closed questions were explored (depending on remaining interview time) to discuss individual views that emerged during the repertory grid session. Despite the unstructured nature of discussions, three main themes reviewed during the literature search (new regulation, consulting and alternative options – see Literature Framework, Section 3.1) were always discussed to some extent with individuals, using the following broad questions:

- What are the effects of changing regulation?
- When/How are consultants used?
- When/How are outsourcing/shared service options considered?

This deliberate direction of open discussion of themed topic areas was to allow for thematic analysis of individual interviews. The intention of questioning themed topic area at a broad level is to avoid the issue of interviewer bias. The method of personal interview has limitations, and significant issues obtaining access to staff were encountered (at the appropriate level, for an appropriate amount of time) to explore the research questions fully. In addition the aspect of interviewer bias/influence was considered carefully during the course of the research project. There are also concerns that “underlying reality” is not always accessed during the course of depth interviews (Rogers and Ryals, 2007), whereby participants provide the answer they believe the researcher wants, rather than “admitting reality”. Ultimately these concerns led to the decision to employ repertory grid technique (discussed further below under Section 6.4). Feedback from the pilot interview stage has been applied as necessary, to change and clarify the interviews applied to the larger sample (see Section 6.4.4).

**Table 8 A summary of research questions, related literature and adopted methodology**

| <i>Overall aim and research objective</i>  | <i>Related literature</i>   | <i>RQ and adopted methodology</i>  |
|--|---|--|
| <b>Aim - In light of changing regulatory cycles to explore whether it is possible to identify a best practice model of compliance for the banking sector.</b>              |   |  |
| Objective 1 -To understand the motives for regulatory compliance by banks<br><br>(See also discussion of concepts in Sections 1.2.1 and 1.2.5)                             | Microeconomic Theory/Macroeconomic Theory – Regulatory capture (Stigler, 1971; Baker, 2010; Omarova, 2011/2012; Young, 2012); Agency Theory (Ross, 1973; Fullenkamp & Sharma; 2012; Alexander; 2006); Rent Seeking (Krueger, 1974; Krawiec; 2005), Avoiding market failure (Keynes – Crotty, 2011) Models – Responsive Regulation (Ayres and Braithwaite, 1992) Self-Regulation/Management based regulation (Stefanadis, 2003; Coglianese and Lazer, 2003), Meta regulation (Gilad, 2010) | RQ1 To what extent does the regulatory cycle influence managements’ decision making over compliance approach?<br>Repertory Grid completion – open questions to discuss new regulation  |
| Objective 2- To explore the different structures of regulatory compliance in operation<br><br>(See also discussion of concepts in Sections 1.2.2, 1.2.3, 1.2.4, and 1.2.5) | Value culture, compliance competence (Jackman, 2001), Partnership and ethical framework (Edwards and Wolfe, 2004/2004/2007; Barraquier, 2011), Deterrence and normative model (Malloy, 2003), Active and passive compliance/Cosmetic compliance (Crump, 2007)   | RQ2a What are the key constructs that influence a managers’ decision over the compliance function approach?<br>RQ2b How do compliance officers’ personal constructs align to academic models of compliance?<br>Repertory Grid completion – exploring compliance officers personal and collective constructs  |
| Objective 3 - To investigate the circumstances under which different approaches would be adopted<br><br>(See also discussion of concepts in Section 1.2.6)                 | Shared Services and Outsourcing (Herbert and Seal, 2009; Mclvor et al., 2009; Marshall, 2001); Transaction Cost Economics/Outsourcing (Spekle et al., 2007); Using Consultants (Gable, 2005; Gullapalli, 2005; Krawiec, 2005)   | RQ3 In cases of new regulation, how do compliance functions rely on external expertise (consultants) or is there proactive promotion of in house knowledge and expertise?<br>Repertory Grid completion – open questions to discuss alternative approaches i.e. using consultants/shared services/outsourcing |

### 6.3 Ethical considerations

The importance of informed consent and clear communication of the purpose of the research has been a vital ethical consideration within the data collection stage (Bryman and Bell, 2011; Easterby-Smith, Thorpe and Jackson, 2012). In addition, where requested by individual participants the collective (anonymised) results of data collection were made available to individual participants to promote research relevance (Easterby-Smith et al., 2012, p. 157).

The University and the Business School set out clear guidelines (via Ethics and Governance Handbook<sup>80</sup>) with regard to ethical approval of research. Ethical approval was initialised shortly after project approval. The results of Northumbria's online ethics tool indicated an 'Amber' rating for the project. This was due to the involvement of people and organisations within the data collection phase of the project. Ethical approval was granted by the Newcastle Business School's Research and Ethics Committee following the submission of the organisational and individual consent forms.

However, one organisation also requested completion of a non-disclosure agreement (NDA) in addition to the organisational consent/informed consent forms. Although the confidentiality and anonymity of all participants was relevant through the design of the data collection, this was an additional step in the process for this organisation when considering future publication from this thesis. The requirement to complete the NDA caused significant delays within the research process, with communication between the respective compliance teams at the university and the organisation being very slow (spanning a period from June 2013 to December 2013), delaying data collection.

### 6.4 The repertory grid technique

The rationale for use of repertory grid technique within this research was to explore compliance officers' tacit knowledge. The completion of the grid facilitated discussions to compare and contrast compliance officers' personal experiences, ranging from worst compliance experience through to their viewpoint of aspirational compliance. The following sections summarise the underlying principles of personal construct theory (Section 6.4.1), and justify the specific techniques involved in administration of a repertory grid session (Sections 6.4.2 to 6.5).

Prior to these more technical discussions, a simple example is presented to try to explain, and simplify the jargon that exists within the academic literature base. Figure

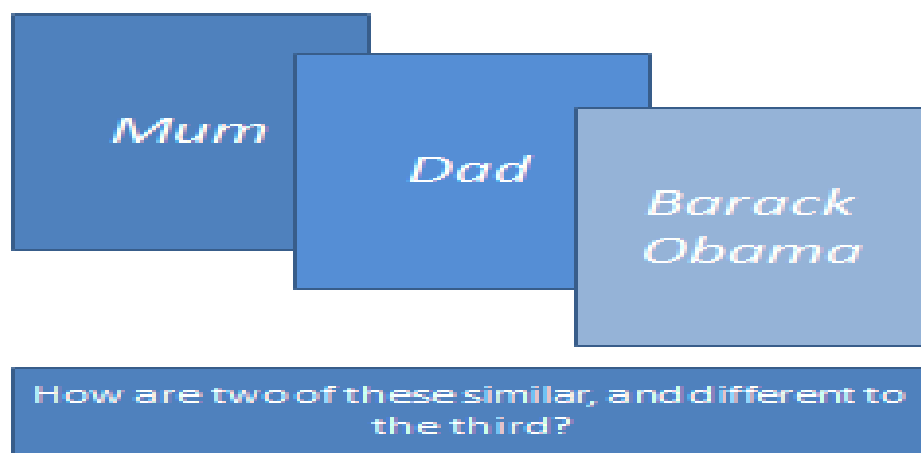
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<sup>80</sup> Information on Northumbria University's policies is publically available at <https://www.northumbria.ac.uk/research/ethics-and-governance/> accessed November 2015.

16 was used during doctoral conferences to explain the methodology selected within this research, by providing a straightforward example of the interviewing technique (in non-technical language). There are various techniques to elicit personal constructs proposed by the literature. However, the most common technique (and the technique used in this study) appears to be that of triadic elicitation. This technique employs selection of three elements (in the example Mum, Dad and Barack Obama) and asking the participant to describe “which two of these are the same in some way, and different from the third?” (Jankowicz, 2004, p. 24), and noting down the ‘thing’ that the two have in common, and the ‘reason’ the third differs<sup>81</sup>. Questions to explore similarities and differences between the three people would be discussed with the participant during sessions (which is termed laddering within the literature), to try to draw out tacit knowledge about the overall topic.

The same technique to explore similarities and differences in compliance experiences has been applied in this thesis. During repertory grid sessions, the compliance officers were asked to compare and contrast their experiences of compliance, ranging from their viewpoint of worst compliance, to their viewpoint of aspirational compliance.

**Figure 16 A simple example of triadic elicitation, which is used to explore experiences within repertory grid sessions**



#### 6.4.1 Personal construct theory

The repertory grid technique is grounded by personal construct theory proposed by Kelly in 1955 (Bell and Banister, 2004). The technique is used to identify the way in which research participants interpret their experience of the world. Duberley, Johnson,

<sup>81</sup> An example of a response may be to consider gender issue in that Dad and Barack Obama are both male, and mum is differentiated as a female. A second example may focus on the relationship issue with mum and dad grouped together as close members of family, and Barack Obama differentiated as being known only due his ‘celebrity’ status.

Catherine and Close (2000) describe how the technique acts as an enabler for the identification of these constructs “which may be difficult to articulate since they are based on tacit knowledge” (p. 430). Jankowicz (2004) provides a brief list of applications of repertory grid. These include the occupational application for “knowledge capture and particularly, the clarification of tacit knowledge” (p. 9). Bell and Bannister (2004) liken an individual’s personal construct system to “talking about his stance towards the world, we are talking about him as a person” (p. 2 of First Edition). Goffin, Raja, and Szwejcowski (2012) propose that the use of repertory grid as a methodological tool allows for a “quantitative angle to qualitative data” (p. 807).

Kelly (1963, Chapter 1) starts his discussion of “theory of personal constructs” with background of the philosophical roots of constructive alternativism. Jankowicz (2004) describes that a repertory grid can be used and defined in a variety of ways. The argument behind this is the fundamental assumption of constructive alternativism underpinning Kelly’s development of theory and the Role Construct Repertory Test (p. 15). Under constructive alternativism, different people will construe the same thing differently, and individuals will construe the same thing differently on separate occasions. Stewart and Stewart and Fonda (1981) summarise the theoretical underpinnings of personal construct theory as below:

- “Perceptions influence expectations, and expectations influence perceptions;
  - The medium through which this happens is known as the construct system;
  - Construct systems are unique to the individual and developed through life.”
- (Stewart et al., 1981, p. 8)

Fransella, Bell and Bannister (2004), based on Kelly’s work, contend that grids are about constructs (p. 7). Kelly (1963) sets out a number of “corollaries” to describe the process of construing: construction corollary; individuality corollary; organisation corollary; dichotomy corollary; choice corollary; range corollary; experience corollary; modulation corollary; commonality corollary; and sociality corollary. A summary of Kelly’s definition/statement on each corollary, and a further layman’s description summarised from Fransella et al. (2004) and Jankowicz (2004), and how these have been applied in this research is provided within Appendix 3.

#### **6.4.2 The repertory grid output**

During the process of a repertory grid session a grid is used to capture data. The resulting grids comprise of four parts: 1) The overall topic under review; 2) A set of elements (which represents the topic); 3) A set of constructs (which represents how the

participant makes sense of, and differentiates between the elements); and 4) A set of ratings of elements on constructs (where the elements are positioned between extremes of constructs to allow for statistical analysis). The formation of the grid emphasises “participation and fostering a sense of inclusion in the production of knowledge” for interviewees (Millward, Asumeng and McDowell, 2010).

An example of the grid template used in during sessions is presented in Figure 17 where the overall topic under review is compliance, the elements are the range of experiences discussed with practitioners (ranging from worst to aspirational compliance), and the resulting discussions record the personal constructs of individuals in the grid itself (see session plan/discussion detailed later within Table 9).

A sample review of prior business research utilising Repertory Grid Technique was performed, which has been included for reference in Appendix 4. It appears that the specific use of repertory grid in financial services research is limited. On searching the literature in Google Scholar using search terms “repertory grid” and “financial services” only 329 records were found (as at 22 October 2014), and only 58 records when the search term of “compliance” was added. On further investigation of these records there were no direct links between the topics of financial service compliance/risk management research (with the reference to financial services often being a tenuous link to the specific research purpose which was often leadership, or information management related). Therefore, the chosen method of repertory grid for this thesis will contribute to the limited literature in this area.

Figure 17 Example of the repertory grid template provided to participants within this study

|   |                                     |   |   |   |   |   |   |                                  |
|---|-------------------------------------|---|---|---|---|---|---|----------------------------------|
| <p align="center"><i>Your own words to describe scenario:</i></p> <p>Example a - 'Ideal/Aspirational' compliance experience<br/>                 Example b - straightforward/efficient compliance experience<br/>                 Example c - routine compliance experience with minor issue<br/>                 Example d - relatively routine compliance with significant issues<br/>                 Example e - compliance experience with major issues<br/>                 Example f - 'worst' compliance experience</p> |                                     |   |   |   |   |   |   | Participant Name:                |
|   |                                     |   |   |   |   |   |   |                                  |
|   |                                     |   |   |   |   |   |   | Participant Code:                |
|   |                                     |   |   |   |   |   |   |                                  |
|   |                                     |   |   |   |   |   |   |                                  |
|   |                                     |   |   |   |   |   |   |                                  |
| Ratings: '1' matches closely with left hand descriptor, '5' matches closely with right hand descriptor, '2,3,4' to rate between extremes.   |                                     |   |   |   |   |   |   |                                  |
| Note: you do not need to 'rank' you can use same scores for multiple examples if necessary  |                                     |   |   |   |   |   |   |                                  |
|   |                                     |   |   |   |   |   |   |                                  |
| Examples Compared   | Similar descriptor                  | a | b | c | d | e | f | Dissimilar descriptor            |
|   |                                     |   |   |   |   |   |   |                                  |
|   |                                     |   |   |   |   |   |   |                                  |
|   |                                     |   |   |   |   |   |   |                                  |
|   |                                     |   |   |   |   |   |   |                                  |
|   | Overall benefit to the organisation |   |   |   |   |   |   | Overall cost to the organisation |



There has been a mixture of applications of the repertory grid method within business research. Wright (2008, p. 755) summarises the repertory grid literature in the strategy field (for supplied and elicited elements), and contends that the grids can be used in a variety of ways to suit the individual research agenda. Some researchers fully embrace the origins of repertory grid technique in personal construct theory and allow participants to fully develop both elements and constructs individually (Alexander, 2008; Senior, 2004). Some researchers provide elements, and then allow participants to prepare construct and rating (Wright, 2012; Goffin, 2012; Thota, 2011; Song, 2008; Panagiotou, 2007). And finally, some researchers prefer to provide both elements, and constructs allowing participants only to rate within the grid. Only two examples of research adopting supplied elements and constructs were provided by Edwards, McDonald and Young (2009) in their literature review of repertory grid research (referencing examples of Lee and Truex (2000) and Young (2004); Edwards et al., 2009, p. 787). By providing all elements and constructs, it suggests the grid acts as a vehicle to collect ratings only (which was discussed further under Section 6.4.1). Edwards et al. (2009) provide a table of impacts of using supplied or elicited elements and constructs (see Figure 18).

The application in this thesis represents a partial repertory grid, as the theming of elements across the range of experiences allows for cross comparison between grids.

**Figure 18 Impact of using supplied or elicited elements and constructs (Edwards, McDonald and Young, 2009, pp. 797-790)**

|                          | Constructs supplied  | Constructs Elicited  |
|--------------------------|--|--|
| <b>Elements Supplied</b> | <b>Fixed Grid</b><br>Easy to Analyse/compare<br>Limited understanding of individuals perceptions<br>Quantitative/Statistical analysis possible | <b>Partial repertory grid</b><br>Some comparisons across elements possible<br>Richness in individual conceptualisation of elements<br>Analysis using techniques such as cluster analysis, principle component analysis |
| <b>Elements Elicited</b> | N/A  | <b>Full repertory grid</b><br>Rich data set<br>Direct comparisons difficult<br>Analysis by identifying themes and coding   |

**Final approach adopted within this thesis**

### 6.4.3 Outline of method in pilot:

Honey (1979) provides a clear overview of the steps involved in the application of the repertory grid technique. For the purposes of the pilot, the elements were pre-determined based on the review of compliance literature. The intention was to elicit all constructs from participants, as based on a review of the application of repertory grid by other researchers (see Appendix 4) as this appeared to be the most commonly adopted method in business research applications. This was expected to take no more than 1 hour, based on discussion of grid delivery in the literature (Appendix 4) and this was indeed the case. The steps for the first iteration of the pilot study were:

1. An outline explaining the repertory grid method was provided to the participant in advance, so they understood the purpose of the technique;
2. Elements were provided at the top of the grid;
3. Individuals were provided with cards with numbers on one side of the cards which correspond with the elements at the top of the grid;
4. Cards were turned face down and shuffled, then three cards drawn at random;
5. Subject marked on the grid which elements were being compared (using element numbers);
6. Always on left side the subject described what aspects the two similar elements share, on the right side express what makes the third element different to other two elements;
7. Finally elements were rated to the constructs (using a 5 point scale), whereby a rating of 1 denoted an understanding that the element closely matches the description in the left most column, whilst a score of 5 would denote an understanding that the element to match more closely with the contrasting description in the right hand column. If it was considered that an element could not be rated against a construct a zero or N/A was to be inserted.

### 6.4.4 Reflections and adaptations following initial pilot of repertory grid session

After preparing the session<sup>82</sup> based on review of the literature on repertory grid (Appendix 4) and using the basic steps outlined in Section 6.4.3 (proposed by Honey (1979)) a practicing compliance officer working within a multinational organisation was approached. This individual was chosen as he was an experienced compliance manager, responsible for oversight and reporting within a complex worldwide

<sup>82</sup> The pilot documentation was deliberately called a 'workshop' in anticipation of flexibility of group interviews, and also to appeal to practitioners in the sense that they would achieve benefit from participating in a workshop which would allow them to use the technique of repertory grid in other business applications through participation.

compliance network. Although this person was not working within the financial service sector, the compliance concepts that were being explored within the grid were transferable between industries for the purpose of the pilot session.

The session outline was sent in advance to allow time to absorb the material, and at the start of the session the purpose of the research was explained, along with the steps involved in completing the grid. A script suggested by Honey (1979) was modified to the topic of this thesis, and followed to avoid impact of interview bias on the results (see Table 9).

Table 9 Final Session Plan adapted from Honey (1979)

What you do

What you say

The first item to complete is a bit of paperwork – please can you all ensure that you have completed your informed consent and demographic information by the end of the session.

This session has been arranged so I can pick your brains about compliance in the financial service sector. I want to find out your views so I can publish empirical research into what it means to run an efficient and effective compliance function, and the implications of using compliance consultants or alternatively outsourcing compliance, or implementing shared service arrangements.

In effect I am inviting you to join an extended survey which will assemble opinions from approximately 30 compliance managers at different levels in the compliance function, and from different organisations.

First let me give you some assurances about the process – the whole survey will be conducted anonymously. Although I have asked for some demographic information this data will be recoded and anonymised, and will not be published to either your employer or other participants. Your ideas will be collected together along with everyone else's. After I have analysed all of the data I will feed back the main findings to everyone who takes part collectively (and if you so wish individually).

Finally I want to reassure you that this is not an exam or test of any kind – even though I am canvassing your views there are no right or wrong ideas or answers. Your opinions are as valuable as all the other participants.

Before I start taking you through the method I shall be using to collect your views, are there any questions you would like to ask about the exercise in general?

---

**What you do****What you say**

---

**Answer questions about the purpose of the survey.**

Let's move onto the survey itself. I hope you will find the survey method interesting, as it is a novel and **unusual way of collecting views** on compliance methods. Rather than a questionnaire style format, you will be completing your responses in the form of a **grid structure**.

**Show them the grid**

Each grid will be individual as they reflect your individual reflections on the topic of compliance.

But first we will start with a simple example – which I will use visual tools to demonstrate.

**Hold up pencil, pen, biro, board marker.**

The topic in this case is writing implements – show them the selected writing implements.

So write these on the top of the grid. Then you would write these different examples on a card (or a post it). Then I want you to pick out **three cards at random** and group them – which two are similar and which is the one which is dissimilar.

Answer this question

**can you think of any other ways in which two of these 'writing implements' are similar to each other and different from the third**

## What you do

## What you say

Write down whatever it is that the pair have in common in the left hand side of the repertory grid form and write down whatever it is that makes the singleton different in the right hand column. (Please also make a note in the second from left column the numbers of the two cards you think are similar and in the second from right column the number of the different element). **Add as many/or as few descriptors** as you wish for these three cards before selecting another three cards.

Make another selection of three cards and repeat.

For the purpose of this example I would like you just to come up with 5 or so descriptors and then I want you to 'rate' your descriptions on a scale of 1 to 5 against the element. So for each element go down the list of descriptions and rate 1 if you think it is most like the description on left, and 5 if you think it is most like the descriptor on the right (or a score of 2, 3, or 4 if you believe the element is between the extremes)

Finally I want you to review the **overall idea** I have provided at the bottom of the grid – and rate in similar way to the way you have rated your own ideas.

So could you quickly work through this process as a practice grid?

Now I want you to revisit the exercise and complete for compliance. In terms of the elements I asked you to **think in advance** of some different examples of compliance approaches/scenarios (which may be personal to you) with the broad

## What you do

## What you say

categories in mind of:

- Example 1 - 'Ideal/Aspirational' compliance approach
- Example 2 - straightforward/efficient compliance approach
- Example 3 - routine compliance approach with minor issue
- Example 4 - relatively routine compliance with significant issues
- Example 5 - compliance approach with major issues
- Example 6 - 'worst' compliance approach

Name these for you individually so they are meaningful for you and populate the top of the grid. Then repeat the process we did for the pens – put your examples on post its and compare listing your descriptors – what makes similar, what makes different.

Answer this question

Take 20 minutes?

**can you think of any other ways in which two of these 'elements' are similar to each other and different from the third in terms of the INPUTS/OUTCOMES you get which influence your decision in your approach to compliance**

Once you feel you have exhausted combinations I would you like you to 'rate' your descriptions on a scale of 1 to 5 against



## What you do

## What you say

the element. So for each element go down the list of descriptions and rate 1 if you think it is most like the description on left, and 5 if you think it is most like the descriptor on the right (or a score of 2, 3, or 4 if you believe the element is between the extremes)

Finally I want you to indicate your opinion of how the overall **idea** I have supplied of 'benefits to the organisation' rate against your own example of compliance approaches.

Before you start I just want you to remember I am trying to understand the **components of different approaches to compliance**, but please also broadly consider the impacts of costs in comparison to benefits of different compliance approaches, and also how the regulatory approach impacts on these approaches.

So now this is over to you – if you have any questions during the course of the exercise please just let me know (but remember I am interested in your personal views).

When the individual started the exercise he immediately encountered problems trying to phrase what he saw to be differences between the elements. Unfortunately he got into a certain mind-set whereby he was only identifying high level differences of internal/external to organisation when he was picking out the different elements and did not drill down further – this was not expected. In the end the decision to terminate the session was made as he simply stated that the exercise was ‘too hard’. This problem was encountered due to a mixture of inexperience of administering the grid, and also the individual not being receptive of the technique.

In order to ensure that these problems were not repeated, feedback was sought from the participant on where they thought the session could be improved for future delivery. This feedback together with reflections of the author are set out in Figure 19.

**Figure 19 Pilot feedback and reflection of the author**

| <b>Feedback from pilot participant</b>  | <b>Reflections on feedback</b>  |
|---|---|
| “Need to spell out purpose so participants can direct their thoughts in the grid”   | The purpose is already set out in session plan, and repeated verbally – so there may be element of interviewer bias if we set purpose out any more  |
| Suggested that not only the elements are provided in the grid, but constructs are also provided – and then the participants can simply rate these | The disadvantage of this would be the lack of practitioner input into forming the constructs. If this was to be implemented the individuals could be asked as an additional step to scale the constructs as which they think are most important. Also spaces could be left in the grid for participants to suggest additional constructs. |
| ‘change the descriptions of the elements’ – the participant thought these were too long (based on Jackman model)                                  | Adapt to something more meaningful for those who are not absorbed in academia   |

The individual offered to look over the grid again to see if it was more digestible after changes were made. After this the literature was reviewed again to form a list of supplied constructs (Table 10). However, spaces were made available for additional contribution of practitioners to ensure that the individuals’ personal constructs would also be included.

The idea of supplied constructs is supported by Goffin et al. (2012), who discuss the idea of ‘hygiene factors’ which relate to constructs which may be frequently mentioned by participants during interview, including repertory grid interviews (as the factors are often referred to in academic and practitioner literature). These ‘hygiene factors’, although frequently cited, may not actually represent the most ‘important’ factor or

concept to individual participants. Therefore, this supported the method to provide certain constructs to the participants (from the literature), so the participants can comment on these 'hygiene factors' whilst being allowed to develop their own, more meaningful personal constructs. Under this basis a second pilot session was held (using supplied constructs in Table 10).

**Table 10 Listing of constructs provided in advance for pilot 2 participant (with links to literature)**

| <b>Construct provided</b>  | <b>Bipolar construct</b>  | <b>Link to literature</b>   |
|--|---|---|
| <b>Compliance benefits perceived to outweigh costs – costs irrelevant</b>                    | Compliance Costs perceived to outweigh benefits                           | Harvey (2004), Satheye (2008)   |
| <b>Commitment to Training</b>  | Minimal Training  | Taylor (2005), SIA (2005)   |
| <b>Commitment to ethics and culture</b>  | Disregard to ethics and culture   | Jackman (2001), Edwards and Wolfe (2005), Wood (2002)   |
| <b>Proactive assessment by management of reducing reputation risk</b>                        | Disregard by management of reputation risk                                | Crump (2007), Calcott (2010), Arora and Gangopadhyay (1995), Shimshack and Ward (2010)                |
| <b>Seen to be 'best practice' by peers</b>   | Disregard of peer performance   | Malloy (2003)   |
| <b>Compliance officers status high -skills set, independence, authority</b>                  | Disregards of compliance officers importance in organisation              | Somerville (2010)   |
| <b>Extensive investment of IT compliance resources</b>                                       | Minimal investment in IT compliance resources                             | Bamberger (2010), Gable (2005), Garcia (2004), Mainelli and Yeandle (2006), Hussein and Hussan (2008) |
| <b>Full awareness of New Regulation – e.g. BASEL III/FATCA</b>                               | Limited knowledge of new regulation                                       | Stoneman (2005), Gebhardt and Novotny-Farkas (2011), Dizdarevic (2011), Wise and Baker (2012)         |
| <b>Compliance costs easily identifiable and monitored</b>                                    | Compliance costs merged into 'admin' function of business – no monitoring | Alfon and Andrews (1993), Frank et. al (1998), Elliehausen (1998), Deloitte (2006)                    |
| <b>Compliance knowledge nurtured and developed in house</b>                                  | Compliance knowledge limited within the business                          | Herbert and Seal (2009)   |
| <b>Internal centre of excellence</b>   | External centre of excellence   | Mclvor et al. (2011)  |
| <b>Business relationships, communication and interfaces essential</b>                        | Minimal regard for business relationships, communication and interfaces   | BASEL (2005), Thomas (1997), Wood (2002), Carretta (2010)   |
| <b>Standardised approach/strategy</b>  | Flexible compliance approach/strategy                                     | COSO (2004)   |
| <b>Continuous development and improvement to compliance – 'customer' driven improvements</b> | No calls for improvement to compliance – stagnant approach                | Crump (2007)  |

In the second pilot session, the session plan had been modified based on the feedback received (Figure 19) and delivered to a second (recently retired) compliance officer. This individual differed from the first pilot participant, as his career revolved around legal counsel roles (with some responsibility for compliance), whereas the first individual had an accounting focussed background. A mix of demographics was

considered important within the pilot stage, as during the live data collection there was an expectation for a mix of background experience for participants.

Again the session plan was sent in advance and the individual offered some feedback – with comments to simplify the ‘technical language’ used (such as elements and constructs) and just instead to describe the grid process. The overall feedback was that the session was well constructed. However, the individual emphasised that participants would not understand from individual reading of the session outline instructions, until they were led through an example of completing the grid. From this, the instruction were adjusted to include a simple grid example as proposed by Tomico, Karapanos, Levy, Mitzutani and Yamanaka (2009, see Section 6.4.5). By receiving the session outline in advance and looking at the suggested descriptors, the individual had already started to think of his own personal constructs which he wanted to be added to the grid. The individual considered that a real benefit to participants would be the actual completion of the grid, provoking thoughts on self-improvement towards ‘aspirational’ levels of compliance.

#### **6.4.5 Discussions with more experienced researchers utilising repertory grid**

During discussions with a couple of more experienced users of repertory grid technique from the University, the principles of the technique were revisited. The main advantage of repertory grid identified of removal of interviewer biases was ultimately lost in the proposed approach adopted in second pilot, by supplying elements and certain constructs based on the literature. This view is in contrast to the concepts of hygiene constructs discussed under Section 6.4.4. However, this is supported by the review of impact of supplying/eliciting elements and constructs performed by Edwards et al. (2009, see Figure 18). Supplying constructs was considered to be predetermining the focus of the session to a great extent, and thus creating interviewer bias by default.

Therefore, the session was adapted once more for use during live data collection. The piloted adaptation of Honey’s step process was used, with categories provided to participants to choose elements of the topic and triadic elicitation of constructs. Jankowicz (2004, pp. 169-177) describe Honey’s content analysis technique and the adaptation of supplying ‘one overall summary’ construct. Designing the grid in this way enables content analysis and comparison of ratings between the elicited construct and the supplied overall construct (using similarity values).

The adapted version included a simple exercise to introduce the participants to using the grid format (using writing implements as a topic, and different pens as visual

examples – see Figure 20 which shows documents used during the session). This is in line with technique performed by Tomico, Karapanos, Levy, Mitzutani and Yamanaka (2009), and which provides an easily digestible topic to introduce the workings of the grid to inexperienced users. This simple exercise was piloted and refined based on feedback from a selection of peers. This was performed in a ‘group context’ as there would be a mix of individual and group sessions performed in live data collection. Grids can be prepared in group situations with the objective of building shared understandings, in as productive a way as possible (Easterby-Smith et al., 2012, p. 208; Burr, Giliberto and Butt, 2014). Feedback from the group pilot resulted in minimal refinement (formatting of grid). A final version of the ‘session’ outline and provided grid (including details of element themes and overall supplied construct) is set out in Table 9.

#### 6.4.6 Sampling and access

Due to the research methodology of personal interview/repertory grid selected, geographical sampling restrictions were applied to include only UK banking organisations. Using the OSIRIS database<sup>83</sup> a listing of UK banking organisations was produced. A strategy to target certain organisations in order to obtain access to individuals was developed. A number of routes to develop access were trialled with no success including:

- Direct approach to a number of (banking) compliance training providers to host a session;
- Direct approach to FSA (prior to restructure) to access both FSA staff and host a session (in one of their advertised ‘compliance’ training sessions);
- Direct approach to author’s own professional institute (ICAEW) to access mailing lists;
- Direct mailings to Chief Compliance officers using the Bank names/address developed through internet searches, from listing produced in OSIRIS.

These routes all developed ‘dead ends’ and so existing contacts from colleagues at the University, were approached directly with an abstract of the proposed research (convenience sampling). After meeting with personnel in one bank, an individual provided another contact within another bank (snowball sampling). In addition, direct contact with individuals (under financial/compliance/risk management roles) was sought via ‘LinkedIn’ networking. A number of contacts were made during conference

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<sup>83</sup> A database which provides information on listed companies, including both financial and non-financial data.

attendance (and from hosting a workshop on ‘ethical compliance’ for practitioners<sup>84</sup>). Table 11 summarises the details of repertory grid sessions with participants, and the data collected.

Although this approach to sampling may be subject to criticism, it must be recognised that gaining access to these types of individuals and organisations is notoriously difficult due to concerns about confidentiality. Arranging access to participants within one organisation took nearly 6 months, due to the requirements to complete a non-disclosure agreement (and getting the compliance teams from the organisation and the University aligned).

**Table 11 Details of repertory grid sessions, and data collected**

| <b>Date</b>   | <b>Participant demographics</b>             | <b>Method employed</b>                   | <b>Data collected<sup>85</sup></b>  |
|---------------|---|--|---|
| August 2013   | Male, Head of Risk Management               | Repertory grid session                   | Repertory grid completed (36 constructs), Transcription of 1 ½ hr. interview    |
| January 2014  | Group of five customer facing employees     | Repertory grid session, group discussion | Five repertory grids completed (68 constructs), field notes of 2 hr. discussion |
| April 2014    | Male, Financial Crime Management            | Repertory grid session                   | Repertory grid completed (24 constructs), Transcription of 1 hr. interview      |
| April 2014    | Female, Compliance Officer                  | Repertory grid session                   | Repertory grid completed (20 constructs), Transcription of 1 hr. interview      |
| November 2014 | Male, Compliance Officer                    | Repertory grid session                   | Repertory grid completed (22 constructs), Transcription of 1 hr. interview      |
| November 2014 | Male, Compliance Officer                    | Repertory grid session                   | Repertory grid completed (24 constructs), Transcription of 1 hr. interview      |
| November 2014 | Male, Compliance/ Risk Officer              | Repertory grid session                   | Repertory grid completed (18 constructs), Transcription of 1 hr. interview      |
| November 2014 | Male, Regulator (former Compliance Officer) | Repertory grid session                   | Repertory grid completed (18 constructs), Transcription of 1 hr. interview      |

#### 6.4.7 Transcription process

To complement the data collected within the grid, interviews were recorded to enhance the validity and rigour of the data produced (see Table 11 for details of participants and

<sup>84</sup> Delivery of workshop ‘A Plea for Ethical Compliance’ at 32nd Cambridge International Symposium on Economic Crime.

<sup>85</sup> See Section 6.5 for reflections on data collected, with comparison to other studies in Table 12. Note that the data from the two pilot studies was used for development of method only (and does not form part of data analysed in Chapter 7).

data collected). The use of voice recording equipment allows a secondary record of the interview between author and participant, allowing reflection and interpretation of the written data provided in the grid in a subjective manner. Hammersley (2010) refers to reliance on 'Verstehen' (subjective interpretivism) within the transcription process. This supports the philosophical stance of pragmatism allowing cohesion of objectivism and subjectivism, in the methodological approach.

The elicitation of constructs during repertory grid interview led to an open discussion between the author and the interviewee on completion of the grids (the importance of data collected during 'open' discussion was identified at pilot stage of interviews). Due to the 'complimentary' nature of the formation of the repertory grid by participants, alongside discussions around grid formation between the researcher and the participant, it was decided to take a more denaturalised route (Oliver, Serovich and Mason, 2005) towards transcription following the principles developed below:

- A 'play script' format to transcription (including line number format for easy future reference);
- No time record denoted in transcription of words said/pauses/interruptions etc.;
- The transcription does not reflect the entire recording time. For example, large periods of interview are spent on grid exercise (and so data is recorded in grid itself). These sections are simply denoted as unrecorded in the transcription. 'Selectivity' is discussed further by Hammersley (2010, p. 556);
- No correction for grammatical errors in speech;
- There is no recognition of accents, or mispronounced words within the transcription (the author as interpreted words, as 'heard' from authors viewpoint);

Transcripts were sent to participants, to allow for any correction considered necessary by participants: with the ultimate purpose of supporting validity and rigour of data within the transcription.

A different approach was adopted for group sessions. Due to the larger size of groups and issues with transcription (i.e. identifying speakers, speakers talking over one another), an alternative method was chosen to record via field notes. Following group discussions, major discussion items were recorded in note format immediately after the session finished. These field notes were sent to the participants for confirmation of content (and allowing additional, specific comments from participants to be added), which supports validity and rigour of data output.



## 6.5 Reflections on data collated and analysed

A major hurdle in this thesis has been the arrangement of access with participants. Whilst participants may initially have expressed interest in contributing to the research there was a large fall out rate. This may be attributed to two factors: the first being those of perceived confidentiality issues given the sensitivities of the overall topic of compliance; and the second an unwillingness to participate in the specifics of the complex grid session. Consequently, the data collection period extended beyond the initial timeframe proposed at planning stages.

### 6.5.1 Reflections on access

Despite the difficulties obtaining access with relevant participants<sup>86</sup> the volume of data from sessions performed is rich, due to the breadth and depth of experiences explored during formation of repertory grids. For analysis purposes the data output of sessions has taken the form of both the grids themselves, and transcripts and field notes of open discussion following completion of the grids. The dominant output of the grid session is the constructs themselves, and, therefore, “the unit of analysis is the construct, not the individual” (Dick and Jankowicz, 2001, p. 193; Jankowicz, 2004, p. 147). Consequently, for saturation of data it is possible to focus on the number of constructs collated rather than the number of individual interviews. Glaser and Strauss (1967) in their wider discussion of grounded theory contend that during research, judgement is required to assess ‘when to stop sampling’ and theoretical saturation is reached, defined as the point at which no further data is being uncovered. To stretch saturation the diversity of the group of participants can be expanded.

This concept has been applied in this research by including those impacted by compliance, alongside those managing compliance within organisations. Although this element of grounded theory has been used within analysis, this study does not claim to position itself within grounded theory. Academics have criticised papers which ignore the roots of grounded theory set out in Glaser and Strauss 1967 founding work, *Discovery* (Walsh, Holton, Baily, Fernandez, Levina and Glaser, 2015). However, the basic assumptions of emergence i.e. remaining open, holds true for analysis and theory generation in this study. Goffin et al. (2012) suggest that Pareto analysis could be used to ascertain that “theoretical saturation” of constructs is reached and suggest that “saturation is reached either when no new categories or very few additional ones emerge from case studies” (p. 816). This applies within content analysis in this study, whereby during first round of categorisation an ‘other’ category was used to categorise

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<sup>86</sup> As discussed earlier in Section 6.4.6, in the end access was obtained for 12 participants as presented in Table 111, and Table 133.



the minority of constructs which were not easily allocated to the categories of the initial template, which was followed by subsequent rounds of categorisation when no new categories emerged (see Section 7.3).

Some prior research adopting repertory grid is summarised within Table 12, which demonstrates a range of constructs collated and analysed from as few as 128 constructs up to 876 constructs. If the extremes of the number of constructs are ignored, it can be argued that a range of 200-400 constructs is sufficient for content and thematic analysis. Table 12 also demonstrates how researchers adapt the use of the tool to suit their individual research agenda i.e. coding, thematic, content, Honey's content, through to principal component analysis (underlining the pragmatic use of the grid within the research domain).

**Table 12 Examples of prior repertory grid research, with details of number of participants and construct volumes analysed**

| Researcher                    | Research Discipline              | Number of Participants                                       | Number of Constructs (and analysis)  |
|-------------------------------|----------------------------------|--|--|
| Wright, et al. (2012)         | Strategic Management research    | 46 full time manager participating                           | 455 constructs (thematic analysis)   |
| Goffin et al. (2012)          | Supply chain management research | Two case studies: Case 1, 39 repertory grid; Case 2, Ongoing | 411 constructs (coding of constructs)  |
| Goffin and Koners (2011)      | New product development research | 30 repertory grid interviews                                 | 273 constructs (Gridlab and categorization of constructs)  |
| Pike, Knott and Newton (2011) | Decision Criteria                | 12 repertory grid interviews                                 | 189 constructs (Thematic analysis)   |
| Thota (2011)                  | Information Systems Research     | Over 2 cycles, 29 repertory grid participants                | 112 constructs in first action research cycle, 121 constructs in second cycle (Honey's content analysis performed) |
| Song and Gale(2008)           | Project Management Research      | 18 repertory grid interviews Completed                       | 128 constructs (content analysis)  |
| Senior and Swailes (2004)     | Performance management           | 60 repertory grid interviews completed                       | 615 constructs (principal component analysis)  |
| Dick and                      | Culture Survey                   | 51 repertory grid  | 380 constructs   |

| Researcher       | Research Discipline                     | Number of Participants                              | Number of Constructs (and analysis) |
|------------------|---|---|-------------------------------------|
| Jankowicz (2001) |   | interviews  | ("simple" content analysis p. 189)  |
| Honey (1979)     | Attitude Survey, Manufacturing Business | 73 repertory grid, performed in groups of approx. 8 | 876 constructs                      |

To ensure that rich descriptions of the compliance officers' experiences and perceptions were explored (to investigate each of the research questions) a qualitative interview method of analysing both grid and interview data has been adopted (Burr et al., 2014). This allows analysis of both the constructs produced during grid interview (which specifically addresses research question 2), and also the interview transcripts where discussion of individual issues were discussed openly by the participants (which addresses research questions 1 and 3 further). By combining the two outputs from interviews with practitioners, a broad set of data has been collated, and includes the story telling aspect within grid sessions.

The data set for this thesis is collated from 12 participants, resulting in a total construct pool of 230 (see Table 13). This represents an average of 19.2 constructs elicited from each session. However, it should be noted that the number of constructs produced was limited by time available for certain participants to be interviewed<sup>87</sup>, rather than a matter of limitations on topics to discuss during the grid formation process.

The average working experience of participants was 20.1 years, which indicates a rich, depth of experience (personal constructs) to draw from whilst undertaking the grid session. As the analysis of the data set is broadly qualitative, the concept of saturation has been followed (Glaser and Strauss, 1967). The concept of saturation was applied within elicitation of constructs during individual sessions themselves using laddering technique to explore the importance of each construct (Crudge and Johnson, 2007; Jankowicz, 2004); and through eyeball analysis of grids following sessions (see Section 7.2). As individual constructs have been collectively analysed under content analysis techniques, and open interviews have been coded individually the data set is considered to reflect representative views of the sample of practitioners at the time of the research.

<sup>87</sup> As found in other studies (Pérez and Picard, 2014), access was extremely difficult to arrange and negotiate, and so the researcher had to adapt around the need and time constraints of the individual participant. This is not considered to impact on the quality of the data, as the number of constructs elicited aligns to other studies (see Appendix 4).

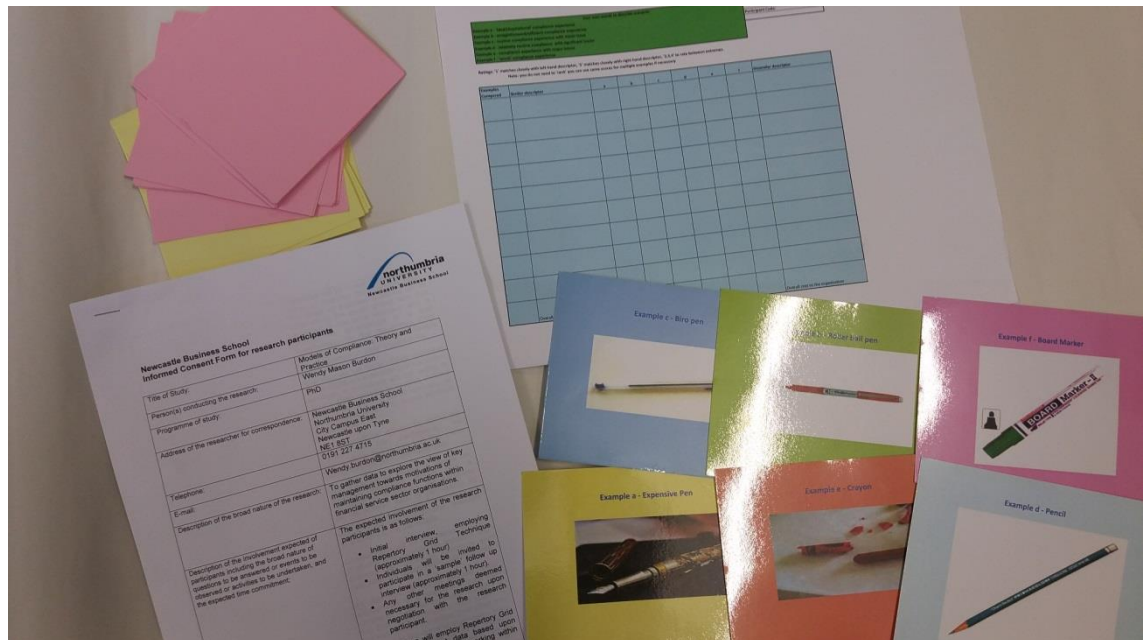
**Table 13 Biographical information of participants**

| Participant Reference | Gender | Experience (years) | (Self) Profession  | Considered              | Number of Constructs |
|-----------------------|--------|--------------------|--------------------|-------------------------|----------------------|
| lmc16                 | Male   | 16                 | Compliance         |                         | 36                   |
| ymo26                 | Male   | 26                 | Other              |                         | 18                   |
| ymo12                 | Male   | 12                 | Other              |                         | 14                   |
| ymo33                 | Male   | 33                 | Other              |                         | 8 <sup>88</sup>      |
| ymo27                 | Male   | 27                 | Other              |                         | 16                   |
| yfo0                  | Female | Not given.         | Other              |                         | 12                   |
| nmo28                 | Male   | 28                 | Other (Consultant) |                         | 24                   |
| efc10                 | Female | 10                 | Compliance         |                         | 20                   |
| vmla19                | Male   | 19                 | Legal              |                         | 22                   |
| jmc10                 | Male   | 10                 | Compliance         |                         | 24                   |
| omc20                 | Male   | 20                 | Compliance         |                         | 18                   |
| rmo20                 | Male   | 20                 | Other              | (Risk/Audit/Compliance) | 18                   |
| <b>Average</b>        |        | <b>20.1</b>        |                    |                         | <b>19.2</b>          |

### 6.5.2 Reflections on the data collection exercise

To assist in the grid session, the documentation provided to participants was made as 'friendly' as possible. This involved preparation of laminated cards for example exercise and colourful grids and cardboard to complete the compliance grid itself (see Figure 20).

**Figure 20 A photograph of the documents used during sessions - the example pen exercise, the grid itself and the cards for triadic elicitation**



<sup>88</sup> Participant Grid was revisited and a number of constructs were unusable (i.e. did not reflect usable bipolar pair for purposes of analysis. Therefore, only 8 constructs used within analysis).

One finding of delivery of grid sessions is that despite pilot studies, meticulous planning and following a “script” (Honey, 1979), each interview outcome was very different. The majority of participants appeared to enjoy the process of completing the grid, making general comments at the end of session such as ‘it’s funny how it makes you think like that’ (verbal comment from participant lmc16). This demonstrates the suitability of repertory grid during interviews within this thesis, offering an alternative to standard interview questions, by promoting a different kind of thinking: ultimately providing a means for the exploration of tacit knowledge. One individual found so much value in the exercise, that they requested extra information on the technique, as they could see the benefit of adapting the repertory grid within their own work in practice (risk assessment analysis).

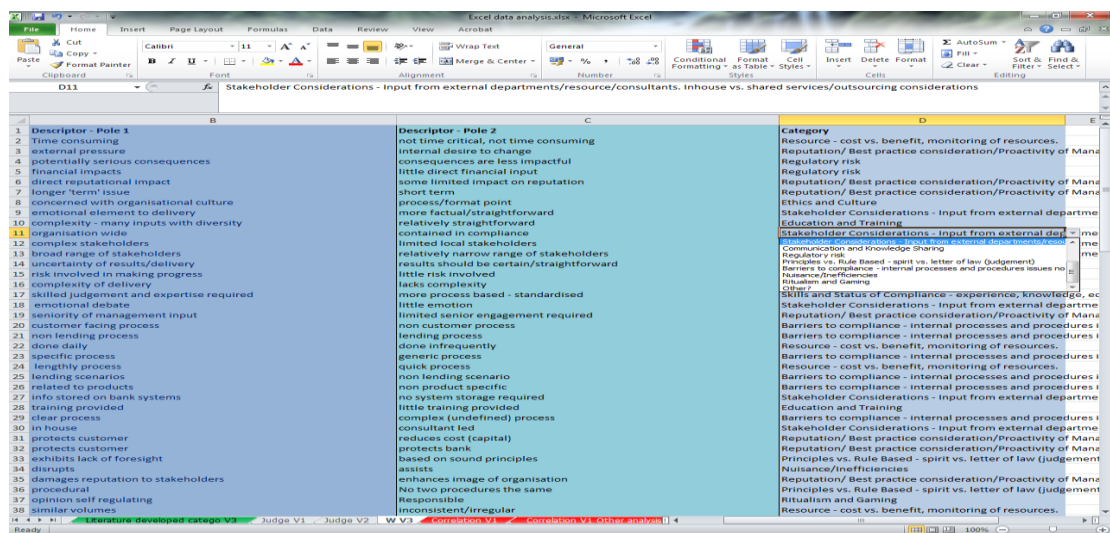
However, there were a minority of cases (two instances) who really struggled to engage with the grid session. In one scenario the participant, appeared to be highly fatigued (due to an excessive workload at the time) and although they did provide some, they failed to produce a high number of constructs. In the other case, despite repeated prompting on how to explore the topic, and how to complete the grid the participant simply “did not get it” (verbal quote from participant ymo33). This highlights the differences in individuals understanding of knowledge development, and provides a disadvantage in the use of this tool – whereby some participants may be unable, or unwilling to engage with the grid session.

An important aspect of the data collection process was to write down the experience after each session. This reflexive practice provided an opportunity to re frame the research methods and analysis as the project unfolded. The literature on repertory grid suggests a range of interview settings are considered acceptable, therefore, both individual and group sessions were set up during pilot and final data collection. However, following the completion of the grid within the live focus group setting (as requested by one organisation for convenience to participants), it was decided that this would be the least preferred environment for collection of future data (through reflection). It was found that it was difficult to administer laddering techniques in a group environment (whereby probing questions ‘why is this/that’ is used to elicit the meanings of the constructs fully i.e. to cluster constructs together or gain more detail on particular constructs). Following this live focus group, all future sessions were arranged on an individual basis. In addition, each grid was analysed on an individual basis immediately following the session, so emergent findings could be used to inform

future interviewees of similarities in constructs and elements they produced during future sessions.

All data was stored within an excel file and coded for anonymity. For the purposes of analysis the constructs were listed on one sheet, along with similarity scores. A drop down box was inserted for content analysis, which was populated with categories by each of the judges/raters<sup>89</sup> during content analysis (see Figure 21 for a screen shot of the analysis file in excel including drop down boxes).

**Figure 21** Screen shot of excel data file showing construct listing with drop down for content analysis (full and final list of categories/constructs in Appendix 7)



The decision to analyse everything electronically, differs from other researchers' interpretation of printing off constructs and sorting manually. This allowed for flexibility and ease of communication between the two judges/raters over email (see Section 7.3.1 for discussion of inter judge reliability).

## 6.6 Analysis of grid

There are a number of techniques that can be utilised to analyse individual repertory grids. Following the completion of data collection, the researcher attended a Northern Area Personal Construct Psychology (PCP) Group meeting<sup>90</sup>, and discussed the issue of analysis with some experienced researchers. For the purpose of this thesis, generally accepted methods of grid analysis have been adopted (as described in Jankowicz, 2004). Eyeball analysis is discussed under Section 6.6.1 which can be

<sup>89</sup> Content analysis was performed by two independent judges (the researcher and a colleague who carries out research in the same field), to increase reliability (see Section 6.6.3, and Section 7.3.1 respectively).

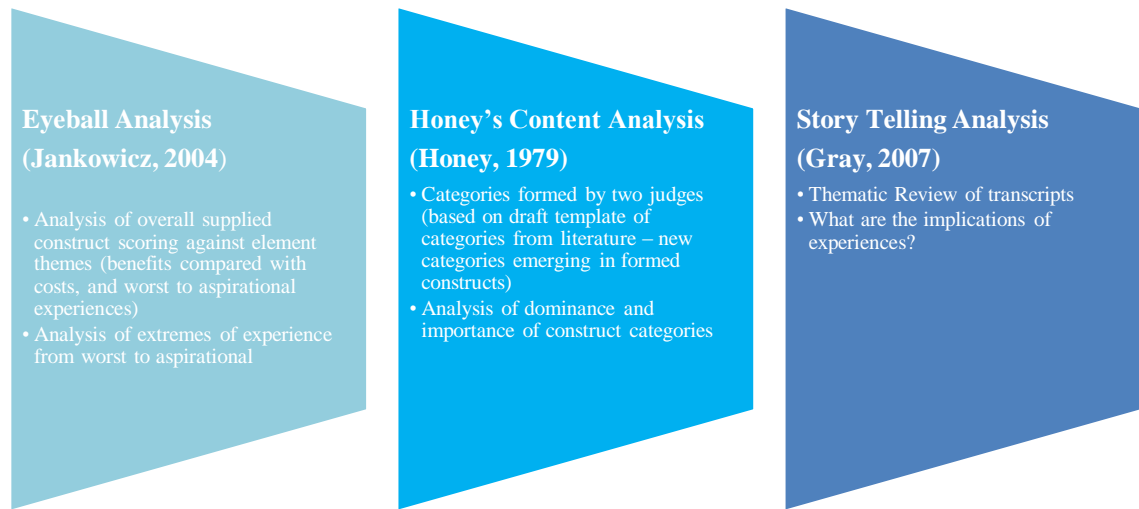
<sup>90</sup> The Personal Construct Psychology Group meets on a regular basis throughout the year, to discuss ongoing research interests. This group represents a broad range of academics who kindly offered advice on 'Kelly' and the direction of this PhD, which assisted completion of this analysis.

applied to any individual grid. This was applied after each session to identify if any of the grid output required immediate clarification. In addition, specific interrogations of 'worst' and 'aspirational' compliance experiences were explored under eyeball analysis (in order to review the constructs formed for the two extremes of compliance experiences explored). Under Section 6.6.2 Honey's Content Analysis is discussed. This form of content analysis has been chosen to link data output from the different sessions, by relying on the provision of an overall construct to all participants. The provision of the overall constructs of 'cost' and 'benefit' to the organisation allowed for analysis of the relative importance of each personal constructs to the individual, and organisations they serve.

Through discussion with more experienced members of the PCP group, it was understood that a greater understanding of the elements and the constructs elicited within the grids can be formed through more extensive analysis of interview transcripts (story telling), which enable theorising to be triangulated between data sets. For example, Honey's content analysis (Honey, 1979) was used in this case to develop categories and an understanding of the relative importance and dominance of categories. However, the results of the content analysis did not always align to the findings in the story telling – which allows for rigour in the research process whilst theorising. Indeed one of the main benefits of the story telling aspect of the grid was gaining insight on the implications that the range of experiences had on the individual (and the collective group). This was applied specifically to the eyeball analysis of grids when considering the benefits or costs associated with the extremes of their worst and aspirational compliance experiences. This was also acknowledged by the participants, during the sessions, where a number commented along the lines of "it's funny how it makes you think like that". This also supports Gray's (2007) comment with regard to the importance on such tooling to enable critical reflection. A summary of the stages of analysis is set out in Figure 22. This figure demonstrates the three distinct phases of analysis which will now be discussed in turn including; Eyeball analysis (Section 6.6.1), Honey's content analysis (Section 6.6.2), and the interview 'story telling' analysis (Section 6.6.4). The data findings are also presented under these three distinct techniques within Chapter 7.



**Figure 22 Stages of analysis performed within this study.**



### 6.6.1 Eyeball analysis

The way in which the repertory grid session is delivered ultimately focuses the analysis tools available to the researcher. However, irrespective of the other analysis decisions, Jankowicz (2004) recommend eyeball analysis to familiarise oneself with the content of the grid as a whole, prior to any other analysis. Eyeball analysis can be broken down into distinct stages (Jankowicz, 2004, p. 81):

- What is the interviewee thinking? – topic of grid, info on qualifying phrases;
- How has interviewee represented topic? – elements agreed;
- How does s/he think? – how many constructs/length of interview (more constructs indicate interest in topic/expertise/frequent exposure to topic);
- What does s/he think? – rating of elements (scaling used), anything obvious in matrix (although unusual);
- draw conclusions – summarise main points and observations.

In certain cases, it was clear using eyeball analysis that the interviewee had 'gone off script' and completed the grid incorrectly (for example, a problem encountered during group sessions due to the one on one feedback on the grid completion being lost in group environments). In these cases follow up emails/conversation were held on an individual basis to clarify and finalise the data within the grids.

Eyeball analysis of the grid provided a holistic view of the interviewees thought process, and allowed for analysis to explore the individual elements themselves (i.e. how interviewees were categorising their experiences from worst to aspirational) alongside a measure of how individuals considered experiences as benefits and costs.



A worked example of how constructs from the grids have been analysed is now presented for clarity. As discussed throughout this Section 6.6 and presented in Chapter 7, there have been three stages of analysis. The first two forms of analysis eyeball analysis, and Honey’s content analysis involved direct interrogation of the grids and elicited constructs.

The construct pair example chosen for illustration originates from grid G1 – IMC16, and is “broad range of stakeholders” compared with “relatively narrow range of stakeholders” which the participant has expressed to describe and contrast experiences for ‘a, b and d’ (see also Figure 17 which outlines full grid where Example a represents ‘Ideal/Aspirational’ compliance experience, Example b represents ‘straightforward/efficient compliance experience’, and Example d represents ‘relatively routine compliance with significant issues’). See Figure 23 below for extract from the grid<sup>91</sup>.

Figure 23 Extract from grid LMC16

| Your own words to describe scenario:  |                             |   |   |   |   |   |   | Date                                      |
|---|-----------------------------|---|---|---|---|---|---|---|
| Example a - 'Ideal/Aspirational' compliance experience  | Removing complexity         |   |   |   |   |   |   | 14/08/2013                                |
| Example b - straightforward/efficient compliance experience   | Improving reporting         |   |   |   |   |   |   | Participant Code:                         |
| Example c - routine compliance experience with minor issue  | Changing behaviour          |   |   |   |   |   |   | IMC16                                     |
| Example d - relatively routine compliance with significant issues   | Dealing with the regulators |   |   |   |   |   |   |   |
| Example e - compliance experience with major issues   | Regulatory investigation    |   |   |   |   |   |   |   |
| Example f - 'worst' compliance experience   | Legacy issues               |   |   |   |   |   |   |   |
| Ratings: '1' matches closely with left hand descriptor, '5' matches closely with right hand descriptor, '2,3,4' to rate between extremes. |                             |   |   |   |   |   |   |   |
| Note: you do not need to 'rank' you can use same scores for multiple examples if necessary  |                             |   |   |   |   |   |   |   |
| <b>Construct pair example</b>   |                             |   |   |   |   |   |   |   |
| Examples Compared   | Similar descriptor          | a | b | c | d | e | f | Dissimilar descriptor                     |
| a,b,d   | broad range of stakeholders | 1 | 5 | 1 | 1 | 1 |   | relatively narrow range of 3 stakeholders |

### 6.6.1.1 Application of Eyeball Analysis – exploration of aspirational experiences in contrast with worst experience (as per analysis in Section 7.2.2)

The construct pair above represents a comparison of an ‘a’ experience (ideal/aspirational compliance experience). Therefore, this construct was listed out separately (along with other ‘a’ experiences) for analysis purposes.

The construct listing of ideal/aspirational experiences was then reviewed manually and each of the constructs was allocated to one of the following listings:

Aspirational Descriptor - Positive connotation

<sup>91</sup> This represents only one construct formed by participant from the total grid for the participant for clarity. This particular grid in the analysis excel file ran to 33 rows, and in final analysis 38 columns wide, so it is not feasible to show the entire excel grid in the thesis itself.

Aspirational Descriptor - Neutral connotation

Aspirational Descriptor - Negative connotation

In this case there did not appear to be either a positive or negative connotation to the descriptor of 'broad range of stakeholders' and, therefore, the construct was added to the neutral connotation listing.

Once all of the 'a' construct descriptors had been allocated to a listing (positive, neutral or negative), each of the listings was then reviewed for 'themes' in the constructs. The themes allocated to the neutral connotation listing were: Process/Procedural (1), Relations and culture (2), Stakeholders/Involvement (3), Skills/Specialism (4). In this case the construct was allocated to the 'stakeholder/involvement' theme. This process was repeated for all constructs to form the results summarised in Figure 29 under Section 7.2.2.

### 6.6.2 Honey's content analysis

Content analysis has a long history within academic research (with analysis of symbols dating back to ancient Greece). It is a popular technique that has been adapted for use across research disciplines, and research philosophies through analysis of "the manifest and latent content" of bodies of data (Krippendorff, 2004). In early content analysis, there was a concentration of researchers studying the manifest content (literal content) of data e.g. quantitative newspaper analysis prior to and early in twentieth century concentrated on the frequency of subject matter. Bryman and Bell (2012) focus on "quantitative content analysis" based on reference to the work of Berelson (1952) and Holsti (1969), where content analysis can be defined as:

"An approach to the analysis of documents and texts that seeks to quantify content in terms of predetermined categories and in a systematic and replicable manner" (Bryman and Bell, 2012, p. 291)

However, during the course of the twentieth century, many researchers have started to adapt their research designs towards qualitative analysis of the latent content (underlying meaning) of the subject matter. Krippendorff (2004) offer an alternative and more flexible definition of content analysis due to fundamental disagreement with the quantitative focus of Berelson's (1952), and Holsti's (1969) discussion of content analysis, which highlights also the qualitative (inferences) value of content analysis:

“Content analysis is a research technique for making replicable and valid inferences from texts (or other meaningful matter) to the contexts of their use” (p. 18)

Easterby-Smith et al. (2012) contend that content analysis is more deductive than grounded analysis. The researcher is interrogating the data for “constructs and ideas that have been decided in advance” (p. 163). Template analysis (King, 1998; King, 2012) is considered to be a middle ground between content and grounded analysis, whereby the researcher will search for themes and patterns within the data.

Honey’s content analysis, which has been adopted in this thesis, could be argued to focus on the manifest content of the data. However, this is not in fact the case, as through the process of categorisation the researcher is required to consider the underlying meanings of the constructs in order to prepare and allocate appropriate categories for further analysis.

The principles of mixed methods research were applied within the content analysis of grids. As discussed further in Chapter 7, Honey’s content analysis was adapted to include an element of template analysis (using the template prepared during the pilots of this study for the first iteration of categorisation – see Table 10). The strength of this method was to identify hygiene type constructs and streamline the analysis process (see Section 7.3).

#### **6.6.2.1 Similarity Scores**

By supplying an overall construct using Honey’s content analysis technique, it is possible to label each elicited constructs and match the ratings to the overall construct, using percentage similarity scores. A score of 100% would indicate that ratings on the construct are identical to the ratings on the overall constructs, and decreasing percentage indicates that the ratings become less similar.

It is also possible to compare “personal metrics”, whereby each individual will have differing similarity scores (Jankowicz, 2004, p. 171). Certain individuals may display fairly narrow percentage similarity scores, whilst others may see many different and unrelated constructs related to the topic leading to a wider range of percentage similarity score. Honey’s technique acknowledges this issue of relative percentage

similarity scores, and, therefore, allows ranking of “high, intermediate or low (H-I-L)”<sup>92</sup> values or “top and tail data”<sup>93</sup> for each particular individual.

### 6.6.2.2 Honey’s Content Analysis Procedure

Jankowicz (2004) sets out the procedural steps of Honey’s content analysis (pp. 173-177). These steps are summarised below, with details of the application within this thesis using the same construct example (brought forward from Figure 23) for illustration purposes.

1. Obtain ratings on both supplied overall construct and elicited constructs against all elements;

The session grids were transferred into excel (including scoring). An extract of the individual participants grid LMC16 is shown in Figure 24, which shows the participants construct pair ‘broad range of stakeholders, in contrast with, relatively narrow range of stakeholders, and the scoring thereof, alongside the scoring for the supplied overall constructs ‘overall benefit to the organisation, in contrast with, overall cost to the organisation’. The reversed ratings are also shown in this extract highlighted in yellow for clarity when using the grid during analysis.

**Figure 24 Extract from grid LMC16, demonstrating construct 'broad range of stakeholders', and overall construct**

| Your own words to describe scenario:  |                                      |   |   |   |                               | Date       |
|---|--------------------------------------|---|---|---|-------------------------------|------------|
| Example a - 'Ideal/Aspirational' compliance experience  | Removing complexity                  |   |   |   |                               | 14/08/2013 |
| Example b - straightforward/efficient compliance experience   | Improving reporting                  |   |   |   |                               |            |
| Example c - routine compliance experience with minor issue  | Changing behaviour                   |   |   |   |                               |            |
| Example d - relatively routine compliance with significant issues   | Dealing with the regulators          |   |   |   |                               |            |
| Example e - compliance experience with major issues   | Regulatory investigation             |   |   |   |                               |            |
| Example f - 'worst' compliance experience   | Legacy issues                        |   |   |   |                               |            |
| Ratings: '1' matches closely with left hand descriptor, '5' matches closely with right hand descriptor, '2,3,4' to rate between extremes. |                                      |   |   |   |                               |            |
| Note: you do not need to 'rank' you can use same scores for multiple examples if necessary  |                                      |   |   |   |                               |            |
| Examples Compared   | Similar descriptor                   | a | b | c | Overall construct and ratings |            |
| a,b,d   | broad range of stakeholders          | 1 | 5 | 1 | 1                             | 1          |
|   | Overall benefits to the organisation | 1 | 2 | 1 | 3                             | 4          |
|   | Overall cost to the organisation     | 5 | 4 | 5 | 3                             | 2          |
|   | Reversed Ratings Overall             | 5 | 4 | 5 | 3                             | 2          |

2. Compute sum of differences (SOD) for each construct against the overall construct – comparing relationship of each individual elicited construct to the overall construct;

- a. Calculate sum of difference between overall construct and first construct

<sup>92</sup> During analysis ‘I’ or ‘intermediate’ was replaced by ‘M’ or ‘medium’, simply for ease of reader differentiating in tables/excel workings between I and L during analysis – this is a minor adaptation due to preference of researcher reading small text throughout analysis process.

<sup>93</sup> As described in Jankowicz (2004, p. 171), the allocation of H/I/L is performed manually for each individual grid, quoting Honey who described this as top and tail data (high similarity score to low similarity scores).

b. Calculate sum of difference between overall construct (reversed) and first construct (unreversed)

c. Note the smaller of the two sum of differences

These steps were performed using excel formula set up at pilot analysis stage.

For the illustrated example, this worked out (in excel) as SOD 10 and Reversed SOD as 14. Therefore, SOD of 10 was taken forward in the calculation for similarity score.

3. Turn the sum of differences into percentage similarity scores, to ensure comparability with other grids (again performed using excel formula set up at pilot analysis stage using Jankowicz's (2004, p. 115) formula of  $100 - ((SD / (LR - 1) \times E)) \times 200$ , where SD is sum of differences, LR is largest possible score, and E is number of elements);

This applied to grids formed in this research as  $=100 - ((AK24 / ((5 - 1) \times 6)) \times 200) = 16.6\%$  as a similarity score for this construct (where AK24 was the cell calculating SOD as 10 as per Step 2).

4. Consider the individual's personal metric, using the percentage similarity scores;

This involves manual review<sup>94</sup> of individual grids overall scoring (which is a range of similarity scores).

5. Label each construct with both indices of percentage similarity score and H-I-L (High, Intermediate or Low) transferring each construct onto a separate file card, and coding with interviewee detail;

With a score of 16.6% this construct was allocated as a 'low' (L).

Following calculations of SOD, similarity score and allocation of H-I-L, all construct details were then transferred to a separate sheet in excel (the construct log), to detail participant code, experiences compared, construct details, SOD, percentage similarity and HIL rating (as per

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<sup>94</sup> See also Footnote 85. The allocations of H/I/L is performed separately for each individual grid, depending on the range of similarity scores within each individual's grid.

Figure 25).

Figure 25 Extract of construct log details

| Participant Log | Experiences compared | Construct                   | Construct Pole                          | SoD | % Similarity | HIL Rating |
|-----------------|----------------------|-----------------------------|---|-----|--------------|------------|
| lmc16           | a,b,d                | broad range of stakeholders | relatively narrow range of stakeholders | 10  | 16.7         | L          |

6. *Identify categories;*

Initial categories were developed from the template designed at the pilot stage from the literature. Two judges (the researcher, and a colleague with an interest in the research specialism) met and discussed these categories as an appropriate starting point and allocated the construct log listing to the categories in excel. An additional category of 'other' was used where the judges did not consider any of the descriptors fell into the category template.

An extract of the judging template which listed out all of the constructs and the options of categories is shown in Figure 26, with the illustrative construct highlighted.

Figure 26 Extract of judging sheet for allocation of categories

| Descriptor - Pole 1                     | Descriptor - Pole 2                     | Category   |
|---|---|--|
| Time consuming                          | not time critical, not time consuming   | Resource - cost vs. benefit, monitoring of resources.    |
| external pressure                       | internal desire to change               | Reputation/ Best practice consideration/Proactivity of M |
| potentially serious consequences        | consequences are less impactful         | Regulatory risk  |
| financial impacts                       | little direct financial input           | Regulatory risk  |
| direct reputational impact              | some limited impact on reputation       | Reputation/ Best practice consideration/Proactivity of M |
| longer 'term' issue                     | short term                              | Reputation/ Best practice consideration/Proactivity of M |
| concerned with organisational culture   | process/format point                    | Ethics and Culture                                       |
| emotional element to delivery           | more factual/straightforward            | Stakeholder Considerations - Input from external depart  |
| complexity - many inputs with diversity | relatively straightforward              | Education and Training                                   |
| organisation wide                       | contained in compliance                 | Stakeholder Considerations - Input from external depart  |
| complex stakeholders                    | limited local stakeholders              | Stakeholder Considerations - Input from external depart  |
| broad range of stakeholders             | relatively narrow range of stakeholders | Stakeholder Considerations - Input from external depart  |

7. *Allocate constructs to categories;*

The judges met after the first round of judging and clarified categories, and discussed/re-performed steps 8/9/10 for each round of judging until appropriate levels agreement were reached.

8. *Tabulate results;*

The full listing (and each round of iteration of judge allocation to categories) was recorded in excel. An extract is included in

Figure 27.

Figure 27 Extract of table of judge allocations

| Descriptor - Pole 1                     | Descriptor - Pole 2                     | Judge 1<br>Category                        | Judge 2<br>Category                        |
|---|---|--|--|
| Time consuming                          | not time critical, not time consuming   | Resource - cost vs. benefit, monitoring of | Resource - cost vs. benefit, monitoring of |
| external pressure                       | internal desire to change               | Reputation/ Best practice consideration/   | Reputation/ Best practice consideration/   |
| potentially serious consequences        | consequences are less impactful         | Regulatory risk                            | Regulatory risk                            |
| financial impacts                       | little direct financial input           | Regulatory risk                            | Regulatory risk                            |
| direct reputational impact              | some limited impact on reputation       | Reputation/ Best practice consideration/   | Reputation/ Best practice consideration/   |
| longer 'term' issue                     | short term                              | Reputation/ Best practice consideration/   | Reputation/ Best practice consideration/   |
| concerned with organisational culture   | process/format point                    | Ethics and Culture                         | Ethics and Culture                         |
| emotional element to delivery           | more factual/straightforward            | Stakeholder Considerations - Input from    | Stakeholder Considerations - Input from    |
| complexity - many inputs with diversity | relatively straightforward              | Education and Training                     | Education and Training                     |
| organisation wide                       | contained in compliance                 | Stakeholder Considerations - Input from    | Stakeholder Considerations - Input from    |
| complex stakeholders                    | limited local stakeholders              | Stakeholder Considerations - Input from    | Stakeholder Considerations - Input from    |
| broad range of stakeholders             | relatively narrow range of stakeholders | Stakeholder Considerations - Input from    | Stakeholder Considerations - Input from    |

9. Establish the reliability of the category systems (using third party judge, to assist with steps 6 to 8);

See Section 6.6.3 below.

10. Summarise table by defining the category headings;

The category table was discussed between judges and defined at each stage (i.e. including comments on which types of constructs to include in categories, as discussed at each iteration) – see extract below Figure 28.

Figure 28 Extract of category table (template) including name of category, and the poles of constructs from literature review and judges' comments on inclusions

|   | Positive aspects                                | Negative aspects                              | Link to literature  | Comments: To include.....  |
|---|---|---|---|--|
| Stakeholder Considerations - Input from external departments/resource/consultants. Inhouse vs. shared services/outsourcing considerations | Extensive investment of IT compliance resources | Minimal investment in IT compliance resources | Bamberger (2010), Gable (2005), Garcia (2004), Mainelli and Yeandle (2006), Hussein and Hussan (2008) | Organisation wide vs. 'in' compliance, stakeholders, Emotion?, Consultants, IT/system change requirements. |
|   | Internal centre of excellence                   | External centre of excellence                 | McIvor and McCracken and McHugh (2011)  |  |

11. Summarise the table, finding examples of each category heading;



a. *Within each category order constructs from top to bottom with respect to percentage similarity scores (i.e. at top those with near identical scores, and at bottom those with lower similarity scores)*

b. *Looking at all constructs within a category, identify personally salient constructs on which there is group consensus (i.e. where H-I-L indices are high, the construct is important to the sample of participants, where H-I-L indices are mixed this shows there is no particular consensus indicating ambivalence about the importance/relevance of the construct, and if H-I-L is low this indicates that the construct does not relate particularly well to the topic in general)*

c. *If subthemes are identified within the category, group according to meaning being expressed*

This was performed manually in excel, there were no further subthemes identified, following the extensive discussions between judges in category formation in steps 6-8)

12. *Summarise table, stating frequency under category heading i.e. how many constructs per category/subcategory;*

See Appendix 7 for a full listing on constructs allocated within each category, and a summary below in Figure 29. In the full listing in Appendix 7 the percentage similarity between the individual construct and the overall construct is stated (from Step 3), and the allocation of H-I-L for each construct is stated (from Step 5) above. In the summary below the average percentage similarity score for constructs allocated in the category is recorded. In addition, a manual review of all constructs allocated to each category was performed (as per Step 4, and Step 5) and an allocation of H-I-L has been recorded for each category.

**Figure 29 Picture of summary table of constructs formed in excel (full list in Appendix 7)**

| Categories  | Number of paired constructs | % Constructs | % Similarity | HIL Value |
|---|-----------------------------|--------------|--------------|-----------|
| Resource - cost vs. benefit, monitoring of resources.   | 15                          | 13           | 38           | M/H       |
| Education and Training  | 11                          | 10           | 27           | M         |
| Ethics and Culture  | 6                           | 5            | 36           | M         |
| Reputation/ Best practice consideration/Proactivity of Management   | 15                          | 13           | 37           | M         |
| Skills and Status of Compliance - experience, knowledge, education and hierarchy within organisation  | 3                           | 3            | 11           | L         |
| Stakeholder Considerations - Input from external departments/resource/consultants.  |                             |              |              |           |
| Inhouse vs. shared services/outsourcing considerations  | 18                          | 16           | 33           | M         |
| Communication and Knowledge Sharing   | 4                           | 3            | 33           | M         |
| Regulatory risk   | 8                           | 7            | 36           | M         |
| Principles vs. Rule Based - spirit vs. letter of law (judgement)  | 9                           | 8            | 54           | H         |
| Barriers to compliance - internal processes and procedures issues not addressed in above categories (i.e. not ethics/culture, skills, resource) | 14                          | 12           | 41           | M/H       |
| Nuisance/Inefficiencies   | 9                           | 8            | 59           | H         |
| Ritualism and Gaming  | 3                           | 3            | 33           | L         |

13. Complete differential analysis as required for the investigation (in terms of demographics of sample);

Importance and dominance of constructs was assessed for each of the construct categories. See Section 7.3.4 and 7.4.5.

As discussed above, a critical step is identifying and allocating to categories (which is effectively steps 6 through to 10 described above), hence the nature of using a third party to confirm this process. Categorical distinction allocates the constructs by “their membership in a class or category, by their having something in common” (Krippendorff, 2004, p. 105). However, this is also similar in definition to thematic distinction, albeit this relates to “combinations of categories” (Krippendorff, 2004, p. 107). Due to the similarities and merge of definitions of allocating to categories by judges, the importance of reliability of content analysis is discussed briefly in Section 6.6.3, and in further depth within the Chapter 7.

### 6.6.3 Reliability and validity of content analysis

Content analysis needs to be reproducible to make sense to other people, and, therefore, it is essential that a reliability check is incorporated within the analysis. To be clear, this is not in reference to the reliability of the grids themselves as “there are many forms of grids with their own unique elements, constructs and scores” (Wright, 2009, p. 758). Reliability is discussed with reference to the content analysis performed on both the collective constructs and interview transcripts.

“Reliability refers to the consistency and stability of findings that enables findings to be replicated” (Burns and Burns, 2008, p. 410)

This takes place during the tabulation phase of analysis. For the purpose of this research a colleague was requested to independently identify categories, allocate constructs to categories and to tabulate the results. There are three types of reliability to consider: stability (the ability to code content in the same way over time); reproducibility (the extent to which coding is the same across multiple coders); and accuracy (by coding against predetermined standards). (Krippendorff, 2004) It is argued within this study, that the concept of stability conflicts somewhat with the philosophies of constructive alternativism, which would contend that stability is irrelevant in light of both participants and researchers' worldview adapting to the experiences through the passage of time (which ultimately would impact on the ability of coding in the same way over time, as new literature and experiences are undertaken).

However, the concepts of reproducibility and accuracy have been considered within this study. The extent to which the table of the author and the colleagues table agree indicates the reliability of the procedures. When measuring inter observer reliability, we are judging the extent to which the two judges agree, and thus we would rate the assessment more reliable if the judges are closely agreed (Burns and Burns, 2008, pp. 424-425). Reliability should not be confused with validity. Reliability is concerned with the accuracy and stability of a measure, whereas validity relates to how appropriate a measure is to assess the construct under observation (Burns and Burns, 2008, p. 425). Validity is concerned with truth and tests claims of the researcher, as opposed to evidence obtained independent of the research (Krippendorff, 2004, p. 212). Often in qualitative research validation takes the form of triangulation, which endorses credibility of the research findings by utilising multiple sources of data or methods (Stemler, 2001). Within this research, by performing content analysis on the constructs formed in the grid, and separate analysis of transcripts of open discussion, triangulation has been achieved. However, there is a complex relationship whereby unreliability limits the chance of validity, but also reliability does not guarantee validity (Krippendorff, 2004, p. 213). Assessment of inter judge correlations (including a discussion of measures including Cohen's Kappa and Krippendorff's Alpha) will be discussed further in the Findings and Analysis Chapter under Section 7.3.1.

#### **6.6.4 Analysis of interview transcripts**

As in Section 6.4.7, each session was recorded and transcribed. In the initial research design, the purpose of recording the interview was a failsafe, to ensure the reliability of

the data recorded within each grid i.e. to provide a greater understanding of the construct elicitation and meaning of constructs.

However, the importance of the interview transcriptions became clear for analysis early on in the process of data collection. The majority of participants found themselves story telling whilst constructing the grid, and so valuable data existed with the interview transcripts for analysis purposes (Gray, 2007).

As the interviews were unstructured by nature (due to the personal nature of grid formation), analysis was performed in separate stages. As discussed above (Section 6.4), where possible all of the participants were asked to consider broadly the three main themes reviewed during the literature search (new regulation, consulting and alternative options).

- What are the effects of changing regulation?
- When/How are consultants used?
- When/How are outsourcing/shared service options considered?

Codes were set up based on these specific questions within the initial coding of interview transcripts, allowing for specific analysis of the interview transcripts prior to immersion. This process was performed manually using tables in word (which was the preferred tooling due to ease of use and simplicity, compared to some application specific tooling such as Nvivo).

#### **6.6.5 Post analysis feedback**

Following analysis of the grid (as described in Sections 6.6.1 to 6.6.4, and presented in Chapter 7), a conceptual model was theorised through triangulation of the existing literature base and the data collated within this study (which is presented in Chapter 8). The development of the conceptual framework is presented in Figure 50 (at the beginning of Chapter 8), to represent the triangulation of the literature against the main findings of this study, to support the theoretical rationale for the emergent attributes of the model (see Table 22).

In order to reinforce reliability of data analysis and interpretation, the resulting model was sent out to the original participants, alongside a number of new contacts which were made following original data collection. It is argued that this aligns to the principles of the Delphi Method, whereby the overall purpose is to “develop a technique to obtain the most reliable consensus of a group of experts” whilst dealing with a

complex problem (Okoli and Pawlowski, 2004). A large majority of Delphi studies focus on ranking mechanisms to achieve consensus. However, for the purpose of this study the element of 'construct validity' has been explored most closely (Okoli and Pawlowski, 2004, p. 19), by revisiting the experts and asking them to validate the researcher's interpretation.

The decision was taken to distribute the conceptual model via email, which represents a form of e interview. By seeking feedback the emails represent an asynchronous interview technique, resulting in email exchanges between participant and researcher (Bampton and Cowton, 2002). The obvious advantage of this technique is the limited expenditure involved in furthering the research agenda (rather than revisiting each of the participants on site). This also acknowledges research ethics and the respect of individuals, as the participants could choose to ignore the email request for further feedback. In addition, the use of this technique avoided the data access concerns which were discussed earlier within this chapter, allowing participants to work around their own work schedules (Morgan and Symon, 2004).

However, the decision to obtain feedback was not without limitation. Meho (2006, p. 1292) contends that participants "may lose focus" or "drop out before the interview is complete". Therefore, the email request for feedback was designed carefully, to ensure that whilst enough information was provided for clarity, the email was suitably worded to capture the participants' interest. The language used within the email was also carefully adapted to avoid academic jargon, as the email was initially directed towards the practitioners who had contributed to the original data collection. A copy of the feedback email can be viewed in Appendix 2.

Despite this careful preparation of the feedback email interview, in practice the respondents did not always respond and provide feedback as expected, which again required the researcher to adapt and allow for flexibility of analysis (following principles of constructive alternativism). This is discussed further in Chapter 8, Section 8.3. For example, despite an ongoing dialogue with one participant over email to discuss feedback, the output of the emails was a telephone conversation for clarity in which notes were taken by the researcher. This again reflects the pragmatic nature of this research, as participants do not always act in the way that is commonly expected in the research process. This informal conversation (which ended up lasting over an hour long) resulted in a number of new dimensions that have been considered and presented in the final model under Section 8.4.

## 6.7 Reflections on limitations of methodology

As with any piece of research, there are a number of limitations to this study which are identified below.

Firstly, due to resource limitation of this research, data collection has been restricted to the UK banking industry. Therefore, this study does not claim generalisability to other regulatory/compliance sectors within the UK, and globally. It is arguable that generalisability will always be an issue in qualitative research. However, generalisability is restricted by the access constraints and the limited sample selected. The preference would have been to also include the financial regulator within the research process. Unfortunately this was not possible due to the timing of the research coinciding with the restructure of the FSA<sup>95</sup> to the PRA/FCA. Generalisability may have been furthered through an extended survey technique. This acts as a potential area of future research post submission. Reliability of content analysis should be rigorous due to use of inter judge/rater reliability (Section 7.3.1). In addition, the output of the analysis in the form of the conceptual model has been extended to further practitioners and academics for feedback (as discussed in Section 6.6.5), which counters the issues of generalisability to a certain extent (discussed further in Chapter 8).

Secondly, Personal Construct Theory is centred on the fundamental postulate and the corollary proposed by Kelly (set out in Appendix 3). The research veered away from the principles of the theory by providing certain constructs at pilot stage (and thus introducing researcher bias). Therefore, the research design was revisited (see also Figure 15) and a methodology applied which aligns to the original theory seeing man as the personal scientist with emphasis on individuality of constructs, whilst still allowing quantitative analysis through the methods applied by Honey. The same criticism could be said by providing general themes for elements to the participants. However, this research is not based on grounded theory, and, consequently, a basic structure to the grid was considered necessary to allow collective analysis of the resulting data (focussing on the commonality corollary and the range corollary).

In addition 'all of the answers' cannot be found through the adopted method of repertory grid. This has led to a modification in the research questions during the course of the research project. There is no possibility to delve into cost benefit analysis further which was desired at the project proposal phase. The largely inductive

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<sup>95</sup> As mentioned earlier the regulator was approached in the early stages of the research, but they declined to participate.

approach via repertory grid acts as a starting point for further deductive research into the topic in the future.

Finally, it must be acknowledged that the data produced by this methodology (alongside the majority of other academic studies) represents “manufactured” data (Silverman, 2013, pp. 31-55). However, it is argued that the issue of author bias has been considered throughout, and actively avoided through the elicitation of data driven by personal construct, and the nature of the open discussions.

## 6.8 Chapter summary

This chapter has introduced and justified the chosen methodological tool of repertory grid, as a means of exploring practitioners’ personal constructs. Evidence of the wide ranging use of repertory grid has been presented from the broader academic community (most notably from its roots in psychology). However, this methodological tool has rarely been used specific to regulatory compliance research. The use of the methodological tool and analysis thereon has been tailored distinctively for this study, and contributes to the regulatory compliance literature by exploring the linear models of compliance in comparison with practitioners’ constructs.

As evidenced in this chapter there have been iterations in the research design from pilot stage through to live data collection, to address limitations that were encountered on the research journey. Despite the issues with access, the flexibility of research design and chosen methodological tool has resulted in a rich data set that is presented in the next chapter. The next chapter is structured around the three forms of analysis of the grid and interview data, which was presented in Section 6.6.



## Chapter 7 Findings and analysis

### 7.0 Introduction

The purpose of this chapter is to present and analyse data collated through repertory grid sessions, and to examine the research questions identified within the methodology chapter. Table 14 summarises the research questions and relates these to supposition statements explored within this chapter, linking to the analysis performed, and the sections discussed. The supposition statements in Table 14 represent pre-supposed thoughts of the author from both prior practical knowledge, and the concepts identified within the literature reviews, prior to analysis of the data. These suppositions are revisited, alongside the main findings of the analysis at the end of this chapter in Table 21.

The data set for this thesis is collated from 12 participants (see also Section 6.5, Table 13). The average working experience of participants was 20.1 years, which indicates a rich, depth of experience (personal constructs) to draw from whilst undertaking the grid interview. During repertory grid formation, and comparison of participant's compliance experiences a key concern of practitioners' emerged around barriers to compliance.

This chapter has been split into a number of sub sections, which follows the distinct phases of analysis performed. In Section 7.1, through to Section 7.3, the analysis of grid data is presented to explore Research Questions 2a and 2b. The analytical framework adopted develops three levels of analysis with initial eyeball analysis of individual grids, followed by immersion and the application of Honey's content analysis on grid constructs. In Section 7.4, further analysis of interview transcripts is undertaken which enables exploration of Research Questions 1 and 3. In Section 7.5, concluding thoughts on the analysis are presented, including a summary of the main findings.

### 7.1 Data analysis of personal constructs

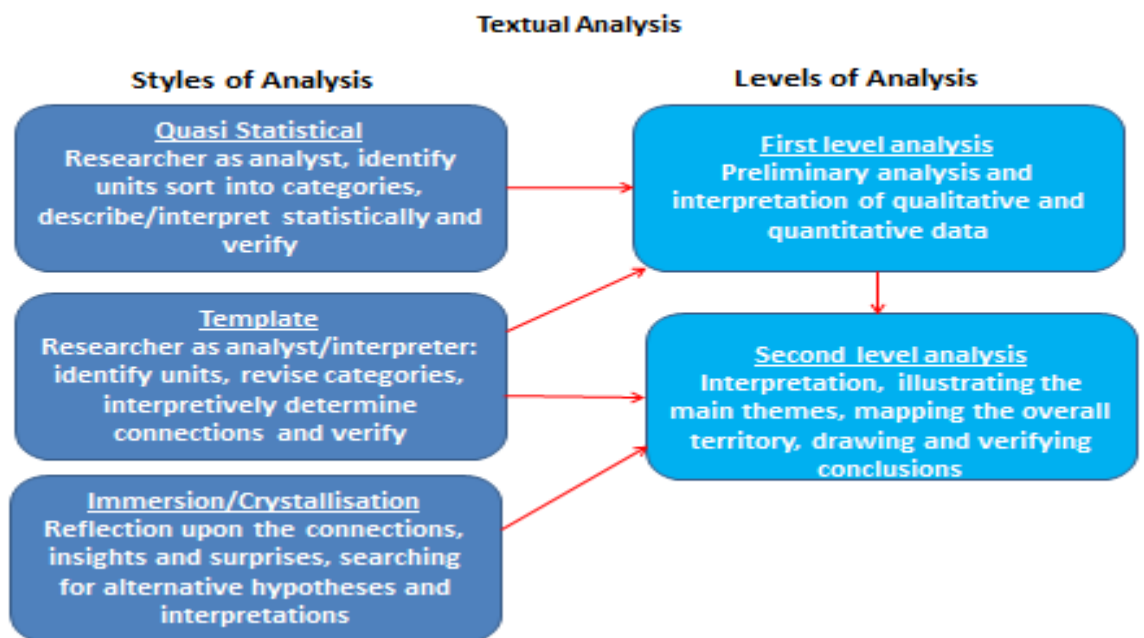
There are a variety of ways in which Personal Construct Theory is applied across differing disciplines (in terms of research methodologies and analysis). Indeed this was one of the main draws to the theory under a pragmatic logic. In discussion with members of the PCP group (see Section 6.6), a theme emerged of focusing on the story telling within personal construct theory and utilising repertory grid within an interview setting. Therefore, to justify the analysis techniques chosen, the main argument is that 'this naturally makes sense' (to the researcher) to analyse the story telling of the participants, contributing to richness of the data set.

**Table 14 Linkage between research questions and analysis of suppositions**

| Research question (RQ)   | Supposition statement   | Underpinning literature   | Analysis performed   | Analysis section |
|--|---|---|--|------------------|
| Research Question 1: To what extent does the regulatory cycle influence managements' decision making over compliance approach?   | Individual compliance officers prioritise workload around the regulatory approach (and the current regulatory risk appetite).   | Enforcement Pyramid (Ayres and Braithwaite, 1992). Section 3.3.1. Jackman's model (2001). Section 4.3.1.  | Interview transcription analysis.                                    | Section 7.4      |
| Research Question 2a: What are the key constructs that influence managers' decision of compliance function approach?   | No suppositions were made for content analysis of constructs.   |   | Honey's content analysis.  | Section 7.3      |
| Research Question 2a: What are the key constructs that influence managers' decision of compliance function approach?   | Aspirational compliance experiences may include an abundance of positive connotation within the descriptors, and that worst compliance experiences may include an abundance of negative connotation within the descriptors given by participants.   | Compliance model, relationship with regulator (Jackman, 2001). Section 4.3.1.   | Eyeball analysis of experiences (elements) and constructs formed.    | Section 7.2      |
| Research Question 2b: How do compliance officers' personal constructs align to academic models of compliance?  | If the scaling of aspirational compliance to worst compliance within the repertory grid were aligned to the linear scale of Jackman's model and contention of "an ethos of ethical compliance" and "unthinking mechanical compliance", the expectation would be for scoring of 1 for aspirational compliance (perceived as a benefit to organisation) and a scoring of 5 for worst compliance experience (perceived as a cost to the organisation). | Compliance model, relationship with the regulator (Jackman, 2001). Section 4.3.1.   | Eyeball analysis of scoring of constructs compared with experiences. | Section 7.2      |
| Research Question 3: In cases of new regulation, how do compliance functions rely on external expertise (consultants) or is there proactive promotion of in house knowledge and expertise? | The approach to new compliance is highly dependent on the resource constraints within the business.   | Consulting (Arnold, 2009); Gable, 2005). Concepts of centres of excellence via shared service, (Ulbrich 2006; Herbert and Seal, 2012). Chapter 5. | Interview transcription analysis.                                    | Section 7.4      |

Whilst acknowledging the themes identified through content analysis; the story telling and laddering of elements and constructs, by the interviewees recorded within transcripts supports the analysis of grid data (Kneiding and Tracey, 2009; Crudge and Johnson, 2007). The different forms of data (interview and grid data) have been analysed separately during first level analysis, and following immersion a secondary review has been undertaken to further identify patterns and themes identified within each data sets; relating to each other, and against the existing literature base (Waddington, 2005, see Figure 30).

**Figure 30 Analytical framework (developed by Waddington 2005)**



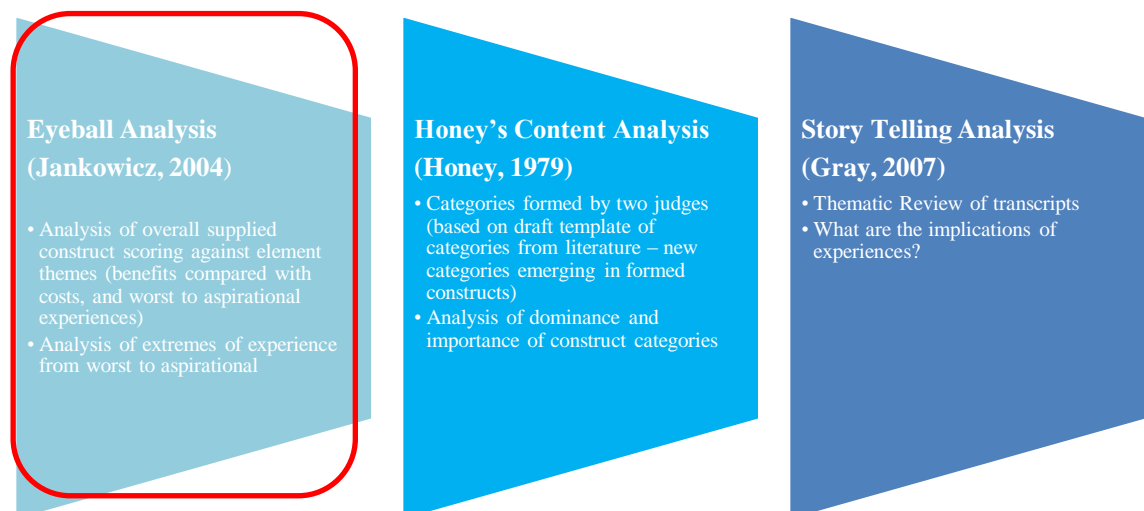
Prior to the presentation of findings, it is essential to revisit a fundamental aspect of Kelly's theory to demonstrate why constructs have been analysed within bipolar pairs. The meaning and understanding of constructs can only be explored fully in the context of the emergent and implicit pole (see dichotomy corollary which is detailed in Appendix 3). For example, the construct of 'good' could be coupled with a construct of 'poor' (in terms of applications skills to compliance processes), or 'good' could be coupled with construct of 'evil' (in terms of moral judgement over compliance decision making) (see also Dick and Jankowicz, 2001, p. 186). This highlights the importance of pairing of constructs for analysis purposes, to obtain an understanding of the participants construct system (see also discussion around Figure 34 and Figure 35, specific to this study).

In addition the importance of ‘types of constructs’ must be considered during analysis. Song and Gale (2008) summarise different categories of constructs; propositional constructs which describe easily observable properties of elements for example black/white; sensory constructs which describe how the person feels or perceives the elements for example hard/soft; and evaluative constructs which describes how the person evaluates the elements for example liked/disliked (adapted from Stewart, et al., 1981, p. 27). Jankowicz (2004, pp. 83-88) offers an extended and alternative categorisation of constructs; core constructs are those which have deep and personal (central) significance to the interviewee (what they value in existence), whilst peripheral constructs summarise feelings and knowledge of less important items; propositional constructs offer basic (often superficial) characteristics of elements, leading to narrow and over specific ranges of convenience, whilst constellatory constructs imply an overarching position of an element, which then allows you to construe from that position (characterised by stereotyping). Other types of constructs described by Jankowicz include; affective (expressing emotion/feeling), behavioural (what elements do), evaluative (opinion/assessment provided), attributional (includes reason for behaviour), and finally, unremarkable (limited implications). The importance of characterising/categorising/classifying constructs is most relevant when considering the analysis of grids.

## 7.2 Eyeball analysis design

The first step of analysis involved eyeball analysis – simply looking at the grids themselves. Figure 31 highlights this first distinct phase of analysis which is presented within this section.

**Figure 31 Distinct phase of analysis (Eyeball Analysis) – figure brought forward from Methodology Chapter, Section 6.6**



Eyeball analysis would usually be restricted to single grids to familiarise oneself “with what’s there” (Jankowicz, 2004, p. 80). However, due to the commonality of the overall supplied construct (see Methodology Chapter, Section 6.4) within each grid, specific focus was given to the scoring by each individuals experience against the concept of overall benefit, in contrast with, overall cost to the organisation. Using this common feature of each grid, the scoring of the supplied overall benefit, in contrast with, overall cost construct was analysed. For this one construct it can be assumed that the scoring acts as a rating scale and average (mean) score may be analysed (Jankowicz, 2004, p. 145).

Eyeball analysis followed three distinct routes, which are unique in nature due to design of the repertory grid explored within this study:

1. An exploration of benefits and costs scoring (Section 7.2.1);
2. An exploration of aspirational and worst compliance experience (Section 7.2.2);
3. And finally a general review of all of the participants experiences – the elements (Section 7.2.3).

The reason analysis has been performed in this manner is to ensure that full consideration of individual experiences (elements) are taken into account within the findings (as the second stage of content analysis, in Section 7.3, will only consider individual constructs).

However, prior to analysis the following limitations are identified. The concepts of benefit and cost are open for interpretation by each individual. In addition, although elements are themed from aspirational to worst experience (see grid template outline, including element themes in Figure 17), each individual’s experiences are standalone.

An extended discussion was held with one participant about ‘from who’s viewpoint’ benefits and costs should be considered. The argument being that in the case of a morally corrupt organisation, then there would be benefits in terms of saved resource/personal benefits being achieved for poor compliance behaviour and so the interpretation of benefits and costs would be skewed when full disclosure about morally corrupt behaviour was not public knowledge. For the purpose of the interview the assumption was taken that information would be publically available for assessing overall benefit/costs – whilst acknowledging that in ‘real world’ practice this would not always be the case with some companies “getting away with murder... under the radar” Participant OMC20.

“So to them, the benefit is huge...it only becomes a cost when they are discovered” Participant OMC20

### 7.2.1 Exploration of benefits in contrast to costs

The following supposition was made prior to analysis (see Table 14 for link to research question and underlying literature):

If the scaling of aspirational compliance to worst compliance within the repertory grid were aligned to the linear scale of Jackman’s model (Figure 32) and contention of “an ethos of ethical compliance” and “unthinking mechanical compliance”, the expectation would be for scoring of 1 for aspirational compliance (perceived as a benefit to organisation) and a scoring of 5 for worst compliance experience (perceived as a cost to the organisation).

The average rating scale for overall benefit, in contrast to, overall cost to the organisation is summarised in Figure 33. This was derived from collating the ratings allocated by each participant against the overall benefit, in contrast to overall cost construct in individual grids, and taking an average of the ratings (a mean score).

Figure 32 Jackman’s model (see also Chapter 4)

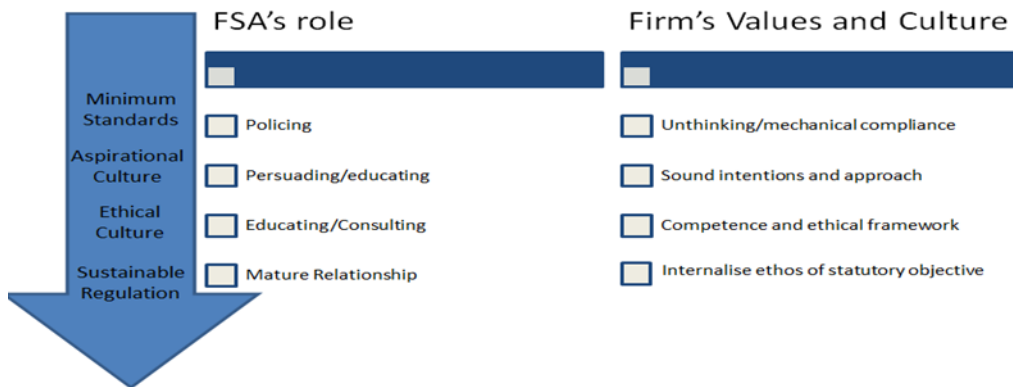


Figure 33 Summary of analysis table - mean scores for overall supplied construct (benefit/cost to organisation) in comparison to experience themes

| Overall benefit/cost to the organisation | Example a - 'ideal/aspirational' compliance experience | Example b - straightforward/efficient compliance experience | Example c - routine compliance experience with minor issue | Example d - relatively routine compliance with significant issues | Example e - compliance experience with major issues | Example f - 'worst' compliance experience |
|--|--|---|--|---|---|---|
| Average Score                            | 1.42   | 1.92  | 2.92   | 2.92  | 3.17  | 4.50                                      |

The mean score represents how closely (on average scoring) the participants consider the experiences are aligned to the overall benefit/cost construct. The expectation would be for scoring of 1 for aspirational compliance (perceived as a benefit to organisation) and a scoring of 5 for worst compliance experience (perceived as a cost to the organisation). Under eyeball analysis of the mean scores (see Figure 33) assigned by the 12 individuals in this study the supposition does not hold entirely true. The reasons for this can be explained by the verbal musings of the participants when scoring the grids. Statements were made by individuals, suggesting that whilst worst experiences are generally accepted as undesirable, individuals and organisations did gain some benefits in the form of learning, and improvements made following events.

“we learnt something from that as a business [...] it meant that people were more aware...It was still a cost, but there was learning, and good knowledge came out of the experience” Participant JMC10

In contrast, ideal/aspirational compliance experiences did not always correlate fully to benefit the organisations. For example when describing the reasons why an efficient compliance experience was seen as more of a cost rather than a benefit, and an experience with significant issues was seen more as a benefit than a cost the following was stated:

“albeit it was the hardest and least pleasurable experience...but that was the one, had it not been managed correctly, would have been the most unfortunate... let’s put it that way shall we...this one made money, but this one could have cost a lot more...” Participant VMLA19

Experiences with minor to significant issues were scored neutrally by the participants between 2.92 and 3.17 (see average mean scores of overall supplied construct, summarised in Figure 33). This indicates that both benefit and costs were seen to result from these experiences in equal/neutral measure. An example of this was evidenced when discussing a process viewed as having major issues with one participant. They discussed a scenario where processes were changed to meet regulatory requirements:

“it was quite engineered to be honest, so if you had to compare the cost of running it, to the benefit of putting it in place then net you are down...over time I am sure you would recover it....so let’s put a 3” Participant RM020



These results indicated that simple linear scales within academic model cannot easily be transferred to practice<sup>96</sup>. Jackman's model did not directly incorporate cost and benefit considerations to his extremes of the compliance approach, and this is an area that needs to be further integrated to understand the outcomes for compliance officers when approaching particular compliance issues. This links to the next section where the aspirational and worst extremes of compliance officer experiences are explored in further detail.

### 7.2.2 Exploration of aspirational and worst experience

The listings of constructs specific to aspirational and worst compliance experience were also reviewed under eyeball analysis to contribute to this discussion (by extracting constructs formed during comparisons of these two extremes of experience from the overall listing<sup>97</sup>). This phase of analysis reflects Immersion/Crystallisation (Borkan, 1999) consisting of engagement and experiencing the constructs to identify patterns and themes and relationships (Waddington and Fletcher, 2005).

The following supposition was made prior to analysis of constructs relating to aspirational and worst experiences (see Table 14 for link to research question and underlying literature):

Aspirational compliance experiences may include an abundance of positive connotation within the descriptors, and that worst compliance experiences may include an abundance of negative connotation within the descriptors given by participants.

However, this was not observed on review of the grid outputs. The constructs formed when comparing aspirational and worst compliance experiences were manually reviewed and sorted into three categories of positive, neutral and negative connotation. Each category (positive/neutral/negative connotation) was then reviewed for themes. This was performed prior to any other content analysis of the full construct set. The result of this analysis is summarised in Table 15 and

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<sup>96</sup> For example, Jackman's model is linear in nature from unthinking compliance (or minimal compliance) to ethical compliance (i.e. beyond compliance), and Ayres and Braithwaites' Enforcement Pyramid is also linear in design from self-regulation (i.e. fairly hands off by regulator) to command and control (i.e. sanctioning and heavy involvement from perspective of regulator).

<sup>97</sup> Within excel, all constructs which had been used to describe 'aspirational compliance' and 'worst compliance' experiences were separately listed for analysis purposes. Aspirational compliance construct descriptors were then categorised under 'positive, neutral and negative' based on individual descriptions. The same process was performed for worst compliance construct descriptors. The 'positive, neutral and negative' categories were then analysed to consider whether themes existed within the descriptions. See worked example in Section 6.6.6.1.

Table 16.

Table 15 Constructs elicited from practitioners to describe aspirational compliance experience, interpreted as positive, neutral and negative connotation, and allocated to themes

| Aspirational Descriptor - Positive connotation   | Aspirational Descriptor - Neutral connotation  | Aspirational Descriptor - Negative connotation                                   |
|--|--|--|
| organisation wide (1)  | longer 'term' issue (4)  | complexity - many inputs with diversity (8)                                      |
| skilled judgement and expertise required (2)   | concerned with organisational culture (5)  | complex stakeholders (8)   |
| done daily (3)   | emotional element to delivery (5)  | uncertainty of results/delivery (9)  |
| training provided (2)  | broad range of stakeholders (6)  | risk involved in making progress (10)  |
| clear process (3)  | emotional debate (5)   | complexity of delivery (8)   |
| assists (3)  | seniority of management input (6)  | lengthy process (11)   |
| enhances image of organisation (3)   | customer facing process (4)  | difficult to implement (8)   |
| common sense approach (3)  | non lending process (4)  | too many checks (11)   |
| efficient (3)  | info stored on bank systems (4)  | major system change required (11)  |
| good to deal with (3)  | in house (4)   | vague information (11)   |
| ease of use (3)  | procedural (4)   | commercial necessity (10)  |
| low risk as no penalties (3)   | opinion self-regulating (5)  | manual use (11)  |
| Compliance experience and competence (2)   | change process (4)   | Risk of legal exposure if it goes wrong (10)                                     |
| Judgement Required (2)   | deal with identification of customer (5)   |  |
| Skills (2)   | one off project (4)  |  |
| Saved money/made money (3)   | project management required (7)  |  |
| Wholly driven by client (1)  | engages stakeholders with different skill sets (e.g. IT customer facing) (7)                                   |  |
| Front end development cost for later gain (3)  | specialised - starting from scratch (no starting point) (7)  |  |
| Skills required in creating system - experience (2)  | event (4)  |  |
| Close direct relationship with client (1)  | could outsource (7)  |  |
| Seen as exciting opportunity, positive (3)   | consultancy firm could do this (simple tasks, easy to spot mistake) (7)  |  |
| Potential to sell products/service (3)   | Bigger impact on non-compliance resource e.g. IT (6)   |  |
| Allocation of above construct to themes  |  |  |
| Themes: Involvement (1), Skills/Specialism (2), Perceived benefits - clarity, costs etc. (3) | Themes: Process/Procedural (4), Relations and culture (5), Stakeholders/Involvement (6), Skills/Specialism (7) | Themes: Complexity (8), Uncertainty (9), Risk (10) and Process inefficiency (11) |

When reviewing aspirational experiences constructs, the negative connotation is less common, and has been categorised (by the researcher) into the collective themes of: complexity; uncertainty; risk; and process inefficiency. Positive connotations are more common and have been categorised into themes of: involvement; skills/specialism; and perceived benefits - clarity, costs etc. Finally the neutral connotations have been reviewed into themes of: process/procedural; relations and culture; stakeholders/involvement; and skills/specialism.

This represents thematic analysis in its most simple form to demonstrate the first perceptions of the data output from the grid interviews (prior to more formal process of Honey's content analysis). The categorisation into themes was performed, and is subject to the individual researcher's literal interpretation and biases. However, the following observations (from analysis of Table 15) may be summarised from this initial analysis of aspirational experiences:

- Although experiences were perceived as aspirational by participants, negative descriptors exist within the constructs formed (third column of Table 15);
- A greater number of positive or neutral connotations exist (first and second column of Table 15) within the descriptors than negative connotation;
- Positive connotations are dominated by themes of perceived benefits, involvement and skills and specialism;
- Negative connotations are dominated by themes of complexity, uncertainty, and risk and process inefficiency.

At the other end of the scale of experiences, constructs used to describe worst compliance experience were also analysed in the same manner. It can be observed (in Table 16) that there are fewer positive connotations within the constructs formed on worst compliance experience. Nevertheless, those that result have been themed as; commitment to change, ease of change, integrity, perceived effectiveness. However, one of these themes may also be scaled as a negative connotation depending on the literal interpretation. For the individual constructs of 'personal integrity important factor' and 'personal integrity', both a positive and a negative connotation may be inferred from the reference to 'personal integrity' (see Figure 34, for reference of such constructs collated from practitioners). The scenario may have required personal integrity by individuals (compliance officers) involved, due to the lack of personal integrity demonstrated by others. Therefore, the viewpoint of observation is paramount

to how this construct may be interpreted as positive or negative. If a lack of personal integrity was evidence this would be viewed in a negative manner. Therefore, the constructs were considered compared to the contrast pole to assess whether these were to be reviewed in a positive or negative connotation.

**Figure 34 Example of construct pairs relating to 'personal integrity'**

|                                     |                                 |
|-------------------------------------|---------------------------------|
| Personal integrity important factor | Lower key - face less challenge |
| Personal integrity                  | Professional requirement        |

Therefore, personal integrity in these construct pairs demonstrate the issues/challenged faced by compliance officers during the experiences, in that personal integrity was seen as an important personal strength to approaching the experience (hence a positive connotation).

In contrast the negative connotations of the descriptors have been themed as; resource impact, perceived cost/inefficiencies i.e. reputation damage, direct costs, (lack of) skills/specialism, barriers/unwillingness to change/comply. If some of the descriptors underlying these themes are looked at in more detail, it may be seen that the compliance officers have little influence to change or impact the personal experience. That is to say, in these experiences the descriptors reflect the fact the compliance view it as 'out of their control' (see example of such a construct in Figure 35). This individual construct pair demonstrates a personal feeling that compliance could not have addressed the problem, due to circumstances outside of their control i.e. lack of staff resource.

**Figure 35 Example of construct relating to resourcing**

|  |  |
|--|--|
| Adequate resources in place to enable policies and procedures to be followed | Lack of key staff to identify and fix problems |
|--|--|

**Table 16 Constructs used by practitioners to describe worst compliance experience sorted into positive, neutral and negative connotations**

| Worst Descriptor - Positive Connotation | Worst Descriptor - Neutral Connotation    | Worst Descriptor - Negative Connotation   |
|---|---|---|
| internal desire to change (1)           | not time critical, not time consuming (5) | little direct financial input (8)         |
| wish to do (1)                          | consequences are less impactful (5)       | some limited impact on reputation (9)     |
| easy to implement (2)                   | non customer process (6)                  | done infrequently (8)                     |
| fully automated process (2)             | lending process (6)                       | little training provided (10)             |
| off shelf compatible software (2)       | non lending scenario (6)                  | different in each case (demographics) (8) |
| focussed (4)                            | non product specific (6)                  | unhelpful approach (9)                    |

| Worst Descriptor - Positive Connotation  | Worst Descriptor - Neutral Connotation  | Worst Descriptor - Negative Connotation   |
|--|---|---|
| Personal integrity important factor (3)  | no system storage required (5)  | inefficient (9)   |
| Personal integrity (3)   | similar volumes (5)   | unhelpful (9)   |
| Communication skills and effectiveness (4)   | security prevention issues (6)  | barriers to change (11)   |
|  | wide ranging project teams (7)  | bad experience (9)  |
|  | Directly involved regulator (7)   | no training (10)  |
|  | Objective is identity data collection (6)   | errors occurred (8)   |
|  | Process could be taught (6)   | major system development (9)  |
|  | Process based on factual data (6)   | one off implementation cost (9)   |
|  | Contact may be motivated by confidentiality (7)                                   | one off (9)   |
|  |   | high project cost (9)   |
|  |   | Senior individuals not wishing to follow a compliance agenda (11)   |
|  |   | Significant time expenditure (9)  |
|  |   | Different agendas - conflict (11)   |
|  |   | Morally corrupt (11)  |
|  |   | Ignoring policies and procedures where it suits (11)  |
|  |   | Lack of key staff to identify and fix problems (11)   |
|  |   | Focus on profit/income without any consideration for policies and procedures (11)   |
|  |   | Reports, complaints ignored at a senior level (11)  |
|  |   | No job satisfaction (9)   |
|  |   | Limited value (9)   |
| <b>Allocation of above construct to themes</b>   |   |   |
| Themes: Commitment to change (1), Ease of Change (2), Integrity (3), Perceived Effectiveness (4) | Themes: Resource impacts (5) Process/Procedural (6), Relationship/Involvement (7) | Theme: Resource impact (8), Perceived cost/inefficiencies - reputation damage, direct costs (9), (Lack of) Skills/Specialism (10), Barriers/Unwillingness to change/comply (11) |

The following observations may be summarised from this initial analysis and categorisation of worst experiences:

- Although experiences were perceived as worst by participants, positive descriptors exist within the constructs formed (first column of Table 16);
- Barriers were identified as a theme within worst experiences, indicating circumstances out of control of compliance officers impacting the situation;
- A greater number of negative or neutral connotations exist within the descriptors than positive connotation (second and third column of Table 16);
- Negative connotations are dominated by themes of resource impact, perceived costs and inefficiencies, lack of skills and barriers to change/comply;
- Positive connotations are dominated by themes of ease of change, integrity and perceived effectiveness.

If the negative connotations of both worst and aspirational experiences are combined you may consider that external drivers and uncertainties (perhaps outside the role of the compliance officers) are driving the negative aspects of the experiences i.e. Worst aligns to; resource impact, perceived costs and inefficiencies, lack of skills and barriers to change/comply: and Aspirational aligns to; complexity, uncertainty, risk and process inefficiency.

If the positive connotation both experiences are combined you can consider that confidence in own abilities and available external support is driving the positive aspect of the experience i.e. Worst = ease of change, integrity and perceived effectiveness; Aspirational = perceived benefits, involvement, and skills and specialism.

These construct themes would, therefore, support Jackman's model focussing on the firm's ethos, whereby the compliance officer is highly reliant on external support/drivers to deal with worst case scenarios. In order for aspirational compliance to be a positive experience, confidence in skills, integrity and external support are essential.

### **7.2.3 Eyeball analysis of elements formed for comparison of aspirational and worst experiences**

Eyeball analysis was also performed on the elements produced by each individual to assess whether commonality could be identified. The results of element elicitation are set out within Table 17 (with the highlighted extracts discussed in the following section).

The first observation is that the interpretation of aspirational to worst compliance experience is very personal to each participant (demonstrating the individuality corollary within Kelly's personal construct theorem – refer to Appendix 3). In addition it

should be noted that the way in which participant recorded elements was also very individual. For example, participants VMLA19 and YM033 wrote down significant narrative to describe very personal experiences. The majority of the other participants only wrote down a short sentence/a few words to prompt themselves to review each experience.

However, in the next stage of analysis (Section 7.3) through content analysis of the elicited constructs formed to discuss the range of experiences (and individual elements) the commonality corollary will be explored further.

A second observation is the importance of confidentiality which was witnessed in one participant (OMC20). This participant was seen to set out fairly generic descriptions to prompt himself to compare experiences. The elements were set out in a less personal fashion in contrast to other participants who provided specific named projects, persons, training course, pieces of regulation in order to represent their aspirational to worst compliance experience. However, participant OMC20 appeared to set out a linear scale of compliance approaches, which is similar to the scaling within academic models such as Jackman/Ayres and Braithwaite when discussing compliance/regulation. Later within the interview, the participant discussed participation within recent training so perhaps this had impacted on their current worldview when completing the grid process (applying experience corollary to element elicitation, within Kelly's theorem).

A final observation on the individual elements produced during interview is that one participant simply could not identify a personal experience that they considered as aspirational in nature. This participant (YFO0) was directed towards a prompt sheet of factors which may be considered as aspirational based on Jackman's model/definition of ethical compliance (in the absence of a personal experience).



**Table 17 Summary table of elements formed in participants' grids- aspirational to worst compliance experiences**

| Participant grid reference | Example a - 'Ideal/Aspirational' compliance experience                          | Example b - straightforward/efficient compliance experience  | Example c - routine compliance experience with minor issue                               | Example d - relatively routine compliance with significant issues | Example e - compliance experience with major issues  | Example f - 'worst' compliance experience                                |
|----------------------------|---|--|--|---|--|--|
| <b>LMC16</b>               | Removing complexity   | Improving reporting  | Changing behaviour   | Dealing with the regulators                                       | Regulatory investigation   | Legacy issues  |
| <b>YMO26</b>               | Morning Procedures  | Entry Control of personal information                        | Account opening  | Control of client monies  | Mortgage interview   | RMC contracts  |
| <b>YM012</b>               | NAMED PERSON - knows everything about asset finance                             | RMC unit 'point in time' commitment                          | Establishing increased facilities under guarantee (NAMED)                                | NAMED - process re 'advice'                                       | CIPL + BLP - making our regulatory reporting consistent  | Money laundering prevention unit exit customers                          |
| <b>YM033*</b>              | Risk procedures aspire to be perfect at completing forms/understanding concerns | Money Laundering unit experiences - efficient, knowledgeable | Risk assessment forms, taking on new clients - sourcing identity of funds deposited etc. | Credit courses significant issues if not adhered to               | Introducing and financial advice by Regulated Advisor - complexity misinterpretation constraints | Account opening for foreign nationals                                    |
| <b>YM027</b>               | Money laundering department   | NAMED compliance officer                                     | Notice withdrawal of   | CHAPS payment call back process                                   | Risk assessment forms - all products   | Trying to change process - several dept. involve/nobody taking ownership |
| <b>YFO0*</b>               | No experience to imagine!   | account opening  | current account mortgage review  | money laundering risk assessments                                 | financial difficulties training  | Mortgage example - no security in place, limit on a/c                    |
| <b>NMO28*</b>              | Electronic verification system implementation                                   | Control of personal information                              | Acceptable customer identification documents   | Transaction monitoring systems                                    | Sanctions checks   | Regulator 4 Document rule introduced 1996                                |
| <b>EFC10*</b>              | Creating KYC (know your customer) risk matrix                                   | Training   | Yearly DPA review  | Sanctions monitoring  | CDD (customer due diligence) project   | Run on bank  |

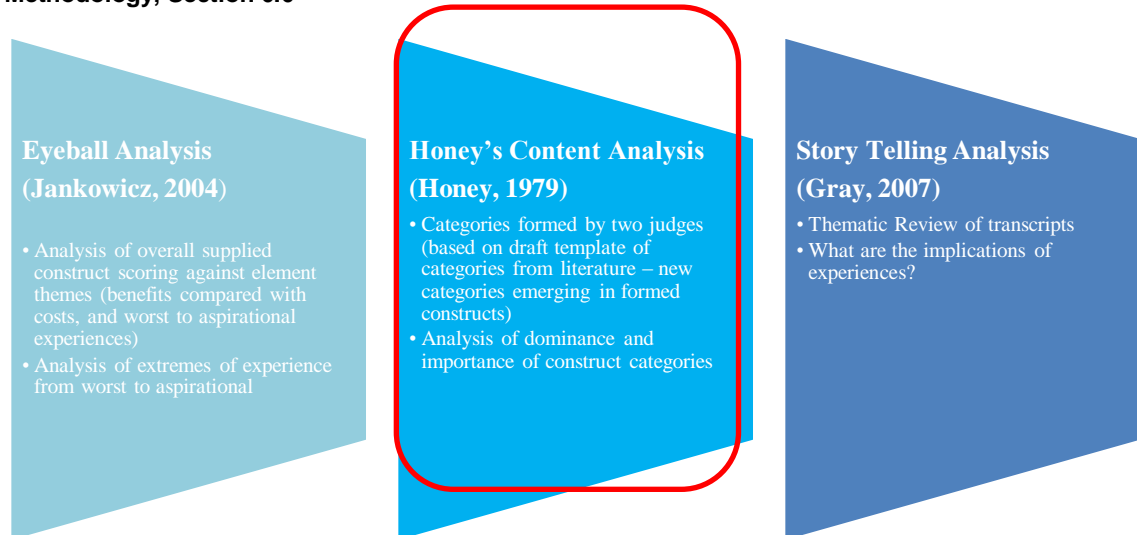
| Participant grid reference | Example a - 'Ideal/Aspirational' compliance experience  | Example b - straightforward/efficient compliance experience      | Example c - routine compliance experience with minor issue  | Example d - relatively routine compliance with significant issues                                | Example e - compliance experience with major issues                                      | Example f - 'worst' compliance experience   |
|----------------------------|---|--|---|--|--|---|
| VMLA19*                    | Piece of business which carried significant risk that was rejected in my absences by the business. On my return I was able to construct a risk management and mitigation plan that meant the business could proceed resulting in £400K p.a. Fee income. | Transactional deadlines - avoiding unnecessary steps and CDD.    | Company beneficial owners problem with due diligence certification standards "true likeness" not received | Identification of breaches - voluminous, relate to regulatory breach                             | Litigation Euro XM – Mis-sell, Conspiracy, Regulatory Body.                              | Being required to investigate a director and colleagues with regards to suspected insider dealings. |
| JMC10                      | Self-service CDD collation and automated screening  | Identifying individual investors and related form filling        | Understanding complex business rationale at time of take on   | Change in legislation surrounding reliance on another's CDD                                      | On-site inspection discovered failure to report third party fraud                        | Intermediary refusing to allow compliance access to investor data                                   |
| OMC20*                     | A good positive compliance culture  | Policies and procedures in place and desire to see them followed | Minor failings are identified but nothing is done to correct them (focus on income/profit)                | Policies and procedures routinely ignored and no effort made to address failings (by management) | Senior management ignore (and possibly encourage) compliance failings on a regular basis | Anything goes, no culture of compliance (anarchy)   |
| RM020                      | Implement fraud prevention programme  | Implementing "ICAAP"   | Risk assessing project leading to improved controls   | Implementing operational risk framework (BASEL II)   | Re designing plausibility limits for payments  | Job security threat   |

\*The elements formed by these individuals are discussed specifically earlier in Section 7.2.3.

### 7.3 Collective construct analysis - content analysis and Honey's content analysis

The steps for Honey's Content Analysis are set out within the methodology chapter under Section 6.6.2. Figure 36 highlights the second distinct phase of analysis which is presented within this section.

**Figure 36 Distinct phase of analysis (Honey's content analysis) – brought forward from Methodology, Section 6.6**



Reliability is an important aspect of content analysis. Therefore, a colleague was requested to independently identify categories, allocate constructs to categories and to tabulate the results. This colleague was chosen due to the nature of their prior practical experience, and their ongoing research interest within the regulatory/compliance field. The resulting categories, therefore, reflect both practitioner and academic viewpoints. The extent to which the table of the researcher and the colleagues (the judges) tables agree indicates the reliability of the procedures. Reliability is discussed under Section 7.3.1.

For the first round of allocating constructs from the grids, categories were developed from constructs found within the initial literature search. These construct categories were identified for the purposes of the pilot stage of interviews, when the intention was to supply certain constructs to the participants from the literature (see Methodology Chapter, Table 10 for listing). These constructs were formed by self-grid interview by the researcher following the review of the literature, to identify "hygiene factor" constructs which may form from existing literature base (Goffin et al., 2012). The idea of supplied constructs is supported by Goffin et al. (2012), where hygiene factors which relate to constructs which may be frequently mentioned by participants during interview

(as the factors are often referred to in academic and practitioner literature). As a modification to Goffin's technique, rather than supplying these hygiene factors in the interview itself, the judges used these as the basis of the first round of categorisation.

The judges used these categories to frame the first round of categorisation with any constructs considered not to fall under these areas allocated as other. The reasons for using this method was to systematically analyse the constructs formed by individuals versus the existing academic literature, and to easily identify any new emerging themes from construct elicitation. Using existing literature to review the initial categorisation identifies how strongly the constructs formed by the participants aligns to existing literature. Through categorisation into a category called other (i.e. constructs which do not fall naturally into categories from existing literature) allows for analysis of themes of importance to practitioners (to contribute to existing literature). Indeed, the principles behind this approach to initial categories may be likened to Template Analysis (King, 1998; King, 2012). The initial template/categorisation was formed from a priori knowledge of the literature (see Table 10, Chapter 6 Methodology).

Allocating constructs in this manner provided a practical process of analysis of categories for both judges. A deliberate choice to analyse categories using excel sheet listings (with 'drop down' boxes for categorisation of each construct) was made. The reason for this technique, rather than more traditional methods of paper on floor/printing off cards, was for the ease of the second judge to communicate results back to the researcher over e mail (and also the ensure a clean paper trail<sup>98</sup> exists of analysis).

### 7.3.1 Inter judge/rater reliability – tables of level of agreement

Agreement between judges during content analysis is widely considered to relate to reliability. However, this relationship is open to misconceptions.

“To be clear, agreement is what we measure; reliability is what we wish to infer from it” (Krippendorff, 2004a, p. 414)

Jankowicz (2004) contend that the most commonly used statistic for this context is Cohen's kappa. It is recommended to seek a figure of 0.8 or above to confirm reliability. However, there are criticisms of Cohen's kappa due to the “kappa paradox” whereby a low kappa value may be misleading, and so it is recommended to combine other statistical methods to confirm inter judge/rater reliability. Another commonly used

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<sup>98</sup> A separate excel sheet was used to record each iteration of the category formation, in the data analysis file.

statistic is Krippendorff's alpha in relation to content analysis inter judge/rater reliability. Krippendorff (2004, pp. 244-245) discusses the commonly used correlation coefficients within content analysis, concluding that their use can be seriously misleading.

Krippendorff (2004) argues that Cohen's kappa is concerned with the two individual observers rather than the population of data under observation, and hence the focus of reliability. Krippendorff (2004) also goes on to dismiss Cronbach's alpha as unsuitable for content analysis as "it was never intended to assess coding efforts" and acts as a correlation coefficient rather than an agreement measure. As Krippendorff's alpha is considered a suitable coefficient for measuring agreement within relatively small samples (Krippendorff, 2004a, p. 428), this coefficient is considered appropriate for this study, alongside the traditionally adopted Cohen's kappa.

With all reliability measures it is found that when agreement is observed fully, and disagreement is absent then the coefficient would measure 1, indicating perfect reliability. The majority of guides on Cohen's kappa consider that a score of 80% or more is required (Stemler, 2001; Jankowicz, 2004). There are three assumptions in using Cohen's kappa: firstly, the units of analysis are independent; secondly, the categories are also independent; and thirdly the judges/raters are operating independently (Stemler, 2001).

Krippendorff (2004, pp. 219-250; 2011) explains the use of Krippendorff's alpha and other coefficients in the attempt to endorse the use of alpha. The advantage of Krippendorff's alpha for this research thesis is the ability to expand the formula for "two observers" with binary data (Krippendorff, 2004, pp. 227-230; Krippendorff, 2011), via distinct executable steps (which were performed in excel manually). However, in order to address the arguments for each measure discussed above, both reliability measures have been calculated to combine the strengths of Cohen's kappa, and Krippendorff's alpha.

### **7.3.2 Reflections on first and subsequent round of categorisation**

Cohen's kappa and Krippendorff's alpha were calculated within excel, as described in Section 7.3.1 to review inter judge agreement. The first iteration of categorisation yielded poor similarity between the categorisation of the two judges (only 34 (30%) of the 115 paired constructs were allocated within the same categories by judges). This highlights the importance of assessing inter judge agreement for reliability purposes during content analysis (Krippendorff, 2004a).

The 'other' category was also reviewed within the first iteration of categorisation. The judges allocated 29 (25%) of the 115 paired constructs to the other category in the absence of a clear link to the hygiene categories developed from the literature. The judges then discussed the rationale behind allocation of constructs to the other category in order to identify suitable themes for new categories which had not been identified via the literature review/formation of hygiene categories. In addition the judges discussed the poor similarity achieved within first round of categorisation and agreed on appropriate definitions for each category.

Following each round of categorisation the two judges met to refine the descriptors of each category, and to discuss areas of non-agreement within categories. Following 3 rounds of categorisation (and subsequent discussion and refinement of categories) final overall agreement of allocation to categories was achieved with greater than 80% agreement across each category, under Cohen's kappa. Average agreement under each coefficient is summarised in Table 18 below:

**Table 18 Summary of agreement coefficients**

|  | <b>Cohen's kappa</b> | <b>Krippendorff's alpha</b> |
|--|----------------------|-----------------------------|
| Resource – costs and benefits, monitoring of resources.  | 96%                  | 96%                         |
| Education and Training   | 95%                  | 90%                         |
| Ethics and Culture   | 100%                 | 100%                        |
| Reputation/ Best practice consideration/Proactivity of Management  | 96%                  | 93%                         |
| Skills and Status of Compliance - experience, knowledge, education and hierarchy within organization   | 80%                  | 66%                         |
| Stakeholder Considerations - Input from external departments/resource/consultants. In-house, in comparison with shared services/outsourcing considerations | 97%                  | 94%                         |
| Communication and Knowledge Sharing  | 88%                  | 80%                         |
| Regulatory risk  | 100%                 | 100%                        |
| Principles, as opposed to, rule Based – spirit, as opposed to, letter of law (judgement)   | 89%                  | 81%                         |
| Barriers to compliance - internal processes and procedures issues not addressed in above categories (i.e. not ethics/culture, skills, resource)            | 91%                  | 85%                         |
| Nuisance/Inefficiencies  | 83%                  | 71%                         |
| Ritualism and Gaming   | 85%                  | 75%                         |

It may be noted that lower scores of agreement were recorded in certain categories under Krippendorff's alpha (even in final categorisation). However, this is attributed to

the lower numbers of constructs allocated within these categories which impacts on the score (see for example, Skills and Status of Compliance category, agreement of 66 per cent under Krippendorff's alpha – overall only 3 constructs allocated (which then impacts on the calculation due to the high level of unallocated constructs). To address this low level of agreement this category was appraised specifically and as the judges disagreed on one construct allocated to this category, this was then reviewed and allocated accordingly.

### 7.3.3 Final categorisation listing for analysis purposes

The summary listing of categories and allocation of constructs can be seen in Table 19. A full listing of constructs allocated within each category can be seen in Appendix 1.

**Table 19 Summary of final categories listing and allocations (see full listing under Appendix 1)**

| Categories   | Number of paired constructs | Allocated Constructs % | Similarity Score % | HML Value |
|--|-----------------------------|------------------------|--------------------|-----------|
| Resource – costs and benefits, monitoring of resources.  | 15                          | 13                     | 38                 | M/H       |
| Education and Training   | 11                          | 10                     | 27                 | M         |
| Ethics and Culture   | 6                           | 5                      | 36                 | M         |
| Reputation/ Best practice consideration/Proactivity of Management  | 15                          | 13                     | 37                 | M         |
| Skills and Status of Compliance - experience, knowledge, education and hierarchy within organisation   | 3                           | 3                      | 11                 | L         |
| Stakeholder Considerations - Input from external departments/resource/consultants. In house compared with shared services/outsourcing considerations | 18                          | 16                     | 33                 | M         |
| Communication and Knowledge Sharing  | 4                           | 3                      | 33                 | M         |
| Regulatory risk  | 8                           | 7                      | 36                 | M         |
| Principles as opposed to Rule Based - spirit as opposed to letter of law (judgement)   | 9                           | 8                      | 54                 | H         |
| Barriers to compliance - internal processes and procedures issues not addressed in other categories (i.e. not ethics/culture, skills, resource)      | 14                          | 12                     | 41                 | M/H       |
| Nuisance/Inefficiencies  | 9                           | 8                      | 59                 | H         |
| Ritualism and Gaming   | 3                           | 3                      | 33                 | L         |



The benefit of adopting an initial template during analysis allowed for direct links to be made back to the literature, and to highlight new emerging categories within the data set. If the final listing of categories is compared to the original template (see Methodology Chapter 6, Table 10) it is observed that a number of the categories have been combined during analysis i.e. reputation/best practice and proactivity of management are seen as one category (within Table 19) even though these might be considered as separate concepts within the literature. In addition three new categories are observed within the data set which were not identified in the literature at point of creating the initial template i.e. barriers to compliance, nuisance and inefficiencies, and ritualism and gaming.

#### **7.3.4 Analysis of categories with respect to dominance**

Tomico et al. (2009) analysed personal constructs across the discrete measures of “dominance, importance and descriptive richness”. Analysis of dominance and importance, involves quantitative analysis, whereas analysis of descriptive richness indicates latent meanings of constructs. In this section a quantitative review of dominance is presented in order to analyse and discuss the categories which reflect the foremost concerns of practitioners (and to consider the reasons why certain categories may not be of principal concern). The underlying meanings (and storytelling) behind experiences and constructs is explored in Section 7.4 via analysis of interview transcripts. Importance is related to the order in which constructs are elicited within each grid interview (Tomico et al., 2009). However, due to the nature of triadic elicitation adopted in method, elicitation order is not considered an appropriate measure for this analysis (as order of elicitation would be influenced by the order in which experiences are selected and compared). Instead, the relative importance is considered in relation to “similarity score” and allocation of “HML” indices under Honey’s content analysis (Jankowicz, 2004, p. 176), and this is undertaken in Section 7.3.5, where each category will be discussed in turn.

A category may be considered to be more dominant when it contains more constructs. Therefore, this simple metric has been summarised in Table 20 (in terms of ranking). The table indicates that there is a limited spread of constructs between categories (ranging from 3-18% of total constructs within each category), which suggests that practitioners’ construal systems are relatively broad, and do not offer headline issues when considering regulatory compliance. Instead there are a number of factors that are considered to be of importance. One significant finding is that the category of ‘barriers to compliance’ ranks within the top 5, representing other issues in achieving regulatory

compliance (i.e. in addition to issues such as ethics/resource constraints which are well documented in the literature).

**Table 20 Ranking of categories by dominance**

| Categories   | Number of paired constructs | % of total constructs | Rank <sup>99</sup> |
|--|-----------------------------|-----------------------|--------------------|
| Stakeholder Considerations - Input from external departments/resource/consultants. In-house compared with shared services/outsourcing considerations | 18                          | 16                    | 1                  |
| Resource – costs and benefits, monitoring of resources.  | 15                          | 13                    | 2=                 |
| Reputation/ Best practice consideration/Proactivity of Management  | 15                          | 13                    | 2=                 |
| Barriers to compliance - internal processes and procedures issues not addressed in other categories (i.e. not ethics/culture, skills, resource)      | 14                          | 12                    | 4                  |
| Education and Training   | 11                          | 10                    | 5                  |
| Principles as opposed to Rule Based - spirit as opposed to letter of law (judgement)   | 9                           | 8                     | 6=                 |
| Nuisance/Inefficiencies  | 9                           | 8                     | 6=                 |
| Regulatory risk  | 8                           | 7                     | 8                  |
| Ethics and Culture   | 6                           | 5                     | 9                  |
| Communication and Knowledge Sharing  | 4                           | 3                     | 10                 |
| Skills and Status of Compliance - experience, knowledge, education and hierarchy within organization   | 3                           | 3                     | 11=                |
| Ritualism and Gaming   | 3                           | 3                     | 11=                |

### 7.3.5 Analysis of categories with respect to importance

As presented in the Methodology Chapter (Section 6.4), an overall construct was provided to all participants during the grid exercise of overall benefit to the organisation, in comparison with, overall cost to the organisation. This allowed for analysis of similarity of scoring in comparison to elicited personal constructs. A score of 100% indicates that ratings on the construct are identical to the ratings on the overall construct, and a decreasing percentage indicates that the ratings become less similar (and for analysis purposes, less important) in comparison to the overall provided

<sup>99</sup> The highest ranking category in terms of dominance has the most constructs allocated within the category (with 1 denoted as highest).

construct of benefit/cost to the organisation. Jankowicz (2004, p. 176) sets out summary procedure for Honey’s content analysis, including the analysis of “mean importance scores” for each category. The similarity scores were presented in Table 19, and they have been ranked in order of importance in Section 7.3.5.1 to Section 7.3.5.4. During formation of construct categories the judges collated thoughts of positive and negative aspects of each category in the excel analysis file (to mimic the dichotomous nature of constructs formed by participants in the repertory grid interviews). These extracts are displayed in Figure 37 through to Figure 48. Each of these categories will now be discussed in turn.

### 7.3.5.1 Categories with ‘high’ importance

There were two categories with high allocations based on similarity score to overall construct: nuisance/inefficiencies, and principles, as opposed to rule based.

**Figure 37 Nuisances/Inefficiencies category**

|                         | Positive aspects   | Negative aspects  |
|-------------------------|--|---|
| Nuisance/Inefficiencies | Compliance is viewed as business enhancing. Enhances business. | Compliance is viewed as business inhibiting. Disrupts business. |

There were no initial links identified during literature review for categorisation of ‘nuisances/inefficiencies’ when reviewing models for regulatory compliance. This is perhaps because much of the literature is directed from a regulators’ viewpoint rather than the compliance officer’s viewpoint. Therefore, this demonstrates the importance of this categorisation identified within this study. Significantly, this categorisation also represents high importance to practitioners in relation to costs and benefits considerations. Examples of constructs allocated to this category include ‘common sense’ contrasted with ‘unhelpful’, ‘ignoring policies/procedures to suit’, ‘profits’ contrasted with ‘compliance’. The category is seen of significance as during the interview process these constructs were seen as outside of the control of compliance officers’ in most cases (and, therefore, perhaps of most importance to policy makers in their goals for regulatory compliance). It may be assumed that these constructs stem from perceptions of the organisations views on compliance being seen as a nuisance or business inhibiting. If these issues could become the focus of regulators, and better controlled (and tackled) by compliance officers’ working in the organisations, perhaps regulatory compliance may become more achievable in practice.

**Figure 38 Principles, as opposed to, rule based – spirit, as opposed to, letter of law (judgement)**

|  | Positive aspects               | Negative aspects                      |
|--|--------------------------------|---------------------------------------|
| Principles vs. Rule Based - spirit vs. letter of law (judgement) | Standardised approach/strategy | Flexible compliance approach/strategy |

The concept of the principles, as opposed to, rule based category stemmed from both prior working experience and the wider knowledge of literature from both accounting/corporate governance domains (e.g. compliance and ‘in control’ procedures under COSO, 2004). The discussion of principles, as opposed to, rule based is usually considered from a jurisdiction/regulatory perspective (i.e. UK in comparison to US approaches), however, in this categorisation the constructs were considered from an inside organisation perspective. Constructs included in this category represent a range of perspectives including: the judgement outlook of the compliance officers, for example ‘judgement’ contrasted with ‘black and white’, ‘routine’ contrasted with ‘one off’; to more process driven aspects for example ‘manual/automated systems’ and ‘too many checks’ i.e. tick box attitude. The significance of this categorisation is also echoed within the wider literature which discusses implications of spirit, as opposed to, letter of law.

#### 7.3.5.2 Categories with ‘high/medium’ importance

There were two categories which were seen as bordering between high/medium based on similarity score: resource, and barriers to compliance.

**Figure 39 Resource – costs and benefits, monitoring of resources**

|   | Positive aspects   | Negative aspects   |
|---|--|--|
| Resource - cost vs. benefit, monitoring of resources. | Compliance benefits perceived to outweigh costs – costs irrelevant<br>Compliance costs easily identifiable and monitored | Compliance Costs perceived to outweigh benefits<br>Compliance costs merged into ‘admin’ function of business – no monitoring |

The concepts within this categorisation represent a significant part of the regulatory literature (Satheye, 2008; Harvey, 2004; Deloitte, 2006; Ellihansen, 1998; Franks et al., 1998; Alfon and Andrews, 1993), and also feature as high/medium importance within the personal constructs of practitioners. Ultimately the running of the compliance and risk management functions are a cost base for any organisation. However, these costs are finely balanced to the benefits of being seen to be compliant (in its many forms i.e. reputation impacts, avoiding sanctions).

Examples of constructs allocated to this category include concepts of; time constraints, monetary costs, frequencies of processes, and adequacy of resourcing functions.

The second category that aligns in importance as M/H compared to the overall construct is that of 'barriers to compliance'. This category was also seen as a dominant area for construct formation. However, this category was not identified specifically during the literature review and the initial formation of the template for analysis. As is the case for the category nuisances/inefficiencies this may be attributable to the majority of literature being directed from a regulators' viewpoint rather than the compliance officer's viewpoint.

**Figure 40 Barriers to compliance - internal processes and procedures issues not addressed in other categories (i.e. not ethics/culture, skills, resource)**

|   | Positive aspects  | Negative aspects  |
|---|---|---|
| Barriers to compliance - internal processes and procedures issues not addressed in above categories (i.e. not ethics/culture, skills, resource) | Barriers have been identified and addressed within the organisation | Barriers have not been addressed leading to regulatory action, or limitations to business |

However, this category is distinct from the 'nuisances' category as the constructs formed described specific inefficiencies or barriers within process and procedures around compliance. Examples included 'clear process' contrasted with 'complex (undefined) process', and 'manual use' contrasted with 'automated'. Therefore, these barriers appear to be largely driven from within organisation decision making over approaches to compliance. If this assumption is made, then there may be feasible solutions to addressing such barriers within organisations. Perhaps, if more effective decision making over process/procedures is made by the right people (in an independent manner) this may combat these everyday barriers impacting on regulatory compliance. This is discussed further in Section 8.2.1.

### **7.3.5.3 Categories with 'medium' importance**

There were six categories which were allocated as medium importance based on scoring compared to overall construct: education and training, ethics and culture, reputation/best practice, stakeholder considerations, communication and knowledge sharing, and regulatory risk.

**Figure 41 Education and training category**

|                        | Positive aspects       | Negative aspects |
|------------------------|------------------------|------------------|
| Education and Training | Commitment to Training | Minimal Training |

Education and training was ranked as 5<sup>th</sup> within dominance and also represent medium importance to practitioners when scoring constructs compared to overall construct. Discussion of education and training also exists within the literature (Taylor, 2005; SIA, 2005) but it should be noted that the literature is more often written from a practitioner's perspective. The types of constructs that were formed in this area included the concepts of provision of training, in comparison to lack of training provision, and also concepts of complexities and skill requirements.

**Figure 42 Ethics and culture category**

|                    | Positive aspects                 | Negative aspects                |
|--------------------|----------------------------------|---------------------------------|
| Ethics and Culture | Commitment to ethics and culture | Disregard to ethics and culture |

Ethics and culture ranked in the lower third with respect to dominance, and is considered of medium importance to practitioners. Given the significant media coverage of cultural issues this is a fairly surprising finding, as an initial assumption was made that this would be an area of prominent concern for practitioners. This also does not align to the academic literature which focusses heavily on ethics and culture within models (Jackman, 2002; Edwards and Wolfe, 2005; Wood, 2002). Examples of constructs allocated to this category include 'positive behaviour and desire to get it right' contrasted with 'morally corrupt', and 'no significant culpability' contrasted with 'consider changes at senior management level'.

**Figure 43 Reputation/best practice consideration/proactivity of management**

|   | Positive aspects  | Negative aspects   |
|---|---|--|
| Reputation/ Best practice consideration/Proactivity of Management | <p>Proactive assessment by management of reducing reputation risk</p> <p>Seen to be 'best practice' by peers</p> <p>Continuous development and improvement to compliance – 'customer' driven improvements</p> | <p>Disregard by management of reputation risk</p> <p>Disregard of peer performance</p> <p>No calls for improvement to compliance – stagnant approach</p> |

In the initial template for analysis, this category actually formed three distinct concepts within the literature i.e. reputation (Crump, 2007; Calcott, 2010; Arora and Gangopadhyay, 1995; Shimshack and Ward, 2010), best practice (Malloy, 2003) and proactivity of management (Crump, 2007). There is also overlap to the literature developed by Parker (2002, p. 63) where she discussed common seminar topics aimed at compliance professionals in Australia including “how to sell compliance to the board” and “the business case for compliance”. However, during the allocation of constructs it was found that there was a level of crossover when practitioners elicited constructs around this area. Therefore, these concepts from the literature were combined in one overall category.

**Figure 44 Stakeholder considerations - input from external departments/resource/consultants. In-house, in comparison with shared services/outsourcing considerations**

|  | Positive aspects                                | Negative aspects                              |
|--|---|---|
| Stakeholder Considerations - Input from external departments/resource/consultants. In-house vs. shared services/outsourcing considerations | Extensive investment of IT compliance resources | Minimal investment in IT compliance resources |
|  | Internal centre of excellence                   | External centre of excellence                 |

The types of constructs which were included in this category included concepts of: ‘commercial necessity’ compared with ‘nice to have’, and ‘must do’ contrasted with ‘wish to do’; short term/long termism; seniority of management input and active support of management; and protecting customer/client driven. These constructs may be considered in conjunction to the categories formed relating to nuisances and barriers, in an attempt to remedy issues within compliance approaches.

In the initial template for analysis, this category actually formed two distinct concepts within the literature i.e. resources and inputs from external providers such as IT/consultants (Bamberger, 2010; Gable, 2005; Garcia, 2004; Mainelli and Yeandle, 2006; Hussein and Hussan, 2008), and outsourcing or use of shared services (McIvor et al., 2011). Again, the constructs elicited from practitioners did not appear to form distinction between the two concepts, and instead focused on wider stakeholder considerations. This was the most dominant of categories for construct elicitation.



Parker (2002, p. 112) also widened this discussion whereby compliance manager consider best practice, or ideal compliance as a “harmonising role”, or a bridge between “the values of wider society, including regulators, governments and public interest groups, and the pursuit of business”.

Constructs allocated included references of: ‘many stakeholders’, or organisation wide and project teams, in comparison with, containment within compliance; consulting involvement (or working with experts) and outsourcing considerations; and system development considerations.

This category was again initially set up in the analysis template as two separate concepts, but during categorisation overlap in construct elicitation was seen so the concepts were combined. This joins two distinct areas of the literature i.e. concepts of share services/outsourcing, in comparison with, in house considerations (Herbert and Seal, 2009), and the concepts of partnership and relationships with regulators (Wood, 2002; Carretta, 2005).

**Figure 45 Communication and knowledge sharing**

|  | <b>Positive aspects</b>  | <b>Negative aspects</b>   |
|--|--|---|
| <b>Communication and Knowledge Sharing</b> | Compliance knowledge nurtured and developed in house           | Compliance knowledge limited within the business                        |
|  | Business relationships, communication and interfaces essential | Minimal regard for business relationships, communication and interfaces |

During analysis the communication/knowledge sharing category did appear to overlap with the stakeholders category. However, the key distinction in this category is the focus on communication mechanism i.e. liaison with other firms/communication skills, and the knowledge elements i.e. selling skills/service. The constructs elicited within this category were of fairly low dominance, signifying that this area is not an area of focus for most practitioners.

This appears to be an unusual observation, as inherently in the literature based it may be assumed that communication and knowledge sharing are often seen as areas demonstrating best practice, or of benefit organisations. This may then suggest underlying trust issues between organisations within the sector. Another concern may surround the issue of having “a foot in each camp” where the compliance officers must

balance their responsibility to the firm versus the organisations they serve (Parker, 2002, p. 174).

**Figure 46 Regulatory risk category**

|                 | Positive aspects  | Negative aspects                    |
|-----------------|---|-------------------------------------|
| Regulatory risk | Full awareness of New Regulation – e.g. BASEL III/FATCA | Limited knowledge of new regulation |

The regulatory risk category was developed from the wider literature on regulatory approaches, and the discussion of new regulation following the financial crisis (Stoneman, 2005; Gebhardt and Novotny-Farkas, 2011; Dizdarevic, 2011; Wise and Baker, 2012; Ayres and Braithwaite, 1992). This category was included in the template to collate constructs referencing how compliance officers might approach new regulation and their relationship with the regulator.

This category is fairly low in dominance but still of medium importance in terms of considerations of overall cost and benefit to the organisation. The constructs that were formed were mainly focussed on ‘consequences’, and ‘risk’ assessment, and ‘impacts’ which suggests reactionary constructs rather than proactivity in this category.

#### 7.3.5.4 Categories with ‘low’ importance

There were two categories which were allocated as low importance based on similarity scoring. These were skills and status of compliance, and ritualism and gaming.

**Figure 47 Skills and status of compliance - experience, knowledge, education and hierarchy within organisation**

|  | Positive aspects  | Negative aspects   |
|--|---|--|
| Skills and Status of Compliance - experience, knowledge, education and hierarchy within organisation | Compliance officers status high<br><br>-skills set, independence, authority | Disregards of compliance officers importance in organisation |

The status of this category as of low importance is a significant finding. This directly contrasted to the literature which discusses the importance of the role of compliance/risk management within organisations (see literature in Section 4.1 to 4.2).

However, the low importance of constructs within this category is also supported by the lower dominance of this category with few constructs (only 3) being allocated.

Perhaps the reason this category does not dominate the constructs of the individuals, is due to the worldview that the compliance officers assume during interview, projecting constructs onto external factors. Self-reference to personal skills set and independence perhaps is an assumed given by participants when discussing personal experiences. However, the constructs that were elicited did align to the literature and included 'personal integrity important factor', 'compliance experience and competence' compared with 'specialist knowledge not required', and 'skilled judgement and expertise required'.

Ritualism and gaming (Braithwaite, Makkai and Braithwaite, 2007) as a category was seen as low importance when comparing to the overall construct of benefits, in comparison with, cost considerations. This category was the least dominant of the categories in terms of number of constructs allocated. This seems to be in direct contrast to the high ranking of the category of stakeholder considerations (if the regulator was considered as a stakeholder). This can be explained by the inherent differences within these categorisations. The stakeholder category is focused on communication and working in partnership with external parties outside the regulatory relationship, whereas ritualism and gaming category is specifically considering the complexities of interactions between the compliance officers and the regulators.

**Figure 48 Ritualism and gaming category**

|                      | Positive aspects  | Negative aspects   |
|----------------------|---|--|
| Ritualism and Gaming | Good working relationship with regulator. Enforcement within firm. Decisions are thought from a 'extended' compliance view. | Compliance officers game the regulator. Letting things go within firm. Decision revolve on 'going as far as needed'. |

This may also be viewed as a significant and positive finding, if it is assumed that the concept of 'playing games' with the regulator does not factor highly within the compliance officers' construal systems. Examples of the constructs that were formed included 'no obligation to report as long as actions taking place to fix' and 'liaison with regulator' contrasted with 'no liaison'. These types of constructs indicate concerns over the communication mechanisms between practitioners and the regulators. So despite these being of low importance and dominance within the compliance officer's worldview, these may be seen as more important from a regulators viewpoint.

### 7.3.6 Summary of Honey's content analysis

There were no suppositions made in respect to constructs elicited from practitioners within the grid<sup>100</sup>. As a result of performing Honey's content analysis on the grid constructs the following main findings have emerged.

The 230 constructs formed by practitioners to describe their personal experiences have been allocated within 12 categories: resource; education and training; ethics and culture; reputation implications; skills and status of compliance officers; stakeholder considerations; communication and knowledge sharing; regulatory risk issues; principle versus rule based concerns; barriers to compliance; nuisances and inefficiencies; and ritualism and gaming.

Of these three new distinct categories have been observed, which were not identified in earlier literature review by the researcher: barriers to compliance, nuisance and inefficiencies, and ritualism and gaming. These issues are revisited in the discussion and triangulation with the literature in Section 8.1.2. There is an attempt to address the barriers to compliance within the conceptual model presented in Chapter 8.

With respect to dominance, there are three distinct splits of category allocation i.e. the top third show 14 to 18 paired constructs allocated, mid third show 6 to 11 paired constructs allocated, and bottom third show only 3 to 4 constructs allocated (see Table 20). The most dominant category was 'stakeholder considerations'. In addition, 'barriers to compliance' was observed within the top third in terms of dominance of construct formation.

With respect to importance, the categories with similarity scores most closely aligned to benefit and cost considerations included 'nuisances/inefficiencies' and 'principles, as opposed to, rule based/spirit, as opposed to, letter of law'. As these reflect the major concerns of compliance officers, these categories may be of significance to regulators and policy makers, in order to respond to issues seen within regulatory compliance in the financial service sector.

One surprising finding in review of importance of construct categories was the low allocation of 'skills and status of compliance'. A presumption was made by the researcher that this would be a key category in comparison to benefits and cost

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<sup>100</sup> Following the principles of Kelly's individuality corollary (see also Appendix 3) the constructs elicited were considered to be personal to each individual based on their own experiences, therefore, no pre supposed assumptions were made in respect to construct elicitation prior to analysis.

concerns. However, this was not observed in the sample of participants completing grid interviews.

#### 7.4 Analysis of interview transcripts

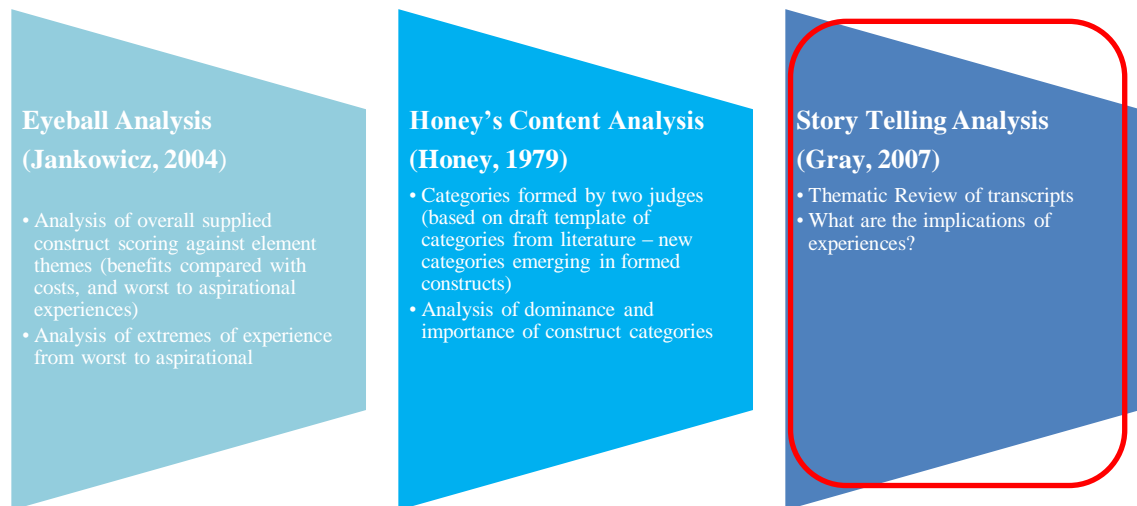
The initial analysis, in Section 7.2 and 7.3, involving eyeball analysis of grids, and content analysis of constructs does not fully explore RQ1 and RQ3. The purpose of this section is to review the story telling aspect of the interview transcripts to explore RQ1 and RQ3.

Research Question 1: To what extent does the regulatory cycle influence managements' decision making over compliance approach?

Research Question 3: In cases of new regulation, how do compliance functions rely on external expertise (consultants) or is there proactive promotion of in house knowledge and expertise?

Figure 49 highlights the final distinct phase of analysis which is presented within this section.

**Figure 49 Distinct phase of analysis (story telling) - figure brought forward from Methodology, Section 6.6**



As per the two step process, set out within Figure 30, the interview transcripts<sup>101</sup> were initially analysed under a systematic process of template coding and then immersion within the data to allow for interpretation. A major limitation within the grid interview is the time available for each individual to participate within story telling. This restriction was ultimately controlled by the nature of the individuals being interviewed i.e. senior personnel within organisations, who were only able to participate for 1-2 hours.

<sup>101</sup> Refer to Table 11, Section 6.4.6 for details of interview data recorded and analysed.

Therefore, RQ 1 and 3 were not fully explored with all participants due to time constraints for certain participants. The interviews were unstructured in nature due to the preparation of the repertory grid element, and construct elicitation. However, where possible the interviewees were probed further under the following open question themes (as described within the methodology chapter):

1. What are the effects of changing regulation?
2. When/How are consultants used?
3. When/How are outsourcing/shared services options considered?

Codes were set up based on the specific research questions within the initial coding template. This allowed for specific analysis of the interview transcripts prior to immersion. This process was performed manually using tables in word. Nvivo was considered for use, however, due to ease of access and the systematic organisation employed within word file, this analysis method was seen as preferable for the individual researcher.

#### **7.4.1 Discussion of supposition statements**

With reference to RQ1 the following supposition was made (see Table 14 for link to research question and underlying literature):

Individual compliance officers prioritise workload around the regulatory approach (and the current regulatory risk appetite).

This supposition has direct links to both Ayres and Braithwaite's responsive regulation and Jackman's model. Under responsive regulations the regulators are reactive to the firms approach to regulatory demands. Under Jackman's model, both the compliance approach and the regulators' approach are interlinked.

With reference to RQ3 the following supposition was made analysis (see Table 14 for link to research question and underlying literature):

The approach to new compliance is highly dependent on the resource constraints within the business.

This supposition has direct links to alternatives to traditional in house compliance models i.e. outsourcing, shared services and consulting considerations.

## 7.4.2 The regulatory approach

Due to the nature of their roles, and direct links to regulatory compliance all of the participants discussed the relationship with the regulators to some extent. Analysis via immersion within the interview texts reveals a number of sub themes within discussions with practitioners.

### 7.4.2.1 Dealing with the regulator

The first of these sub themes were issues of dealing with the regulator (or relationship with regulator).

“As the banks’ don’t wish to fall foul of any requirements, we tend to over-regulate in some areas, which then has an adverse effect on customer service and engagement” Participant YMO26

This quote reflects respect for the regulator and fear of adverse reaction from the regulator. This of course has direct links to responsive regulation, and the enforcement pyramid. By keeping the regulator on side there is lower risk of sanctions or regulatory actions. However, the cost of over complying within the financial service organisations may result in adverse effects on the consumer i.e. additional over regulation of processes.

“Inspection by the regulator had come up with findings [...] so there was lots of pain to go through within the business” Participant JMC10

This quote portrays negative emotions of dealing with the regulator. Through non-compliance and the resulting regulatory response the business suffered. This is again directly linked to the enforcement pyramid, whereby non-compliance results in increasing severity of sanction or pain for the business.

However, there was push back on the concept of regulation from practitioner in the quote below. The concept of increasing regulation was seen as an inhibitor, rather than an encouragement for greater compliance. This would directly contrast with the dynamics of the enforcement pyramid. However, this is aligned to Jackman’s model whereby firms are encouraged to follow spirit rather than letter of the law.

“Regulation doesn’t solve the problem. In some ways they make it worse...because all that you do is create this tick box mentality, when everyone is struggling to meet this book of regulations, which is about a foot thick” Participant OMC20



The importance of the regulator as a stakeholder is encompassed in the quote below.

“You were actually dealing with the regulator and you had to get them to buy into it because you had to get a really good, fair, understanding of what they want” Participant EFC10

This is supportive of the concept of the enforcement pyramid whereby the regulator is reactive to the actions of the firm. Clear communication between both parties is essential to achieve regulatory compliance. This also has links to Wood’s 2002 Partnership model (see Section 4.4.1). This model was also linked to Jackman’s model by Edward’s and Wolfe (2004).

This argument is also supported by Smith (2011) who argued that:

“Responsive regulation is most successful where human agency is personal central and regular in creating regulatory relationships” (p. 733)

Therefore, the resourcing of this human relationship, at both the regulator and the regulated, is of vital importance to move regulatory compliance forward.

#### ***7.4.2.2 Motivations and difficulties of regulatory compliance***

The second of the subthemes was motivations and difficulties of regulatory compliance.

“So yes we do need to be one step ahead of the game really, we need to be.....In some cases we work with them, in some cases it is released to everyone at the same time” Participant NMO28

“they are not black and white, there’s judgement and shades of grey...making sure you are doing things properly, but nevertheless allowing yourself to take into account factors which they won’t have thought about” Participant VMLA19

These two quotes demonstrate the inherent difficulties in responding to regulatory change. The idea of ‘being ahead of the game’ indicates a desire to demonstrate proactivity and best practice to the regulator and peers. The importance of the ‘work with them’ indicates the importance the reactive relationship between both regulator and firms. However, there are negative aspects of this relationship. The first quote portrays a sense of pressure to achieve to expectations, by being ahead and proactive, which will inevitably put strain on the relationships of the professionals involved.

The second comment indicates the complexities and ‘shades of grey’ within the relationship. This has direct links to the findings within the personal construct analysis

linking to the category of 'principles, as opposed to, rule based/spirit, as opposed to, letter' (see Section 7.3.5.1). This shows the interrelationship between communication with the regulator and application of professional judgement. This is also reflected in Jackman's model as well, in a mature relationship. Although not highlighted directly within the model itself, the concept of trust is inferred within this relationship (Harvey and Bosworth, 2013).

One participant considered the relationship with the regulator in some depth and seemed to be justifying the importance of the role of compliance in an organisation. The quote below reflects the 'compliance as inhibitor' concept in a positive manner. This links to the findings of high importance, of the nuisance category, within content analysis of constructs (Section 7.3.5.1). Compliance is an essential intervention (or perhaps a necessary nuisance) for businesses in terms of risk, and the relationship with the regulator.

“So compliance is a form of risk management, it's regulatory risk management, and it is also a form of ensuring we abide by the laws and regulations [...] it was where compliance was an intervention” Participant VMLA19

The same participant went on to consider relationships with regulator with links to culture (in the quote below). Again, the intervention of compliance is essential for the regulatory relationship to ensure that misdemeanours are reported and dealt with appropriately. The significance of this quote is the complexity of this statement as it relies: firstly, on an ethical compliance officer; secondly, on an appropriate culture in the organisation (i.e. the compliance officer is allowed to perform his duties); and finally, on a good relationship with the regulator to deal with issues identified.

“cultural issues yes, absolutely....and the other side of it, where it is significant is any regulatory breach, because that as you are probably aware, and regulatory breach of any significance needs to be reported to the regulator and that creates a tension within the business because that ... because obviously the business does not automatically want to notify the regulator of any problem” Participant VMLA19

Providing a contradictory viewpoint, again with links to culture and ethics of individuals involved, the quote below highlights the inevitable barriers to the compliance function and the relationship with the regulator. Even if both the regulator and the compliance officers are aligned in goals of achieving regulatory compliance, rogue individuals will succeed in unethical behaviours.

“If someone is determined... because if you think about this, every one of these banks had the correct policies and procedures in place. The regulator had been in, and the policies and procedures were spot on” Participant OMC20

This theme of barriers to compliance was also highlighted in the review of personal constructs in Section 7.3.

#### **7.4.2.3 Dealing with new regulation**

The final subtheme included discussions of dealing with new regulations.

“So the way we look at this then is very much, supply and demand... at the highest level, we have a schedule of regulatory change, that will come down the pipe” Participant LMC20

“The regulations don’t change significantly they kind of just get tweaked here and there [...] identifies if there’s a gap between the old and new and that’s how you know where to update” Participant EFC10

The two quotes above link directly to concepts of resourcing of skills towards new regulations. The first one demonstrates a proactivity of compliance professionals of knowing what is coming and resourcing how they will deal with the issues. The second quote indicates a pragmatic approach to dealing with new regulations via assessing gaps and effectively getting on with it.

However, in instances of significant change it is not simply a matter of resourcing from within organisations. Participants highlighted the importance, and necessity of working with others. In the quote below there are two key points illustrated. The first is the importance of interactions with other organisations/compliance professionals through organisations such as the BBA. This demonstrates a willingness for knowledge sharing and trust with other organisations. The second is the inevitability in certain cases to include consultants in dealing with new regulations.

“to a degree through things like the BBA, so on big topics of compliance, for example, we will talk to other banks about its... so on legacy issues, SME derivatives for example or mis-selling of interest rate derivatives, there’s a pretty common industry standard there, but we still use consultants there” Participant LMC16

A second participant (from a different sector of the industry) makes a similar point in the quote below. This underscores the importance of knowledge sharing and trust of other organisations in the sector, in order to meet regulatory changes.

“it enables all the trade bodies to get together, and discuss which bits of these particular elements of these recommendations, are well, um I suppose valid, are possible to implement, and the costs involved in it all” Participant NMO28

The inevitable use of consultants is also validated in the quote below.

“Need external expertise to understand/cope with new regulation” Participant YMO26

The issues and costs of dealing with new regulations were also discussed by some participants. The frustrations of complying with regulatory demands are encompassed in the quote below. The participant highlighted that this was an experience from some years ago – but the fact that this was still forming part of his personal worldview evidences the importance of this aspect of the regulatory relationship. The significance of communication (and the pitfalls of miscommunication) between regulator and compliance professionals is important in cost benefit considerations whilst dealing with new regulation.

“setting up systems based on two documents and then turning around and changing, so we had to change all the systems again...cost us a fortune, and a nightmare in time...training, everything” Participant NMO28

Conversely, an alternative view is also presented in the quote below. Despite the inconvenience and costs of implementing new regulations, the importance of adherence to regulatory demands is demonstrated in the experience below. Despite misgivings about implementing this particular compliance update, overall the experience was seen in a positive light, and a benefit to the organisation.

“It had to be done, so if we hadn’t we would have lost [...]. Did we learn anything on the way?...actually, yes, I think it is a bit of a tenuous link, but we probably saved ourselves hundreds of thousands, even millions of pounds” Participant RMO20

This is an important finding, whereby, compliance officers can benefit and learn from compliance experiences which they may initially view as problematic i.e. worst compliance experiences.

### 7.4.3 Alternatives

The discussion of alternative routes for regulatory compliance reflects individual experiences. This exposes inherent difference in the organisations and jurisdictions in which the compliance officers had worked. Some organisations are able to (and willing to) highly resource the compliance function, whereas some organisations have limitations on resources towards compliance. The quote below reflects the specialised skills required in certain scenarios. If the compliance function is adequately resourced they may choose to employ consultants in this instance.

“you might use advisors all the time for this type of stuff... and then for regulatory investigations for example, you would use specialists, legal firms, big 4 accountancy (type) firms would provide specialist know how to deliver narrow parts of your program” Participant LMC16

However, the use of external consultants appeared a completely alien (and unnecessary) concept to other individuals, as per quote below. If funding resource is limited it is a matter a compliance professionals getting on with it themselves. Therefore, this suggests that alternatives are heavily influenced by the individual organisations resource structure.

“I can’t think that we have ever used consultants on anything to do with money laundering compliance” Participant NMO28

It should be noted that this viewpoint was limited to only 1 of the 12 participants. Other participants were supportive of use of consultants. Consultants were seen as a mechanism to add credibility to the claims or recommendations of the compliance officers i.e. ‘if a multinational consultant has okayed this, then we must be going about this in the right way’. Consultants were seen as a mechanism to get support of all stakeholders, as per the quote below.

“You had to get the key stakeholders on board, because you weren’t just dealing with in that situation I went to ask a consultant to do that” Participant EFC10

Nevertheless, the use of consultants is not always adopted. There are certain circumstances when use of consultants is seen as appropriate and certain situations where their use may be seen as frivolous. As per the quote below, compliance consultants were seen as a benefit to support the approach to new regulation, to avoid

'scraping through'. The concept of balancing resources is also introduced – consultants being seen as a temporary workforce to meet a short term need.

“Some firms did most of it in house, and achieved a minimum level of compliance... but absolutely scraped through...those paying the minimum tend to be the smaller organisations, with minimal use of external consultants, and tend to be simpler businesses and might have spent £10 million .... On the other end we spent £120 million, probably £80 million was with consultants, to develop models, to produce documentation, to run programmes, that's purely because we did not want to gear up with ermm.... 200 people, and put them on our cost base” Participant LMC16

The same participant reinforces the balancing of resource in the next quote. The concept of maintaining steady employee numbers of resource via use of external contractors (consultants). So despite the large costs involved in using consultants, this is seen as a preferable alternative to increasing the underlying base costs of the business (which from an accounting viewpoint seems counter intuitive).

“so at each point you consider what best blend of internal and external contracting of resource, outsourcing some stuff to third parties completely [...] because what you don't want to do is to increase our base level of costs” Participant LMC16

Ultimately, we return to the idea that the use of consultants is highly dependent on the organisation structure. When discussing outsourcing (rather than use of consultants) the concept of organisation dynamics is seen as key. Consultants and outsourcing serve an essential purpose within the sector of financial service regulatory compliance from a cost/benefits viewpoint, as per the quote below.

“there is a diversity of scale that creates a market for such a function, that is to say that larger companies tend to operate these functions in-house, but the smaller firms find it cost effective to outsource” Participant YMO26

However, there are a number of risks involved in use of consultants or outsourcing. From the perspective of a function providing outsourcing services (to other organisations), risks remain from a reputational point of view. While the risk of regulatory compliance remains with the individual organisation who outsource, the firms offering outsourcing services suffer also from reputational damage in instance of non-compliance/regulatory breach. A regulatory breach indicates that their processes

are not working effectively to meet their client's needs, as per the quote below, and risk by association applies.

“All they're doing is outsourcing to us, so we have to make sure we manage it properly. Ermm. So our risk becomes reputational. If one of our clients does something terribly wrong, and we just go along with it, then our risk is by association” Participant NMO28

There were also a number of barriers, or costs presented when considering use of these alternatives. The first unsurprisingly is the cost of such services. The quote which follows highlights that costs of such services are not commensurate with the benefits received.

“Now whilst we have got some value from that in terms of better models built, slightly better documentation, have they got a billion of value from it? No chance.... And majority of that's gone to consultants” Participant LMC16

Also, irrespective of the use of such alternatives, stakeholders buy in is seen as a much greater force in terms of compliance effectiveness. Without buy in from the top, compliance functions will inevitably fail, as per the quote below.

“If the board don't accept this need [...] and are simply saying 'ok thanks compliance, yes fine, yes noted thank you very much, yes but we have to make X amount of income this month, this year or whatever' it's not going to work. Compliance will never succeed” Participant OMC20

Finally, all of the issues around alternatives are dwarfed by the underlying issues of spirit, as opposed to, letter of the law. Ultimately the consulting and outsourcing industries are providing a service to compliance functions. However, if the underlying approach is not geared towards an ethical, and judgement based rationale, then compliance again will fail, as per the quote below.

“No I don't think it is rule based, and that is where I think there again is a mistake ....Report it, investigate it, ask questions...because the trouble is you are creating a huge industry around compliance and too much of it is ticking boxes, and not enough is about thinking about what we are doing... what is the purpose of what we are doing....which is what the risk based approach (is...) should be about” Participant OMC20



In summary, these discussions consider the concept that many organisations have widespread use of consultants or outsourced services to deal with regulatory demands. Some organisations may employ consultants to meet short term resource demands. Some organisations may employ consultants for technical expertise. And finally, some organisations would consider consultants as a form of outsourcing compliance.

Although not formally recorded in data, whilst presenting a workshop at a conference<sup>102</sup> to a range of consultants, practitioners and academics the issue of ‘consultants’ was raised. In this small group opinion was divided between ‘why pay for consultants when we are capable ourselves’ to the (consultants’ viewpoint) of the specialism that are offered by such services – spend money, to save money. The idea of consultants adding credibility to recommendations/processes adopted by compliance was also discussed in this workshop, which demonstrates the dominance of this construct in discussions with a number of practitioners.

#### **7.4.4 Summary of conclusions on suppositions 1 and 4 from interview data analysis**

At the start of this section, two separate suppositions were presented which were aligned to RQ1 and RQ3 in Table 14.

##### **7.4.4.1 Discussion of Supposition 1**

Individual compliance officers prioritise workload around the regulatory approach (and the current regulatory risk appetite).

From the analysis above, it may be concluded that compliance officers are highly aware of the regulatory cycle and plan resources carefully around regulatory changes. This suggests a level of proactivity which is seen as desirable from a regulatory viewpoint. The findings overview resulting from the analysis of quotes by participants when discussing the regulatory relationship, now follows:

- Compliance officers are respectful of their relationship with the regulator;
- However, there are negative emotions associated with dealings with the regulator;
- There is push back from practitioners regarding over-regulation;
- There is an expectation for regulators to be reactive to actions taken by the organisations;

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<sup>102</sup> Delivery of workshop ‘A Plea for Ethical Compliance’ at 32nd Cambridge International Symposium on Economic Crime

- There are inherent difficulties in responding to regulatory change: resource, judgement, and relationships are seen as important drivers (and sources of difficulty);
- Despite best intentions of compliance functions/regulators, culture (and unethical behaviours) still act as barriers to compliance;
- Resourcing change is seen as a key barrier for dealing with new regulation;
- Knowledge sharing is considered essential to drive regulatory change;
- Communication is also considered essential for the regulatory change to be successful.

From these points, we can see that compliance officers are focused on maintenance of strong relationships with the regulator, and do indeed prioritise workloads around the regulatory approach. Significant attributes to the relationship include respect, clear communication, and knowledge sharing. However, barriers of culture, resource, and miscommunication may inhibit the relationship between compliance officers and the regulator.

#### **7.4.4.2 Discussion of Supposition 4**

The approach to new compliance is highly dependent on the resource constraints within the business.

From the discussion on alternative approaches above it may be concluded that use of alternatives varies depending on the dynamics within the organisation (which is often outside the control of the compliance officers themselves). The following reflects a summary of analysis of quotes by participants when discussing alternatives:

- Subject to resource restraints, the majority of organisation would use consultants to affect regulatory change;
- Consultants involvement may provide credibility to the compliance function recommendations;
- Consultants are seen as a short term/temporary resource;
- Costs of consultants are not always seen as commensurate with benefits received;
- Risks are associated with alternatives, and include high costs and reputational risks;
- Irrespective of alternatives adopted, internal barriers within the organisation will inhibit the compliance function (management buy in, and spirit, as opposed to letter of the law considerations).

The subjects of resource/costs were of high importance during discussions of alternatives. However, this is balanced with the concepts of credibility and smoothing of resource. Moreover, the barriers to compliance were also highlighted by practitioners with recurring theme of culture (management buy in) and also judgement (spirit/letter of the law).

### **7.5 Concluding thoughts**

This chapter has presented the analysis of data collated during interviews with practitioners. As discussed in the methodology chapter (Chapter 6), and also revisited within this chapter, repertory grid allows flexibility for researchers to tailor use of grids, and resulting analysis to their own research agenda. This has been capitalised within this analysis to allow story telling from interview data to be triangulated with content analysis of constructs. The original research questions and suppositions which were used as a framework in order to analyse data (Table 14) have been explored with main findings summarised in Table 21.

The next chapter will synthesise these key findings against the existing literature base, and present an alternative conceptual model for the compliance function.

**Table 21 A summary of the research questions, the suppositions explored, and the main findings presented in Chapter 7**

| Research question  | Supposition   | Main findings (and section discussed)  |
|--|---|--|
| Research Question 1: To what extent does the regulatory cycle influence managements' decision making over compliance approach? | Individual compliance officers prioritise workload around the regulatory approach (and the current regulatory risk appetite). | Compliance officers are highly aware of the importance of relationships with the regulator, and remain proactive in prioritising workload around the regulatory approach. Key barriers to the relationship include poor culture, inadequate resourcing and miscommunication. (Section 7.4, Section 7.4.4)  |
| Research Question 2a: What are the key constructs that influence managers' decision of compliance function approach?           | No suppositions were made for content analysis of constructs.   | <p>Compliance officers' personal constructs have been classified into 12 categories from the 230 pooled constructs. The following categories were identified during analysis: resource; education and training; ethics and culture; reputation implications; skills and status of compliance officers; stakeholder considerations; communication and knowledge sharing; regulatory risk issues; principle vs rule based concerns; barriers to compliance; nuisances and inefficiencies; and ritualism and gaming.</p> <p>Three new categories of personal constructs are observed within the data set which were not identified in the literature at point of creating the initial template i.e. barriers to compliance, nuisance and inefficiencies and ritualism and gaming. Of these new categories 'barriers to compliance' was seen to be of medium/high in terms of both dominance and importance. The most dominant category was 'stakeholder considerations'. With respect to importance, the categories with similarity scores most closely aligned to benefit and cost considerations included 'nuisances/inefficiencies' and 'principles, as opposed to, rule based/spirit, as opposed to, letter of law'</p> <p>The results of the category formations will be taken forward into the next chapter and synthesised against the existing literature, to consider whether any steps may be taken by regulators or practitioners to overcome these issues surrounding regulatory compliance. (Section 7.3, Section 7.3.6)</p> |

| Research question  | Supposition   | Main findings (and section discussed)   |
|--|---|---|
| Research Question 2a: What are the key constructs that influence managers' decision of compliance function approach?   | Aspirational compliance experiences may include an abundance of positive connotation within the descriptors, and that worst compliance experiences may include an abundance of negative connotation within the descriptors given by participants.   | When practitioners describe negative connotations of their experience the key drivers appear to be external factors and uncertainties (often outside control of compliance office). (Section 7.2, Section 7.2.2)  |
| Research Question 2b: How do compliance officers' personal constructs align to academic models of compliance?  | If the scaling of aspirational compliance to worst compliance within the repertory grid were aligned to the linear scale of Jackman's model and contention of "an ethos of ethical compliance" and "unthinking mechanical compliance", the expectation would be for scoring of 1 for aspirational compliance (perceived as a benefit to organisation) and a scoring of 5 for worst compliance experience (perceived as a cost to the organisation). | Practitioners do not align perceptions of benefits and costs in a linear fashion, when comparing worst and aspirational compliance experience. Benefits are often achieved within difficult situations, and costs are often apparent in otherwise ideal scenarios. This challenges the traditional models presented within academic literature. (Section 7.2, Section 7.2.1)  |
| Research Question 3: In cases of new regulation, how do compliance functions rely on external expertise (consultants) or is there proactive promotion of in house knowledge and expertise? | The approach to new compliance is highly dependent on the resource constraints within the business.   | Themes of resource/costs of consultants and alternatives were dominant influences for decision making over use. However, credibility added in using consultants was also seen to be a dominant factor for decision making in use of alternatives. Barriers were again highlighted, when exploring this supposition with recurring theme of culture (management buy in) and also judgement (spirit/letter of law).(Section 7.4, Section 7.4.4) |

## Chapter 8 Discussion – The compliance trust

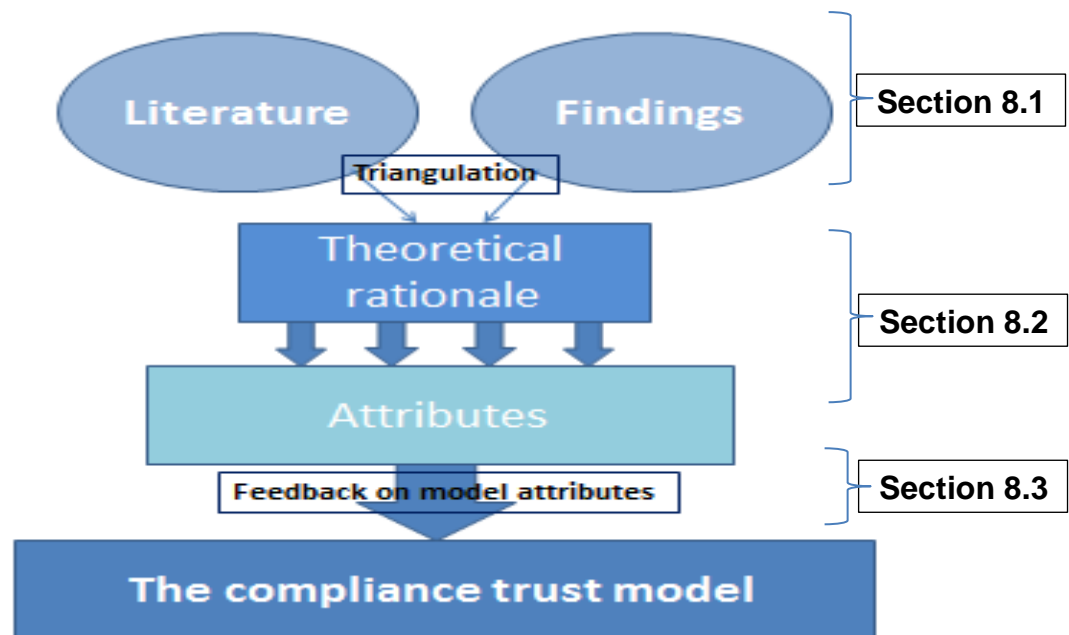
“Rationalists regime and bargaining theorists and, more surprisingly, constructivists have largely ignored the influence of social interaction on compliance decisions” (Checkel, 2001, p. 554)

### 8.0 Introduction

The quote above reflects the importance of understanding the compliance officers' worldview when considering theories around compliance. Therefore, the purpose of this chapter will be to consider the existing literature base, in combination with the analysis of the data from this thesis. The intention is to triangulate and synthesise the personal constructs of the participants against existing models from the literature, and provide an alternative model for compliance. A practical approach has been adopted to present the conceptual model in response to research objective 3 (which, in reaction to the quote above, emphasises the importance of social interactions with a number of stakeholders). However, given the sample sizes involved and qualitative nature of analysis, the findings cannot be generalised. This chapter offers tentative suggestions of interpretation from the main findings identified during analysis.

Figure 50 summarises the development of the conceptual model within this chapter (to expand upon the research design, which is set out in Figure 2). This chapter has been split into three main sections, which follows the course of development of the conceptual model (Figure 50). Section 8.1 considers each of the research objectives in turn and triangulates the existing literature in comparison to the data presented within this study, providing a theoretical rationale for the conceptual model. Section 8.2 presents the theoretical rationale for the emergent model attributes, with the overall model designed to offer an alternative solution to current models adopted within financial service practice and the literature. This model blends key concepts from literature and the findings from this study. Through development of this model, Objective 3 has been explored specifically within this section. Discussion and feedback from practitioners relating to the model is set out within Section 8.3, in order to strengthen the interpretation of the findings of this study, and prior to the presentation of the final model in Section 8.4. This section also addresses the central argument of this thesis of 'why compliance is viewed as business inhibiting' by providing an alternative solution towards regulatory compliance.

Figure 50 Development of the conceptual model



## 8.1 Research objectives

The following research objectives (and underlying research questions) were presented in the introduction to this study:

Objective 1. To understand the motives for regulatory compliance by banks.

RQ1 To what extent does the regulatory cycle influence managements' decision making over compliance approach?

Objective 2. To explore the different structures of regulatory compliance in operation.

RQ2a What are the key constructs that influence managers' decision over the compliance function approach?

RQ2b How do compliance officers' personal constructs align to academic models of compliance?

Objective 3. To investigate the circumstances under which different approaches would be adopted.

RQ3 In cases of new regulation, how do compliance functions rely on external expertise (consultants) or is there proactive promotion of in house knowledge and expertise?



Each of these research objectives, and the underlying research questions and findings will be summarised in turn. For each research objective a distinct review of the literature was performed. This was then followed by the data collection involving practitioners. Triangulation of both literature and key findings synthesises the conceptual model presented within Section 8.2. However, it is acknowledged that the wider literature and findings from this study are inevitably interlinked. Whilst it has been argued that the methodology employed explores personal constructs to provide rich and deep interview data, ultimately (as with many forms of qualitative and subject driven research data), the participants' views have emerged to an extent from their own review of literature/training and professional documents around the topic. Quoting Silverman's arguments against "our cultural love affair with the real":

"Most qualitative research who champion the subject's point of view or privilege experience simply do not question where the subject's 'viewpoint' comes from or how 'experience' gets defined the way it does by those very individuals whose experience they seek to document" (Silverman, 2013, p. 130)

Therefore, it is important to ensure that synthesis between the literature and the data collected within this study is performed, to identify any gaps within the respective sources. This synthesis (structured around research objectives) is presented in Sections 8.1.1 to 8.1.3.

### **8.1.1 Research objective 1: To understand the motives for regulatory compliance by banks**

#### ***8.1.1.1 Key points from the regulation literature***

In order to understand the motives for regulatory compliance, a thorough review of the regulatory literature was completed prior to development of methodology and interaction with practitioners. The purpose of the regulation literature review was to understand 'what compliance officers are complying with'. As evidenced in Chapter 3, a broad range of scholars contribute to the regulatory literature base. A direct (and practical) impact of the most recent financial crisis has been increased regulatory focus at a national (i.e. UK) and a global level. This ultimately does not explain the motives for regulatory compliance, but it does provide context to the pressures faced within the industry.

Responsive regulation (Ayres and Braithwaite, 1992) embodies a founding piece of regulatory literature, and the enforcement pyramid has been used as a key model to frame the analysis of the data presented in this study. Although the model does not

provide direct understanding of the motives for regulatory compliance, it does provide an indication of the complex relationship between the regulator and the regulated. This model provides an expectation of actions from the regulator via the enforcement pyramid, which may influence decision making of compliance officers when adopting approaches to regulatory compliance. Key principles within this model are the maintenance of appropriate relationships between the regulator, and the regulated. These attributes include clear communication and evidence of responsiveness in behaviours by the regulator. The overlap between relationships and culture was introduced earlier by Meidinger (1987), who discussed the concepts (and issues) of regulatory communities. The work on regulatory communities aligns to the concept of compliance communities which acts as a feature of the model presented in Section 8.2.

However, the enforcement pyramid faces barriers of the “deterrence trap” if penalties are not seen to be sufficient to deter misconduct (Parker, 2006), and this may indeed be seen to be a practical issue within the financial service sector. Despite significant fines and sanction from regulators, the highly profitably nature of the financial service industry may result in inappropriate behaviour for short term gains (connecting also to Barraquier’s 2011 compliance model linking ethical behaviours, decision making and associated emotions). This also indicates barriers in the form of micro view whereby compliance officers and individuals within the firm may not fully appreciate the macro impact they have on the wider firm and sector. The literature has discussed the concept of macro view from a regulatory perspective (IMF, 2010; Galati and Moessner, 2010; Baker, 2010) but this is not linked to the compliance officers themselves, or coherently linked to the motivations for regulatory compliance.

This lack of macro view at compliance officer level within organisations also highlights issues with self-regulation. A number of authors discuss the self-regulatory approach both pre, and post crisis (Stefanadis, 2003; Coglianese and Lazer, 2003; Ford, 2008 and 2011; Gilad, 2010; Calcott, 2010, Rossi, 2010). Whilst the principles are sound in theory, these appear to have failed to work in practice within the financial service industry – perhaps directly related to the concept that the compliance officers are not in a position to understand the macro view impacts of their actions. Again a global view may motivate individual compliance officers to achieve regulatory compliance. The global view is discussed by Moshirian (2011, 2012) from a regulatory perspective, but not from a compliance perspective within organisations. Fuller and Sharma (2012) endorse the concept of regulatory academies model (again from a regulatory perspective), and this concept would also benefit compliance officers by providing

macro and global view of the regulatory and compliance issues (and required response).

Regulatory capture must also be brought into this discussion of barriers to regulatory compliance, and has clear links with the objective to review the motivations for regulatory compliance. Various academics have studied this issue, and discussed the implications for regulatory failure (Baker, 2010; Young, 2012; Harvey and Bosworth, 2013). In its simplest form, a fundamental concept behind regulatory capture is a lack of independence between parties. Therefore, this forms a key principle in the conceptual model presented in Section 8.2. This is also supported by Smith (2011), who contended that there is a need for regulatory staff to act with scepticism and with independence, and should not “be placed in a position where it is easier to adopt the values and purposes of the regulated entities” (p. 740). Whilst this is written from a regulatory perspective the same principles should apply for the compliance officers within each organisation.

Underpinning the regulatory literature is the debate of theoretical principles of public interest (Pigou, 1932) and public choice theories developed in the 1970s. At the time of this thesis the public interest arguments (see Section 3.3) have been evidenced by a period of re-regulation following the most recent financial crisis. Therefore, the interests of the ‘public’ must be acknowledged within a conceptual model which would bear any relevance to financial service practice at this time. The concepts of public interest groups (PIGS) have been discussed by numerous authors in various conceptual forms (Ayres and Braithwaite, 1992; Omarova – public interest council, 2012; Levine - the Sentinel, 2012). Consequently, appropriate stakeholders in the form of transnational groups and informal industry leadership<sup>103</sup> have been included as major stakeholders with direct communication channels within the compliance trust conceptual model.

More recently Braithwaite and Hong (2015) suggested the concept of “regulatory ambassadors”. It may also be argued that the formation of the compliance trust, would acts as an alternate form of regulatory ambassador within the organisations they would serve (in acknowledgement of the stakeholder relationship between regulator and the compliance trust). However, this takes a slightly different form than that described by Braithwaite and Hong (2015), as in this instance the compliance officers, whilst acting as ambassadors, would also be expected to hold expertise (whereas Braithwaite and

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<sup>103</sup> Some other authors have already considered informal industry leadership. Arora (2010) examines the role and work of the existing international regulatory bodies. Abbott and Snidal (2013), Helleiner and Pagliari (2011) discuss transnational regulation and issues.

Hong (2015) acknowledge the “trade-off between solving the problem of thin relationships and the technical competence problem” p. 20)

In conclusion, it can be seen that a number of barriers to effective regulation (and regulatory compliance) are offered within the existing literature. However, these are written from the perspective of the regulators and the policy makers, rather than the perspective of the regulated (the compliance officers and the organisations they represent). Therefore, in an attempt to address these issues an alternative conceptual model of the compliance trust is presented (Section 8.2). This is modelled from the perspective of the compliance personnel working within the financial service industry, with the regulator as one of the stakeholders. Emergent attributes are described within the model in Table 22, which links directly back to the literature and issues discussed above.

#### **8.1.1.2 Key findings from the data – Research Question 1**

Within the data presented in Analysis and Findings Chapter, the following main findings were summarised with reference to research question 1 (extracted from Table 21).

Research Question 1: To what extent does the regulatory cycle influence managements’ decision making over compliance approach?

Supposition 1: Individual compliance officers prioritise workload around the regulatory approach (and the current regulatory risk appetite).

Key Findings: Compliance officers are highly aware of the importance of relationships with the regulator, and remain proactive in prioritising workload around the regulatory approach. Barriers to the relationship between regulator and the compliance officers include; poor culture, inadequate resourcing, and miscommunication.

Existing regulatory literature, and more specifically the responsive regulation model (Ayres and Braithwaite, 1992), is focused on the reactivity and actions of the regulator and policy makers. The data collated in this study contributes instead to the discussion of the ‘reactivity of the regulated’. Proactivity (and motivation to comply) was demonstrated during discussions with practitioners interviewed within this study. However, the barriers to compliance were highlighted as significant considerations in approaches to regulatory compliance.

Barriers to regulatory compliance are already discussed within the literature. However, the focus has been more specifically directed on the regulators and/or policymakers’ viewpoint. Therefore, a divide exists between the barriers identified within the

regulatory literature, and the perceptions of those trying to comply with the regulation, as found from this study. Irrespective of regulatory approaches adopted by regulators (i.e. re-regulation/de-regulation) there are inherent difficulties in supporting individual compliance officers facing barriers of culture, resourcing and miscommunication. However, this does reinforce the concepts that relationships between the regulator and the regulated are vital to overcoming such barriers faced within the sector.

In addition, the reality exists that despite both academic and practitioner literature endorsing best practice models, these issues/barriers to regulatory compliance still feature within the personal constructs of practitioners. This also reinforces that the current literature is ineffective in bridging the academia/theory/practice gap.

This study did not seek to specifically address the issue of culture within financial service organisations. However, there has been inevitable overlap into cultural concerns. Historically, and more recently it has been proven that culture issues still exist within the sector<sup>104</sup>. Haynes (2005) highlighted the importance of the independence of the function, whilst commenting on the personal attributes, including strength of “personality to withstand pressures”, which aligns to the findings of this study in relation to the issues posed by barriers to compliance. Therefore, the attribute of independence of compliance/risk professionals from the organisations that they serve, supported within the conceptual model, will mitigate some of the barriers that culture issues within financial service firms may present to regulatory compliance. In addition, the issue of inadequate resourcing and miscommunication is addressed within the conceptual model presented in Section 8.2, by ensuring these factors also form emergent attributes within the model.

A significant contribution achieved within this research objective, has been the exploration of grid data and interview data within Chapter 7, from the compliance officers’ viewpoint (as discussed above) as opposed to the wider debates in the literature from the regulators’ viewpoint.

## **8.1.2 Research objective 2: To explore the different structures of regulatory compliance in operation**

### **8.1.2.1 Key points from the compliance literature**

There is limited, recent academic literature which discusses structures/models of regulatory compliance from a financial service compliance viewpoint. A possible

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<sup>104</sup> See FCA website for numerous examples of scandals, and regulatory actions relating to inadequacies in culture, including a 2015 example <http://www.fca.org.uk/news/two-former-senior-executives-of-martin-brokers-fined-and-banned> accessed February 2015.

reason, evidenced within this thesis, is compliance and risk professional may be unwilling to engage with academics due to time and confidentiality constraints. However, a literature base does exist albeit written largely from a practitioner's perspective rather than academic viewpoints. Despite the existence of this best practice literature (as complimented by the regulatory literature), compliance professionals continue to face barriers within the financial service sector.

During the initial literature review, Jackman's model was identified as a practical model (given its publication in FSA DP18, 2002, p. 9). Although Jackman's model has limited citations, the rationale for use in this thesis is the relevance and specific focus of the model in the financial service sector, coupled with clear and inverse link to the widely cited enforcement model of Ayres and Braithwaite. The model was used to outline the pilot study; and ultimately, the linear nature of the model ('unthinking/mechanical compliance' to 'internalised ethos of statutory approach') influenced the methodological design of the experiences discussed with practitioners during repertory grid interviews (worst to aspirational compliance experiences). Other academics have developed Jackman's model further with focus on the partnership and relationships with the regulator (Woods, 2002; Edwards and Wolfe, 2005). The underlying links to ethical approaches to regulatory compliance are echoed in more recent publications and the media (Duska, 2011; Harvey and Bosworth-Davies, 2013; Llewellyn et al., 2014; BBC, 2014a).

A fundamental limitation within Jackman's model is the willingness and ability to comply, coupled with normative behaviours, in contrast to compliance cost considerations (Malloy, 2003; May, 2004). Compliance literature widely identifies economic, social and normative motivations for compliance (Parker, 2012). By creating a 'compliance trust' the network of compliance officers will share and balance the social, economic and normative attributes, across the financial service organisations they serve. Inclusion of the major stakeholders of the regulators, the organisations (financial service firms), and transnational groups will allow compliance officers to create a network which balances the needs of all stakeholders.

These discussions are underpinned by a number of theories depending on which viewpoint that the current models of compliance and the proposed conceptual model (Section 8.4) are considered from. Institutional theory is of importance from an individual organisation's point of view, in the current models in practice (i.e. individual financial organisations employing in-house/outsourced compliance professionals). However, within the compliance trust model institutional theory would apply in a

different way; with emphasis on the relationships between the stakeholders and the compliance trust (most specifically from the coercive perspective within these relationships). However, it may also be argued that Kohlberg's model (see Table 2) is more applicable within the compliance trust itself (and the professionals that would be employed within the trust). If the assumption that most business professionals are acting at the conventional level when reasoning i.e. doing what is expected by others, then the compliance trust and the interactions with the variety of stakeholders will lead to appropriate decision making within the trust. Through involvement of informal industry leadership in HR/policy making within the trust, then appropriate individuals with higher levels of moral reasoning may be identified to promote the overall morality within the trust.

In conclusion, the (majority) of existing literature regarding compliance models focuses on motivations for compliance (see Section 4.4), without really addressing the issues and barriers faced in practice. The literature is valid and promotes concepts for best (and ethical) practice from a range of academics and practitioners, but fails to fully consider the issues faced by compliance professionals, in their relationships within the organisation they serve, and when dealing with the regulatory demands. This may simply be due to the sheer diversity of firms within the sector. Kenny (2014) also identify with these issues with the concepts of "dependence corruption". Therefore, the introduction of the conceptual model in Section 3 supersedes this issue by providing rotation of independent compliance resource across all firms. Knowledge sharing and best practice are implied within this model – if individuals face barriers to compliance in the organisations they serve, ultimately they can obtain support initially via the compliance trust network, and then through the other stakeholders in the relationship (regulators and public interest groups).

#### ***8.1.2.2 Key findings from personal constructs data– research question 2***

This study provides a contribution to the literature by exploring practitioners' personal constructs relating to compliance. The benefit of the methodology adopted in this study, is the ability to explore tacit knowledge of the practitioners whilst avoiding interviewer bias. Through construct elicitation this has allowed for analysis of the major issues that compliance officers face when considering their approach to compliance decision making.

Within the data presented in Analysis and Findings (Chapter 7), the following main findings were summarised with reference to research question 2a and 2b (extracted from Table 21).



Research Question 2a: What are the key constructs that influence managers' decision of compliance function approach?

Content Analysis of constructs – no supposition

Key Findings

Compliance officers' personal constructs have been classified into 12 categories from the 230 pooled constructs. The following categories were identified during analysis: resource; education and training; ethics and culture; reputation implications; skills and status of compliance officers; stakeholder considerations; communication and knowledge sharing; regulatory risk issues; principle as opposed to rule based concerns; barriers to compliance; nuisances and inefficiencies; and ritualism and gaming.

Three new categories of personal constructs are observed within the data set, which were not identified in the literature at point of creating the initial template i.e. barriers to compliance, nuisance and inefficiencies, and ritualism and gaming. Of these new categories 'barriers to compliance' was seen to be of medium/high in terms of both dominance and importance. The most dominant category was 'stakeholder considerations'. With respect to importance, the categories with similarity scores most closely aligned to benefit and cost considerations included 'nuisances/inefficiencies' and 'principle as opposed to rule based/spirit as opposed to letter of the law'.

The main themes identified within practitioners' constructs overlap with culture issues, where categories of 'barriers to compliance' and 'nuisance and inefficiencies' were highlighted. This signals that compliance officers' experiences are affected depending on the culture of the firm in which they operate. An indication of the status of these issues is the alignment of these constructs in respect to importance ranking, in comparison to the concepts of cost and benefit considerations to the organisations (see Section 7.2.1). By positioning the operational management of compliance resource outside of the organisation they serve (as presented in the theoretical model in Section 8.2), this may address some of these cultural issues and nuisances that compliance officers face in their daily quest for regulatory compliance.

In addition, the most dominant of construct categories related to 'stakeholder considerations' (see Section 7.3.4). This has been embedded within the theoretical model presented in Section 8.2 in the form of communication channels which are opened up (see Section 8.2.5). Instead of being directly employed by one of the major

stakeholders (the firm they operate within), and hence reliant from a personal perspective (i.e. job security), then compliance officers would be in a better position to act with complete independence and allocate a more equitable consideration of all stakeholders when considering compliance decision making. The implication would be to reduce the barriers facing regulatory compliance, from an individual compliance officer's viewpoint, as they would not face dependence barriers of being employed by the firms that they would serve.

Research Question 2a: What are the key constructs that influence managers' decision of compliance function approach?

Supposition 2 - Aspirational compliance experiences may include an abundance of positive connotation within the descriptors, and that worst compliance experiences may include an abundance of negative connotation within the descriptors given by participants.

#### Key Findings

When practitioners describe negative connotations of their experience the main drivers appear to be external factors and uncertainties (often outside control of compliance office).

Research Question 2b: How do compliance officers' personal constructs align to academic models of compliance?

Supposition 3 - If the scaling of aspirational compliance to worst compliance within the repertory grid were aligned to the linear scale of Jackman's model and contention of 'an ethos of ethical compliance' and 'unthinking mechanical compliance', the expectation would be for scoring of 1 for aspirational compliance (perceived as a benefit to organisation) and a scoring of 5 for worst compliance experience (perceived as a cost to the organisation).

#### Key Findings

Practitioners do not align perceptions of benefits and costs in a linear fashion, when comparing worst and aspirational compliance experience. Benefits are often achieved within difficult situations, and costs are often apparent in otherwise ideal scenarios. This challenges the traditional models presented within academic literature.

By purposely reviewing constructs surrounding both the worst and aspirational experiences of the compliance officers, a comparison to existing compliance models is possible. A significant finding of this study is that perceived benefits and cost (or positive and negative connotation) do not align fully with the linear scales presented in academic models (specifically Jackman's model and Ayres and Braithwaite's enforcement pyramid for regulatory compliance). There are costs associated with aspirational compliance, and there are benefits of worst compliance experiences. For example, when exploring benefits relating to worst compliance experience positive themes (albeit a minority) have emerged from review of these constructs indicating the benefits of practitioners sharing such experiences; through knowledge sharing these benefits can also be capitalised within other organisations. This notion is transferred to the conceptual model below by the inclusion of attributes of macro view and knowledge rotation. Even the worst experiences can then be used in future decision making in other organisations given the macro view aspect of the compliance trust. By rotating compliance officers between organisations, prior learning from experiences can impact and benefit other organisations within the trust.

### **8.1.3 Research objective 3: To investigate the circumstances under which different approaches would be adopted.**

#### ***8.1.3.1 Key points from the alternatives literature – shared services and consulting***

The central purpose of reviewing the regulatory and compliance literature was to obtain an understanding of models that are currently in place and to consider limitations in their use (i.e. questions of why, what and how, in response to objectives 1 and 2). However, the third research objective is more difficult to address as it is not a matter of theory building, but rather, unpicking of existing models and considering remoulding of concepts that are applicable to current regulatory compliance practice.

Therefore, alternative models of meeting regulatory compliance were reviewed within the literature search. Author bias from prior work experience, promoted the initial interest in consulting literature. Current practitioners also consider outsourcing and shared services options as valid routes to regulatory compliance. Arnold (2009) highlighted the associated costs within the “thriving consultancy industry”. However, there is limited empirical evidence presented in the literature related specifically to the use of compliance consultants<sup>105</sup>. Given the reported spend on consulting in the

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<sup>105</sup> Google Scholar search on “compliance consultant” and “financial service” yields 12 results, March 2015.

financial service industry<sup>106</sup> this seems to be an oversight by the academic community. Considering the focus on cost benefit studies for regulatory compliance, the additional costs associated with consultants would be seen as a quick win for practitioners to try to minimise. Therefore, this has been addressed in the compliance trust model presented in Section 8.2 (whereby consulting knowledge and costs would be spread across all stakeholders within the trust).

It is acknowledged that “competing organisations” already form “network, alliances and strategic partnerships” (Filatochev and Nakajima, 2010, p. 601) in order to collaborate in challenging environments<sup>107</sup>. However, there is much more focus in the literature on models for shared services and outsourcing. Economies of scale are discussed via transaction cost economics (Spekle et al., 2007; Widener and Selto, 1999, Lindvall, 2011). Concepts of centres of excellence are discussed by other authors (Ulbrich 2006; Herbert and Seal, 2012). These concepts are transferable to the proposed conceptual model within Section 8.2. The identified benefits of knowledge sharing, centres of excellence and economies of scale will apply within the network of the compliance trust. This will not run as a profit making endeavour as traditional consulting models and outsourcing options are arranged. However, the complexities of managing costs while delivering suitable services will mirror the problems currently encountered in practice in shared service/outsourcing models. Therefore, development of suitable performance indicators for each of the stakeholders would need to be balanced and assessed on a continuous basis, in the same way that shared service arrangements function.

#### **8.1.3.2 Key findings from the data – Research Question 3**

Within the data presented in Analysis and Findings Chapter, the following main findings were summarised with reference to research question 3 (extracted from Table 21).

Research Question 3: In cases of new regulation, how do compliance functions rely on external expertise (consultants) or is there proactive promotion of in house knowledge and expertise?

Supposition 4: The approach to new compliance is highly dependent on the resource constraints within the business.

<sup>106</sup> The Economist reported global spend of \$49 billion in 2012 by financial-services consulting business (one fifth of consulting industry total revenues) <http://www.economist.com/news/finance-and-economics/21586827-advisory-industry-has-shown-remarkable-resilience-crisis-advice-squad> accessed March 2015.

<sup>107</sup> An example in this case would be the British Banking Association.

## Key Findings

Themes of resource/costs of consultants and alternatives were dominant influences for decision making over use. However, credibility added in using consultants was also seen to be a dominant factor for decision making in use of alternatives. Barriers were again highlighted, when exploring this supposition with recurring theme of culture (management buy in) and also judgement (spirit/letter of the law)

Inherent differences into approaches to compliance were identified in discussions with practitioners. An emerging theme was the inevitable use of consultants and the credibility that this would add to ensure management buy in. This concept has been embedded within the conceptual model, with the advantage of combining use of consultants (when necessary) with knowledge sharing (thus, resulting in cost savings across the compliance trust).

## 8.2 Introduction of 'The Compliance Trust' conceptual model – theoretical rationale

Earlier chapters exploring the research objectives have considered the motivations behind regulatory compliance (via the literature review), and how compliance officers deal with their compliance issues on a day to day basis (through engagement with practitioners during the data collection process). However, the earlier discussions which triangulate the literature and the analysis of data set (under Section 8.1) do not fully address the final research objective.

Objective 3: To investigate the circumstances under which different approaches would be adopted.

The importance of this research objective is evidenced through the literature review, which indicates that academics (and practitioners) have been unable to develop fully functioning regulatory compliance models which overcome the complexities of practice within financial services, and avoid regulatory misconduct. The literature (and media) widely explores motivations behind regulatory misconduct due to the nature of public interest in the financial markets. However, solutions to the issues are yet to be identified and implemented. The data presented in earlier chapter also contributes to an understanding of the practical difficulties in achieving regulatory compliance. In order to meet Objective 3 a conceptual framework was developed through triangulation of literature and findings, as presented in Table 22.

Grounded within the summary of the literature and the results of data analysis discussed in the previous section, it is proposed that an alternative model for a centralised trust of compliance may address some of the issues faced by compliance teams within financial service organisations (an updated version is presented in Figure 51). There appears to be an unanswered question in both academic literature and practice based knowledge, as to whether compliance could be centralised to the degree of a shared service arrangement between multiple banks, under a model of 'The Compliance Trust'.

This model differs from traditional commercial consultancy or outsourcing. Costs would be controlled through the interaction between the shared service function, with the multiple banks controlling the budgets through a trust structure. The trust would follow the principles of a cost controlled service centre serving all of its stakeholders, rather than a profit making entity. This model will also differ from banking forum groups which are already in existence (such as the BBA) as the compliance officers working within the trust would be separated (independent) from the banking organisation that they would serve, promoting independence (and hence issues surrounding trust would exist within the resulting compliance community, rather than the individual banking organisations).

To be effective it is considered that five emergent attributes of; independence, a macroview, rotation and knowledge sharing, funding independence, and clear communication, are essential to overcome the barriers to regulatory compliance identified in the discussion in Section 8.1 (from the literature and the main findings of this study). The development of the five emergent attributes from triangulation of the supporting literature, and main findings from this study is summarised in Table 22. The theoretical rationale for each attribute (as evidenced in the review of literature and data in Section 8.1) is discussed in Section 8.2.1 to 8.2.5.

**Table 22 Summary of development of conceptual model, triangulation of existing literature and findings from this study, to formulate theoretical rationale and emergent attributes of the model**

| Supporting literature   | Link to findings   | Theoretical rationale   | Emergent attribute of model  |
|---|--|---|------------------------------|
| Ayres and Braithwaite – public interest groups (1992 onwards), Omarova – public interest council (2012), Levine - the Sentinel (2012)<br>Kenny – dependence corruption (2014)<br>Haynes – independence (2005)   | Culture barriers exist within organisation, which inhibit compliance. (Section 7.4, Section 7.4.4)<br>Compliance is viewed as a nuisance or business inhibiting. (Section 7.3)   | Avoidance of business inhibiting concepts, as trust would act as a discrete entity.<br>Avoidance of intimidation threats.<br>Clear route to ethical compliance.<br>Avoidance of culture issues of in house employment.  | Independence                 |
| Moshiran – global view (2011); Arnold – thriving consultancy trade (2009)<br>Concept of self-regulation (Stefanadis, 2003; Coglianese and Lazer, 2003; Ford, 2008 and 2011; Gilad, 2010; Calcott, 2010, Rossi, 2010)<br>Macro prudential focus/policy (IMF, 2010; Galati and Moessner, 2010, Baker, 2010) | Compliance professional actually benefit from worst compliance experiences, allowing continuous learning for future experiences. (Section 7.2.1, Section 7.2.2, Section 8.1.2.2)<br>Use of consultants is often inevitable. (Section 7.4). | Appreciation of the wider implications of regulatory compliance issues across industry (rather than an in house or business focused view).<br>Communication mechanisms in trust allow a macro view of regulatory compliance issues.<br>Meets the needs of the global financial institutions promoting cross border exchange of information.<br>Allows for collective use of consultants (when necessary only) to achieve greater good.<br>Strength of group allows for clear contribution to both businesses and regulatory bodies. | Macro view                   |
| Fuller and Sharma - regulatory academies model (2012), Concept of regulatory capture (Baker, 2010; Young, 2012; Harvey and Bosworth, 2013).   | Resource issues remain a major concern for practitioners. Despite expanded compliance industry expertise in recent decades, there  | Avoid issues of regulatory capture (or compliance trap) – lobbying could be strengthened from a compliance perspective.   | Rotation – knowledge sharing |



| Supporting literature  | Link to findings  | Theoretical rationale  | Emergent attribute of model  |
|--|---|--|------------------------------|
| Concepts of centres of excellence via shared service, (Ulbrich 2006; Herbert and Seal, 2012)<br>Knowledge studies (Nonaka) and information asymmetries (Brennan et al., 2015)  | remains issues balancing resources across different jurisdictions and organisations depending on regulatory demands. Use of consultants is often inevitable. (Section 7.4)  | Benefit from shared knowledge –allows for best practice (and self-regulation) amongst businesses within community via rotation (benefits of consulting without the cost)                                     |                              |
| Gap in Literature regarding equitable cost sharing and independence (however, implied by Public Interest Groups?)<br>Implications of normative behaviours in contrast to compliance costs (Malloy, 2003; May 2004)<br>Economies of scale concepts (Spekle et al., 2007; Widener and Selto, 1999, Lindvall, 2011) | Culture barriers exist within organisation, which inhibit compliance. (Section 7.4)<br>Resourcing issues are impacted by culture of firm. (Section 7.4)   | Equitable cost sharing across sector. Allow for economies of scale (transaction cost economics).<br>Salaries of compliance officers unlinked to businesses (and performance of businesses) they are serving. | Funding independence         |
| Jackman – firms value and culture role with regulator (2002); Woods partnership model (2002);, Edwards and Wolfe – compliance competence (2005)<br>Kenny – dependence corruption (2014)<br>Mitchell et al. (1997) – stakeholder salience<br>Braithwaite and Hong (2015) – Regulatory Ambassadors                 | Stakeholder issues form a dominant aspect of the participants construct formation during interview. (Section 7.3)<br>Compliance professional actually benefit from worst compliance experiences, allowing continuous learning for future experiences.(Section 7.2.1, Section 7.2.2) | Accountability amongst all parties.<br>Direct and unfettered communication channels with all stakeholder groups.<br>Equitable responsibility to all stakeholders.  | Clear communication channels |

### 8.2.1 Independence – theoretical rationale

The findings from this study indicate that significant barriers to compliance may exist when compliance officers are embedded within the businesses they serve, due to the common perceptions that compliance is business inhibiting. The literature has already called for independent public interest groups; therefore, the contention of this study would be to create a model of independence which would avoid any “dependence corruption” (Kenny, 2014) issues for the individual compliance officers.

Therefore, in the conceptual model independence of compliance officers from financial service firms would result in:

- Avoidance of business inhibiting concepts, as trust would act as a discrete entity, independent from the firms that the compliance officers would serve, focusing instead on public interests (Section 7.3).
- Avoidance of intimidation threats to individual compliance officers, due to independence from the banks they serve (which would minimise barriers to compliance, Section 7.3).
- A clear route to ethical compliance with minimised barriers to compliance (supporting Jackman’s model for ‘aspirational’ compliance), linked to public interests.
- Avoidance of culture issues of in-house employment at individual banking institutions – the compliance culture would be directed from the trust (Section 7.4 and 7.4.4).

### 8.2.2 Macro view – theoretical rationale

Note by stating macro view, it is considered that the trust operates at a macro level across the sector, rather than only the micro level within individual firms. The macro view concept also has some overlap with communication of knowledge (introduced in Section 1.3) and knowledge sharing (discussed in Sections 8.2.3). As argued within Section 8.1.1 the concept of macro view has been considered from a regulatory perspective (IMF, 2010; Galati and Moessner, 2010; Baker, 2010) but this has not been linked to the compliance officers’ perspective who are trying to maintain regulatory compliance.

By having a macro view community from a compliance officers’ perspective, this would allow the trust to benefit from the principles of self-regulation across the sector. As discussed in the data findings the compliance professionals benefit from their worst experiences, which allows for continuous learning at a macro view level within the trust.

Through self-regulation principles, the trust can learn and benefit from undesirable regulatory compliance experiences (Section 8.1.2), and benefit at the macro level across the industry. In addition, when consulting experience is required, again this can be considered at a macro level, with ultimate cost savings due to the global view that the compliance trust can adopt.

Therefore, in the conceptual model, the compliance trust community would benefit from:

- Appreciation of the wider implications of regulatory compliance issues across industry (rather than an 'in house' or business focused view, Section 8.1.1.1).
- Communication mechanisms in 'trust' allow a macro view of regulatory compliance issues (combined with learning from individual experiences, Section 7.2.1 and 7.2.2).
- Meets the needs of the global financial institutions promoting cross border exchange of information (Section 8.1.1.1).
- The trust structure allows for collective use of consultants (when necessary only) to achieve greater good, with dissemination of macro view knowledge across all individuals participating in the trust (Section 8.1.3).
- Strength of group allows for clear contribution to both businesses and regulatory bodies.

### **8.2.3 Rotation/Knowledge sharing – theoretical rationale**

The benefits of such a model would include a centralised hub of compliance expertise which could be rotated on periodic basis across financial institutions to ensure knowledge sharing. This model has indirect links to Nonaka's work on tacit/implicit knowledge and knowledge sharing (see Section 1.3), and also Brennan et al. (2015, p. 28) conceptual model of manager/non-executive directors information asymmetry. The macro view compliance community would provide a direct information link to the multiple stakeholder groups. Individuals' tacit knowledge would be expected to convert to a collective explicit knowledge which could be shared to address issues of the black box of financial service regulation and compliance.

Therefore, in the conceptual model, the compliance trust community would benefit through rotation of resource and ultimately:

- Avoid issues of regulatory capture (or compliance trap) – lobbying could be strengthened from a compliance perspective (Section 8.1.1).

- Benefit from shared knowledge –allows for best practice (and self-regulation) amongst businesses within community via rotation (benefits of consulting without the cost, Section 7.4)

Another indirect benefit of rotation will be to address any compliance culture issues that may arise. In Meidinger’s (1987, p. 372) discussion of regulatory communities, it is stressed that to affect “collective action”, a way of incorporating this is through systematic “change of membership”. This was written from the regulatory community perspective. However, the same principles may be applied to a corresponding compliance community such as the compliance trust.

#### **8.2.4 Funding Independence – theoretical rationale**

Funding could be provided on a fee basis from the banks they serve, with independence maintained by rotation of compliance teams servicing the individual banks (whilst benefiting from growth in central knowledge and expertise). Globalisation of standards and practice could be monitored and developed through interaction with the transnational groups, and the national regulators. The major advantage of such a shared approach to compliance would be seen to be cost and efficiency saving of sharing knowledge (for example, sharing of consultants and tooling).

Therefore, in the conceptual model, the compliance trust community would benefit from:

- Equitable cost sharing<sup>108</sup> across sector (Section 8.1.3).
- Allow for economies of scale (transaction cost economics).
- Salaries of compliance officers decoupled from the financial service organisations (and performance of organisations) they are serving, which would minimise barriers to compliance (dependence corruption, Section 8.1.2.1).

#### **8.2.5 Clear communication channels – theoretical rationale**

The service organisation could be made accountable to multiple stakeholder groups including not only the banks funding the enterprise, but also the country specific regulators and other transnational organisation interested in macro financial regulation, embracing the partnership model set out by Woods (2002), and also the latest direction of some regulators towards macro prudential regulation following the latest financial crisis. Resourcing this human relationship between the regulators (and other

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<sup>108</sup> A charging mechanism is not identified within this thesis, as neither the literature nor the findings provide an overall answer to this question. However, this is an important consideration to develop the model further in future research, as the trust would enable economies of scale (especially when resourcing for new pieces of regulation), and some sort of charging mechanism would need to be devised based on the relationship with firms they serve.

stakeholders) will be an issue, as previous findings in studies of financial service comment that where a lack of “human agency” exists then regulatory compliance will suffer (Smith, 2011).

Therefore, the benefits of the compliance trust model would include:

- Accountability amongst all parties through clear communication (and avoidance of miscommunication (Section 8.1.1.2).
- Direct and unfettered communication channels with all stakeholder groups (Section 8.1.1.1).
- Equitable responsibility to all stakeholders (8.1.2.2).

By positioning the compliance community as a central hub, accountable to numerous stakeholders whilst maintain independence this should counter the issues identified in the latest financial crisis of regulatory capture. Arora (2010) examined the work of the existing international regulatory bodies (e.g. IMF, BIS, BASEL Committee, FATF, FSB) – the compliance communities HR function could be monitored directly by these global public interest authorities.

However, the inevitable stumbling block to such an approach is trust – the banks have maintained in-house legal, risk and compliance functions for obvious reasons of confidentiality and trust, and, it is debatable as to whether these issues can be overcome in the proposed model. This will be discussed further under Section 8.3, when feedback from practitioners is considered.

### **8.3 Feedback from practitioners**

As discussed in Section 6.6.5, feedback on the Compliance Trust conceptual model was sought from practitioners (see Table 23). The purpose of this was to add rigour to the analysis and interpretation of practitioners’ constructs, performed within this chapter, and the Findings and Analysis, Chapter 7. This aligns to the methodological rationale of the Delphi method, via the systematic process of attempting to obtain group consensus with new aspects researched in the “post research” phase (Saizarbitoria, 2006). Along with summarised findings of the data collection process, practitioners were requested to consider the emergent attributes of the model and the theoretical rationale behind the model, and to comment on whether the model was feasible in practice. Practitioners were asked to consider the following questions specifically:

1. Do you agree that the stated attribute benefits compliance/risk management officers in pursuit of regulatory compliance?

2. Are there remaining barriers to regulatory compliance in the presented model/attributes?
3. Are the theoretical attributes of the model feasible in practice?

This also demonstrates a further iteration of the research design (see Figure 2), again reflecting the underlying philosophy of constructive alternativism. Feedback was obtained from existing participants, and also those who had expressed an interest in the research following data collection (through contacts made at conferences). In addition, whilst respondents were asked to provide feedback in a set format within reply emails (in response to the specified questions above), all respondents ignored this request and sent responses either through free format email or during extended discussions over the phone. This reflects an underlying issue in the majority of research: the researcher must be adaptable to the needs of the participants. Ultimately some excellent discussions ensued with participants which are presented below in Sections 8.3.1 to Section 8.3.5. A summary of the format of responses is set out in Table 23 below.

**Table 23 Summary of feedback providers, and format of feedback**

| <b>Respondent Reference</b>                  | <b>Assessment of Expertise</b>                                  | <b>Format of feedback provided</b>                 |
|--|---|--|
| <b>Feedback Participant 1 (FP1)</b>          | Participated in original study                                  | Email – written                                    |
| <b>Feedback Participant 2 (FP2)</b>          | Participated in original study                                  | Email – written                                    |
| <b>Feedback Participant 3 (FP3)</b>          | New participant – Director/Compliance Consultant                | Email/Telephone – written and verbal (notes taken) |
| <b>Feedback Participant 4 (FP4)</b>          | New Participant – Head of Risk and Regulation at Organisation X | Email/Telephone – written and verbal (notes taken) |
| <b>Academic Feedback Participant 1 (AF1)</b> | Regulatory and Compliance Literature                            | Email – written                                    |

Whilst acknowledging that the theoretical attributes were valid ‘in theory’, practitioners were not always fully supportive of the model. The quote below demonstrates the

continued divide between theory and practice, in terms of concerns of theoretical standpoints and the 'real world':

“Whilst I can appreciate the potential attraction of your proposed ‘Compliance Community’ model from a conceptual/theoretical standpoint I have some serious concerns as to how this could possibly work in the real world” FP 1

### 8.3.1 It's all about culture – the need to ensure a “Voice”

One of the concerns with the model was the issues of how culture is addressed.

“This is an issue on both sides; compliance taking a rigid uncommercial stance and, therefore, seen as a barrier to business whilst the business fails to appreciate the need to meet regulatory obligations. The good compliance officer/function is ‘commercial’ and works with the business to find solutions that, where possible, meets both needs; accepting that sometimes the answer has to be no. I struggle to see how this could work within your proposals” FP1

In response to this critique of the model, these cultural issues already exist within current frameworks. Although the model does not address these issues specifically it is inherent within the attribute of independence and communication that existing barriers (in the form of cultural issues) are minimised i.e. compliance officers in the trust will operate in a cultural environment which is set by the trust rather than the individual firms they serve, and through clear communication and accountability to all stakeholders, this will allow for a more desirable culture to develop across the entire sector.

Another participant (FP3) had also reflected on this from a personal viewpoint. Whilst considering her own experiences, and some of her ‘less fortunate’ colleagues, she stated that the reason she had had success in her role and avoided scandals was through her open access to the CEO. In order to ensure the right culture the compliance representative must have an appropriate ‘voice’. This was not identified in the initial draft of the compliance trust but is a vital consideration point. This could easily be remedied in the form of corporate governance codes, whereby the compliance trusts could act as Non-Executive Directors on the boards of firms that they represent (again on a rotation basis). This has been added within an outlying mechanism within the compliance trust model in Figure 51.

Another respondent (FP4) highlighted the issues around risk control frameworks across different jurisdictions (as a limitation to the model). He discussed the issues that



different regulatory jurisdictions apply varying methods of regulations, and due to the importance of relationships in the model, this may result in practical issues for implementation across jurisdictions. The respondent had experience of working in different sectors and countries and highlighted the inherent differences in the 'role of compliance' across jurisdictions. This then widens the culture related issue which was discussed at an organisational level by other feedback participants. He used the example of France to describe the interpretation of 'compliance' as more of an 'internal control/internal audit' function as opposed to the wider 'risk' definitions that are applied to compliance officers in countries such as the UK. This piece of feedback highlights issues of generalisability within the model in terms of how labels of compliance are viewed differently across jurisdictions. However, in defence of the model, and in response to this specific piece of feedback, these differences between jurisdictions have been overcome by the larger, global banking groups, and therefore, this would suggest that these barriers across jurisdictions are indeed surmountable in practice.

### **8.3.2 Consideration of the practicalities – resourcing and pay structures and regulatory permissions?**

A second concern is that of resourcing:

“Resourcing is an issue for some companies but effectively pooling the resource in the way you suggest begs serious questions as to the size of the team, who gets priority, how would cost share be established, limits on time available etc. I am aware of recent examples where huge resources have been brought in to address regulatory failings; HSBC for example hired thousands of people on short term contracts to resolve some of their customer due diligence issues.” FP 1

In response to this criticism of the model, again these resourcing issues already exist within current frameworks (as evidenced in the analysis chapter). Resourcing is already seen as an issue at the micro level of individual firms (and are currently managed within firms), therefore, this may be adapted in this model that resourcing can also be managed at the macro level of the compliance trust. That is not to say that resourcing does not remain an area of concern within the model, however, it may be argued that these are manageable risks within the model.

Another practical concern is how would the firms fund this, and how would the compliance trust salaries remain 'competitive' (FP 3). Ultimately the employees of the trust would have personal economic motivations, and career trajectory concerns when working under such a model. Again this would come back to corporate governance

considerations (i.e. in terms of remuneration committee roles), ensuring the right people in the right job for the right pay. The participant acknowledged, however, that the motivations of salary might be superseded by the protection that the trust would offer, whereby, 'shoot the messenger' concerns of working in the profession would be minimised (see discussion in Section 8.3.4).

A final concern in the model is that of regulatory permissions:

“there may still be inhibitors that prevent it working effectively....the lack of regulatory permission to allow for compliance responsibility to be outsourced....every firm would still need to have an expert to demonstrate their risk stance to the regulator” FP2

This perhaps is a misconception in the model. The only way that the compliance trust would ever be possible if there was a real shift in the current norms. This model does not represent outsourcing; there would remain a responsible expert. However, this would be collectively the trust, and the individual allocated to represent the trust in the firm at the point in time. Accountability to the regulator would remain at a firm level, with assurances and direct communication through the trust, and the nominated representatives of the trust. In an ideal world this would move back to trust and self-regulation with the sector.

### 8.3.3 A cynical view of consultants

Other practitioners considered that there were similarities in rationale to prior organisations which were set up for the purpose of smaller financial institutions to share knowledge:

“Mutual One provided compliance management for smaller institutions that struggled to afford appropriately qualified staff” FP 2

The motivation for such a structure was to allow for knowledge sharing and pooling of resources (which is part of emergent attributes of the compliance trust). However, ultimately Mutual One was swallowed up by RSM Tenon, evolving into Baker Tilley.

“More cynically, could it end up another income stream for PWC, or KPMG etc.”  
FP2

This concern was shared by another respondent (FP3) who stressed that to avoid falling into the consulting worldview, the compliance trust would have to position itself through the motivations of 'integrity' rather than 'economic' pursuits. A potential solution

they identified would be to position the trust alongside a 'recommending institute' or body with membership indoctrinated with the belief of social purpose rather than economic gain (with strict professional recognition and CPD criteria). This also resonates with the attribute of independence – to be truly independent the trust needs to strongly advertise the integrity and social purpose of the trust, to avoid the issues such as the expectation gap that has developed within the audit profession.

The audit expectation gap has been widely explored over the last century. Quoting Limpberg (1932):

“The audit function is rooted in the confidence that society places in the effectiveness of the audit and in the opinion of the accountant....if the confidence is betrayed, the function, too, is destroyed” (Porter, Simon and Hatherly, 2011, p. 197)

The issues of the audit expectation gap could so easily be transferred to a model such as the compliance trust, whereby the stakeholders (including the public) would need to be constantly reassured in the capabilities, independence and adequacy of communication mechanisms to maintain confidence. Therefore, the overriding attribute of integrity has been added as an overarching function of the model in Figure 51.

The attribute of independence was discussed further with FP4. He was very supportive of the concept of independence 'in theory', but highlighted that a number of practical issues existed. The first discussion raised the issue, of how involved the compliance personnel need to be. Ultimately to understand and promote effective compliance (in a truly advisory fashion) they need to be working at 'front line' within organisation. This of course was viewed as a barrier to independence. The second discussion with the same participant surrounded the issue of 'reward structures' for compliance. He argued that an impossible problem exists in practice of how to reward compliance with questions over how to assess 'good compliance', when you can often see compliance costs clearly, but cannot always quantify benefits of compliance (this links back to the literature in Section 3.5). In this scenario, how can compliance officers be seen to be acting independently when inappropriate reward structures exist, and where good compliance is so difficult to measure. In response to this specific feedback, the elements of the relationship of knowledge rotation within the compliance trust must be revisited.

Therefore, this is a practical problem, which needs to be addressed. However, there is a fine balance between familiarity and gaining appropriate knowledge about the firms

the compliance trust will serve. In response to the second issues of independence in contrast to reward structure – again this is a wider issue, and included within the overarching elements of integrity and culture within the trust. The relationship with industry leadership will be essential here, to ensure that appropriate mechanisms are in place to identify and measure good compliance.

#### **8.3.4 A real benefit – don't shoot the messenger**

A final discussion was held with participants about the potential of the model to protect compliance officers within their roles. This discussion also links to recent updates from the FCA, with reference to accountability.

The participant (FP3) discussed the 'furore' in the industry regarding the treatment of compliance personnel involved in Bahrain Bank<sup>109</sup>, whereby compliance was implicated and blamed, ultimately destroying the individual's career. The participant expanded and comments on the 'shoot the messenger' mentality, which results in a vicious circle between regulators and the firms.

"The regulators require more disclosure, the messengers don't want to admit to misdemeanours due to the sanctions (and personal implications) and so keep quiet." FP 3 (paraphrased from telephone interview notes).

This represents a direct conflict of ethical compliance when the risks exceed the rewards at a personal level, which then ultimately may lead to undesirable societal consequences. Indeed the risks at a corporate level are also clear whereby the FCA have issued significant fines in recent years, with comments from the industry to the stick rather than the carrot approach<sup>110</sup>. For example a recent press release in the FCA (discussing a sanction of £227 million) stated:

"Deutsche Bank's failings were compounded by them repeatedly misleading us. The bank took far too long to produce vital documents and it moved far too slowly to fix relevant systems and controls." (FCA, 2015)

This appears to implicate the compliance officers in terms of their actions (or inactions) which ultimately resulted in significant sanctions. Of course there are other examples of scandals where compliance officers have been implicated or scapegoated within the

<sup>109</sup> More details can be seen within media sites such as <http://compliance.com/the-american-banker-at-the-heart-of-the-middle-east-biggest-financial-scandal-says-he-was-treated-like-a-slave/> accessed June 2015.

<sup>110</sup> See media articles, commenting on the fines in excess of £2bn issues to industry since the FCA's incorporation. <http://www.bankingtech.com/273262/regulation-why-it-must-be-seen-as-the-carrot-rather-than-the-stick/> accessed June 2015.

media, and under this worldview the compliance officers form personal constructs and act accordingly depending on personal circumstance.

This is not a desirable situation from a societal viewpoint, and this relies heavily on the personal integrity of the individual compliance officers. The benefit of the compliance trust is the mechanism of employing compliance personnel as a collective, and representation as a collective. The fear of negative personal consequence for ethical action will be overcome, and clear communication between all parties is embedded within the compliance trust model.

The regulator has issued more recent guidance in July 2014 which partially addresses this issue of scapegoating of compliance professionals. Under the 'Senior Manager's Regime' accountability will apply at more senior levels. The effect is highlighted in a recent industry publication:

"This replaces the significant influence function element of the current Approved Persons Regime for those firms within the scope of the consultation, and is intended to focus accountability on a smaller number of the most senior individuals in a firm" (Ernst and Young, 2014)

Following final consultation the final version of the 'Fair and Effective Market Report' has been released jointly by HM Treasury, Bank of England and the FCA, on 10 June 2015. Whilst highlighting some progress in the financial markets, the report stresses that some gaps remain (specifically discussing the Fixed Income, Currency and Commodities (FICC) markets):

"First, the professionalism and accountability of individuals in FICC markets remains too low and variable. Second, key FICC markets lack effective mechanisms for agreeing, promulgating and adhering to common standards of market practice. Third, gaps remain in the coverage of regulation. And, fourth, there is more to do to raise standards in global markets, including those for spot FX." (HM Treasury, Bank of England, FCA, 2015, p. 11)

From this quote it is accepted within the industry that there are remaining issues in the standards within the financial market. The report goes on to discuss issues such as accountability and governance. This resonates with the findings of this study, and shows that steps are being taken to avoid the issues of 'shoot the messenger'.

Therefore, the concept of the voice (discussed under Section 8.3.1) should be reconsidered here, given the latest movement of the regulatory bodies with regards to

accountability. The matrix of decision making becomes very complex, when trying to balance independence, voice and accountability. As presented in Section 8.3.1, some practitioners contend that there needs to be appropriate respect for the compliance functions within the organisations they serve. In order to achieve voice, respect and appropriate accountability, compliance personnel need to be embedded within the firms themselves, which then contradicts with the independence concept. Another participant raised the issue of governance structures again arguing:

“If compliance was recruited and reported to audit committee chair (like outsourced internal audit) this would be different to say, where dominant CEO .....Interestingly shift in thinking this year from a couple of US regulators to the core UK model. US model, traditionally dominated by Legal. Best approach these days is direct to CEO with dotted line to independent NED Chair or Audit Chair” FP4

This participant strengthened the discussion on voice; however, the reporting lines were debated. FP3 contended that the reporting line should be direct to CEO, whereas FP4 contended that reporting lines should be via independent non-executives. Irrespective of these differences, which would no doubt vary across different jurisdictions and complexities of organisational structure, the concept of voice is an important feature for inclusion in the compliance trust model.

### **8.3.5 Academic feedback**

A number of academics were also approached for feedback on the model (who had influenced the direction of the literature review, and identified within the emergent theoretical attributes in the model). Unfortunately, limited replies were received due to conflicting workload demands of those approached, or those that did respond provided only brief comments about the research being ‘an interesting approach’. Despite a lack of time to respond fully, a number of the academics directed towards suitable literature to add to analysis process.

One respondent echoed the issues in implementing such models in practice:

“I suppose the difficulty is always about practical implementation. It is not the idea is impractical. I think it could work very well in practice. The difficulty is that the politics of getting people to agree to setting it up in the first place.”AF1

So although limited feedback has been obtained from academics to date, this statement discusses the real issues in taking such a model forward. It is debatable

whether organisation and compliance officers are suitably motivated (whether economically, politically or normatively driven) to adopt change in the sector unless another crisis occurs. Therefore, from a pragmatic (and practical) perspective the intention will be to present this model to the wider academic community (alongside practitioners) to refine and develop the model for potential future adoption.

#### **8.4 The 'Compliance Trust V2.0'**

To conclude, the feedback discussion above reflects that there were a number of gaps identified by practitioners in the initial model summarised in Table 22 (where the emergent attributes were theorised from the findings of this study, and existing literature as per Figure 50).

The purpose of the initial summarisation in tabular format was to “describe clearly how the data were interpreted” (Sinkovics, Penz and Ghauri, 2008). A second version of the model which incorporates the feedback discussed in Section 8.3 is presented pictorially in Figure 51. This model incorporates the five emergent attributes discussed in Section 8.2 (and summarised in Table 22): independence, macroview, rotation, funding independence and clear communication channels. The additional overarching principles of voice (in terms of governance, see discussion Section 8.3.4), culture (see discussion Section 8.3.1), and integrity (see discussion Section 8.3.3) have been incorporated as a result of feedback discussions with participants.

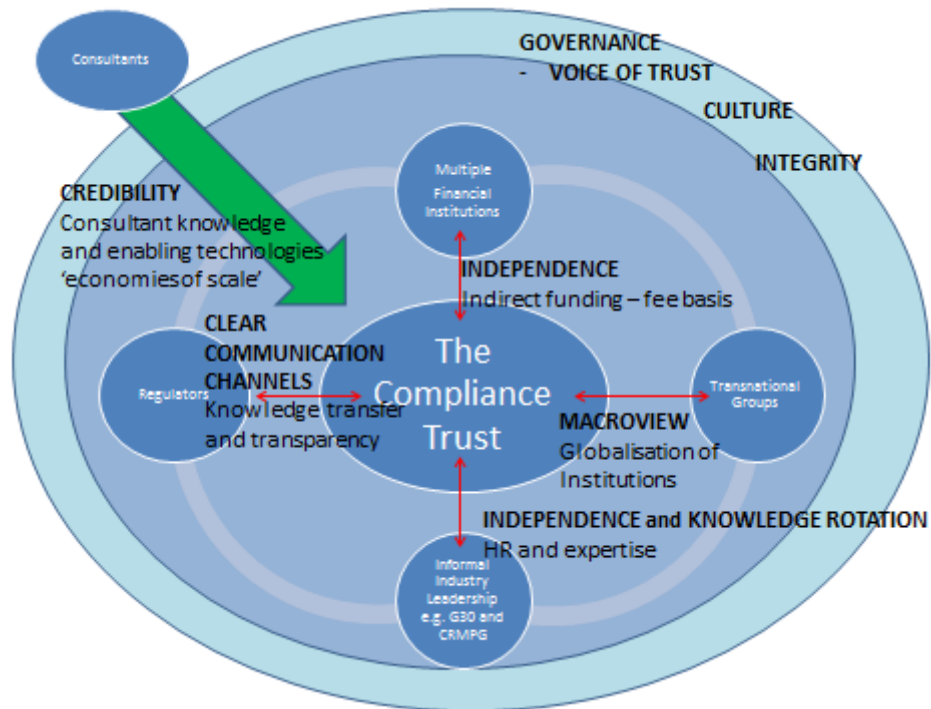
As discussed with Feedback Participant 4, this model will not be ideally suited across all financial service organisations, as it is almost impossible to integrate a model which deals with the differentials in size, complexity and internationalisation of all organisations. However, the intention is to take this model and present to a wider forum of both academics, and practitioners to consider whether the model has some merit in future for a majority of organisations in the ever expanding and internationalising financial service industry. It is acknowledged inherently, that one size does not fit all.

This model is presented as an original contribution to the literature. Feedback from academic expert (AF1) indicated the importance of producing a conceptual model which are accessible to practitioners (alongside academics) in order to bridge the academic/practitioner divide.

“I always think that it is good to have these ideas put forward in as practical a way as possible - so that when a crisis happens, and it becomes politically possible to make change, the model is there ready to be picked up and implemented.” AF1



Figure 51 Author developed model of shared service outsourced compliance community – ‘The Compliance Trust’



However, the contention would be that this model should be considered proactively ahead of any future crisis (rather than reactively in response to future crises). Therefore, this model has been developed from the worldview of the compliance practitioners, as opposed to the more frequently critiqued worldviews of regulators and policy makers, representing a contribution to the literature. The contribution to theory is revisited in Section 8.5.

The centralised structure of the trust would benefit jurisdictions where compliance officer/risk managers skills are in short supply, due to the inherent consolidation of knowledge, skills and experience within the trust structure. In addition, there has been recent media discussion of the ‘transient’ and ‘fluid’ nature of the workforce, whereby professionals are moving between organisations to gain experience, which is impacting on compliance risk<sup>111</sup>. However, the nature of the compliance trust would allow for this fluidity and career development within the trust itself (through rotation of roles), without the loss of expertise within the overall structure. This would provide a contribution to practice, to address this issue of transiency, and resourcing within the compliance profession. The implications on practice is revisited in Section 8.5.

<sup>111</sup> A 2015 article discussing this issue, and the impacts of ‘loyalty and commitment’ on compliance can be seen at [http://pwc.blogs.com/fraud\\_academy/2015/07/transient-nature-of-workforces-and-the-impact-on-compliance-programmes.html](http://pwc.blogs.com/fraud_academy/2015/07/transient-nature-of-workforces-and-the-impact-on-compliance-programmes.html)

One of the main findings of this research has been the continued issue of barriers to regulatory compliance. The suggestion of this study is that these barriers to compliance must be removed piece by piece, in order for future scandals to be avoided and for trust to be restored in the sector. By raising awareness across professionals in the sector of the issues, then organisations can work with stakeholders to effectively remove these 'in firm' barriers.

Via feedback, the compliance trust model is considered by practitioners as 'sound in theory' but not necessarily in practice. However, through raising awareness of potential alternatives and focusing practitioners on the real issues of barriers to regulatory compliance, this may enable the industry to raise responsiveness within individual firms and move closer to the goals of regulatory compliance. The central arguments of this thesis, whereby, 'compliance is a nuisance' are addressed within this model, by forcing the independent operation of the trust structure outside the direct control of the financial institutions that they serve (and instead focusing on the relationships with a range of other stakeholders). Initial steps could be taken by the profession in use of this model as an alternative to the existing mechanisms, as this model addresses some of the fundamental barriers to regulatory compliance within the sector.

## 8.5 Concluding this research thesis

"Research that uncovers, evaluates, explains, and critiques the workings of regulatory capitalism is, therefore, important for pragmatic, policy-oriented reasons, and also for more fundamental theory building reasons" (Parker and Nielson, 2009, p. 50)

The purpose of this section is to summarise the research journey taken within completion of this thesis. The original contributions of this study are presented in Section 8.5.1, including the implications on theory and practice (Sections 8.5.1.1 and 8.5.1.2). Limitations and future research direction are then considered in Section 8.5.2 and 8.5.3.

### 8.5.1 Original contributions and findings

There are four categories of original contribution identified in this study:

1. Contribution to method within this field of compliance study (introduced within Chapter 6);
2. Contribution to understanding of personal constructs of practicing financial service professionals (through analysis of grid and interview data in Chapter 7);

3. Unique findings emerging from this study to update the existing literature base from a compliance viewpoint (as opposed to a regulators viewpoint), to develop the compliance trust model (developed in Sections 8.2, with final model presented in Section 8.4);
4. Feedback from practitioners on theoretical model developed in this study (presented in Section 8.3).

The use of repertory grid in this study offers a contribution to method. Repertory grid has been widely used since the introduction of the technique by Kelly, in clinical psychology practice. The tool is considered a “powerful cognitive mapping tool” (Wright, 2008) allowing participants to interpret their experiences. As evidenced in a review of social science, and specifically business related studies the application has been widened by researchers to investigate diverse areas of the business literature, with wide use by marketing researchers (Rogers and Ryals, 2007), information systems (Thota, 2011; Alexander et al., 2008; Oppenheim et al., 2003; Lee and Truex, 2000), strategic management research (Wright, 2008; Wright et al., 2013; Panagiotou, 2007), and, project and performance management research (Song and Gale, 2008; Senior and Swailes, 2004; Duberley et al., 2000). However, there appears to be limited application of this technique in the regulatory compliance or financial service literature<sup>112</sup>. On interrogation of the literature that is available relating to financial services, the majority of the studies are actually unrelated to the compliance or risk management field<sup>113</sup>. Therefore, the first contribution is the use of methodological tool repertory grid in the specific research field of regulatory compliance. None of the practitioners interviewed were aware of this technique, although the majority saw benefits to being interviewed in this way to explore their experiences at deeper levels (rather than surface skimming in standard interview question and answer style). Therefore, it is argued that the data collated in this study represents tacit, explicit and implicit knowledge of practitioners.

The second contribution is represented in the empirical data set offered in the form of personal constructs. There are limited, recent studies within this field which contribute data representing the experiences of compliance officers in a period of regulatory flux.

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<sup>112</sup> Using the search terms "content analysis" and "repertory grid" and "financial services", Google Scholar yield only 80 results (as at May 2015), and only 5 results if the search term “compliance” is added, which indicates the limited application of this method within the literature in this field.

<sup>113</sup> For example Robertson, Gratton and Rout (1990) was found in the search to relate to financial services sector, but the method was directed towards situational interview assessment and job performance which is unrelated to compliance.

The particular strength of the adopted tool of repertory grid is the access to the “underlying reality” of practitioners (Rogers and Ryals, 2007). However, it must be acknowledged that there are limitations in this data set in terms of generalisability (as is the case for the majority of qualitative research). The data set, whilst rich in terms of the experiences of those interviewed, represents only a small sample of individuals working in the sector. Nevertheless, it is argued that the way in which data has been analysed and then presented back to the original participants (and indeed to new participants in the form of contacts made at conferences, and sought through academia) counters the issue of generalisability somewhat. The intention will be to take this model forward to both the academic and practice based community in future presentation and publications.

Thirdly, this study has been written from an unusual viewpoint, representing the worldview of the compliance practitioners rather than the more frequently argued views of the regulators and policy makers. By using this view, and combining with the existing literature, a conceptual model has been presented in order to address the barriers to compliance highlighted during data collection. Overcoming barriers to regulatory compliance has benefits for a number of stakeholders impacted by regulatory compliance. The model will be of particular use to jurisdictions where compliance officer/risk managers are in short supply, as a centralised trust will act as a consolidation point for knowledge, skill and experience.

Finally, and most importantly for research impact, the compliance trust model theorised from the review of the literature and the main findings of this study, has been presented back to practitioners for feedback (as discussed earlier in Chapter 8). The purpose of obtaining feedback on the theoretical model was an attempt to bridge the theoretical/practice gap (along with addressing concerns over generalisability). The feedback has been considered, and further arguments have been presented to underpin the strength of the theoretical model.

#### ***8.5.1.1 Implications on practice***

The review of the literature highlighted the increasing status of compliance and risk management within the financial service sector. However, despite the increasing resources within the function the data collated from practitioners emphasised that barriers to compliance are impeding regulatory compliance, which ultimately impacts society in a negative manner (as evidenced in the on-going scandals plaguing the sector, discussed in Section 1.0).

To restore trust in the sector following the global financial crisis, increased regulatory pressures have been applied by policy makers across the world. However, these regulatory pressures have not fully addressed issues of non-compliance in the sector (again evidenced by on-going scandals within the sector).

Therefore, this study offers a potential alternative approach for practitioners and policy makers (presented in Section 8.4). Whilst traditional models of compliance have their own relative merits and drawbacks, perhaps a fresh perspective is required to force organisations to face the barriers to regulatory compliance. This study has involved discussions with practitioners who are striving to achieve regulatory compliance, but face barriers in their day to day business where compliance is seen as business inhibiting.

However, it must also be noted at this point that the contribution to practice is often lost through the publication mechanisms within academia. Pfeffer (2007) critiques the disconnect between business research within academia and practice, blaming the mechanisms of unreliable peer review and structure of career progression within business schools for the lack of impact within practice, and on public policy. The lack of academic input in contemporary management ideas is highlighted by a number of publications and reviews of “management innovations” (Pfeffer, 2007), which is in contrast to other fields of research such as medicine and engineering.

#### **8.5.1.2 Implications for theory**

“Academic colleagues expect new knowledge and theoretical insight. Organization managers anticipate practical recommendations” (Buchanan and Bryman, 2007, p. 494)

As a result of general discussions with practitioners within this study, it may be argued that practitioners rarely consider theory during practice. This is not a new phenomenon (as evidenced in quote above). However, one of the main conclusion drawn from this study is that there needs to be more interaction between practitioners and academics to resolve the remaining practical issues that remain within theories and models presented by academics. Indeed, the complexities within the subject matter of compliance do not facilitate easy application to one specific theory.

Perhaps the real problem with theory creation (and inclusion of practitioners) lies within the categorisation of theories by researcher to frame their research in terms of grand theories, middle range or mini theories, and emergent theories/concept development. Ultimately practitioners are uninterested in grand theories for their day to day issue,

due to their inherent ambiguity – so they would be most interested in emergent theories based on current research, whereas ambitious academics are always be striving for contribution towards mini and grand theories.

Indeed to summarise this research, the framework for the methods employed of repertory grid evolved from the cognitive theories of Kelly, to align to constructive alternativism within epistemology, which in turn aligns to the pragmatic ontology (see methodology, Chapter 6, Figure 14). Therefore, this study has used grand theory to frame the research, in order to contribute a model which influences emergent theory, which may in turn impact practice.

The compliance trust model developed from this research draws most notably from institutional theory (DiMaggio and Powell, 1983), whilst also considering the somewhat conflicting economic, social and normative motivations for compliance (Parker, 2012). However, as discussed in Section 8.2, within the compliance trust model institutional theory would apply in a different way to traditional models of compliance; with emphasis on the relationships between the stakeholders and the compliance trust (most specifically from the coercive perspective within these relationships). Mitchell et al. (1997) also argue that many grand theories are used to explain the underlying stakeholder relationships:

“Agency, resource dependence, and transaction cost theories are particularly helpful in explaining why power plays such an important role in the attention managers give to stakeholders” (p. 863)

Therefore, the compliance model is ultimately underpinned by these grand theories which help to explain the conflicting relationships that will emerge in the compliance trust structure. The major development, as argued in Section 8.2 and 8.3 is that in order for the sector to move forward barriers to compliance need to be removed for compliance officers who currently sit within the financial service industry. Ultimately, the arguments presented for the compliance trust, indicate that some barriers (albeit, not all) will be removed by creating the attributes of independence (and funding independence), knowledge sharing, macro view, and clear communication channels (See Figure 51).

The network of compliance officers will need to balance the conflicting social, economic and normative attributes, across the financial service organisations they serve, but in an equitable manner to meet the needs of all stakeholders. Links to Kohlberg’s moral development are also made with implication on the professionals that would be

employed within the compliance trust. Through involvement of informal industry leadership in Human Resources<sup>114</sup>/policy making within the trust then appropriate individuals with higher levels of moral reasoning may be identified to promote the overall morality within the trust.

In summary, in order for a shift in compliance culture to be fully realised the combined contribution to both practice and academic theory need to be coherently combined and progressed. Practice need to acknowledge and remove existing barriers to regulatory compliance, and the conceptual framework within this study needs to be communicated within the academic community for discussion against higher levels of theory.

### 8.5.2 Limitations of this study

As acknowledged already within Chapter 6, limitations exist within the chosen methodology. However, it is also argued in order to align to personal philosophy, that the methodological choices made were inevitable. In addition, not all of the initial questions identified at proposal stage (specifically, from an accounting background focussing on cost benefit concerns) have been addressed. However, under the advisement of supervision team, the only way to move forward through the research process was to focus on achievable objectives and research questions.

As for the majority of research undertaken, the resulting data has been manufactured (Silverman, 2013). However, the usual issues around manufactured data (i.e. researcher bias and influence) have been minimised to an extent due to the open exploration of personal constructs of the participants.

Many would also argue that the lack of generalisability of this research due to the qualitative design is also a weakness. However, again due to exploratory nature of this research the possibility of a quantitative approach was simply not suitable to answer the research questions which resulted from the review of the literature. Indeed there has been recent quantitative research performed in this area (funded by commercial means) to explore the issues faced by the financial service industry. However, this simply does not provide the depth required to fully interpret the issues faced by compliance professionals. Despite the inherent differences in research design, the conclusions of the quantitative research compliments the findings of this thesis

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<sup>114</sup> An expectation would be that the informal industry leadership would play a role in recruitment, selection and oversight of management within the trust to ensure that the right people (i.e. in terms of morality and ethical concerns) are retained to ensure the principles and motivations of the trust are maintained (i.e. societal benefit as opposed to a profit making entity – see Section 8.3.3).



whereby the issue of communications and transparency is seen as a major concern (and required for remedy):

“Without an aggressive plan to stamp out misconduct, we are simply sitting and waiting for another financial disaster to strike. We needn’t be so powerless. We can formulate and initiate such a recovery plan, but it must start with an implicit partnership between employees and employers to speak up about possible wrongdoing in the workplace.” (Tenbrunsel and Thomas, 2015, p. 9)

Therefore, it is reasoned that whilst the findings of this study may not be generalisable, they provide a complimentary exploratory depth to other more generalisable quantitative studies around the same issues facing the sector.

The final acknowledgement of limitations must be around the issue of compliance culture. Although there has been overlap and discussion throughout this thesis, the issue of compliance culture is not fully resolved or theorised within this study. Whilst specific discussion has been made with respect to compliance culture (see Section 8.3.1) the model that has been presented in this study does not address culture explicitly. Although the presented model removes some of the barriers created and impacting on compliance culture, the issues is seen as entirely too complex to be embodied or solved within a theoretical model. Meidinger (1987) criticises research in which culture is presented in a “diffuse, inconsistent, and often simplistic ways”, consequently, this thesis does not claim to add to the range of the culture literature which is already in existence around the topic of regulatory compliance. More recently academics have discussed culture from the perspective of the regulator (O’Brien et al., 2014; Ring et al., 2014). Ultimately, further (more specific) research is required to explore compliance culture more fully (from the perspective of the compliance officer).

There may also be scope for further research with regards to accountability which has been mentioned briefly in Section 8.3.4, given the most recent publications by the FCA (on accountability allocations of responsibility). Within a separate consultation paper examples of allocating senior management responsibility are provided (FCA, 2015b, pp. 24-25), including:

“Responsibilities for overseeing the adoption of the firm’s culture in the day to day management of the firm” (FCA, 2015b, p. 24, Figure 5)

This seems an extremely wide area of responsibility, and it seems a little simplistic for this to be allocated to a responsible person given the complexity of culture in practice.

This is outside the scope of this study, given the timing of these consultations (in 2015), so can be considered an area for future research.

### 8.5.3 Future research

In order to capitalise on the evident interest in the topic of regulatory compliance (as evidenced by the number of events and conference organised for practitioners) the intention will be to move forward with the theoretical model presented in this study, and to consider whether this model may be adopted in practice across other jurisdictions.

In addition, areas that have not been investigated in this study (due to limitations identified in the methodology chapter and also above in Section 8.5.2) will be further explored and incorporated more fully in the theoretical model presented i.e. specifically culture and cost benefit implications.

The complexity of the issue of regulatory compliance necessitates further research, as the boundaries of compliance are so wide within the financial service arena. 'One size' is unlikely to fit all, and a greater understanding of the issues facing practitioners in the rapidly changing regulatory environment is essential from both the regulators viewpoint, and from a wider societal viewpoint (in terms of the impacts seen in instance of non-compliance).

In addition, a number of potential research avenue identified within the literature review have not been fully explored in the thesis. As identified at the end of the review of literature there are a number of outstanding gaps in the literature including the following research question:

Future RQ: To what extent do compliance officers monitor cost of compliance?

The literature in the area of costs of compliance is fairly aged, or written from a consulting viewpoint (i.e. specific reports via consulting bodies such as Deloitte/Oxera). The intention will be to take this forward and combine the risk management and accounting literature (with regard to functional costing) to provide a more updated and theory driven study around the issues of compliance costs, given the increasing burden of regulatory demands.

Future RQ: What are the educational and career attributes of financial service chief compliance/risk managers?

Again the literature in this area seems to be more practitioner driven, rather than academic. However, there are important links to this topic in terms of connections

between academic ethical theories, linking to the professional concerns of practitioners. Indeed during discussion with one feedback participant, they specifically comments on the diversity of backgrounds in the sector, and seemed to have taken personal insult, as to why many of the profession were from a Chartered Accountant background, when she considered the persons best suited to the role need to have been involved in the 'business' before moving to compliance. Therefore, this future research question will again bridge the academic/practice divide in that the field of study will provide insight to both academic theory and the profession.

## 8.6 Final Conclusion

Personal motivations behind exploring this topic area have evolved alongside the continuing interest in regulatory compliance within both the academic community and the wider media. An initial (and naïve) assumption was that an answer would exist to solving the regulatory compliance issues plaguing the financial sector. However, via interaction with practitioners a more realistic and sympathetic tone has been adopted within this study. Through contact with compliance professionals, the sheer diversity of issues facing professionals in their day to day operations appears to provide an insurmountable hurdle to full regulatory compliance. During discussion with practitioners this point was very clearly highlighted in feedback which reflects the continued divide between theory and practice:

“There are many companies where the compliance function works very effectively with the business, adding value and achieving the objectives the regulations are there to encourage. The fact that there are companies failing the compliance test is due to a wide variety of factors, some of which you have identified, but sadly I do not think your proposals present a viable practical solution to address them” FP 1

Therefore, it must be acknowledged that this study merely highlights operational issues faced by professions, and does not adequately offer a full solution to the problem. However, it may be argued by taking small steps to remove some (if not all) of the obstacles presented in practice, then further exploration of this complex topic will be possible. Indeed, this topic is of such importance from a societal viewpoint that we cannot simply ignore the obstacles and carry on regardless. To revisit a second piece of the feedback on the model:

“I suppose the difficulty is always about practical implementation. It is not that the idea is impractical. I think it could work very well in practice. The difficulty is that the politics of getting people to agree to setting it up in the first place.”AF1

Therefore, the future objective for research in this area is one of persuasion. Persuasion that the model is viable to practitioners in an imperfect world, and, persuasion, that small steps are required to overcome the obstacles facing practitioners.

To conclude, the only way to create a path forward towards the goal of regulatory compliance is through greater collaboration between academics (who have time to think) and practitioners (who have to live it). This study infers that the academic/practitioner divide appears to be inhibiting progress towards regulatory compliance. Ultimately benefits are to be gained from a societal viewpoint, if the goals of academics and professionals are aligned to study these obstacles more fully (and in partnership).

## Appendix 1 Construct listing/categorisation

| Categories  | Construct Pairs  |  | Number of paired constructs | % Constructs | % Similarity | HIL Value |
|---|--|--|-----------------------------|--------------|--------------|-----------|
| Resource – costs and benefits, monitoring of resources. |  |  | 15                          | 13           | 38           | M/H       |
|   | Adequate resources in place to enable policies and procedures to be followed | Lack of key staff to identify and fix problems |                             |              | 75           | h         |
|   | effective  | no added benefit                               |                             |              | 67           | h         |
|   | Costs with no tangible benefit   | Front end development cost for later gain      |                             |              | 67           | h         |

| Categories | Construct Pairs                         |                                       | Number of paired constructs | % Constructs | % Similarity | HIL Value |
|------------|---|---------------------------------------|-----------------------------|--------------|--------------|-----------|
|            | Time consuming                          | not time critical, not time consuming |                             |              | 58           | h         |
|            | done daily                              | done infrequently                     |                             |              | 50           | h         |
|            | lengthy process                         | quick process                         |                             |              | 42           | m         |
|            | regular                                 | one off                               |                             |              | 42           | m         |
|            | Significant time expenditure            | Fairly light on resource requirements |                             |              | 42           | m         |
|            | more resource required to drive forward | only need one person to complete      |                             |              | 33           | m         |
|            | more time consuming                     | less time needed                      |                             |              | 33           | m         |

| Categories                    | Construct Pairs             |                              | Number of paired constructs | % Constructs | % Similarity | HIL Value |
|-------------------------------|-----------------------------|------------------------------|-----------------------------|--------------|--------------|-----------|
|                               | high project cost           | low project cost             |                             |              | 25           | l         |
|                               | routine                     | one off project              |                             |              | 17           | l         |
|                               | similar volumes             | inconsistent/irregular       |                             |              | 8            | l         |
|                               | Saved money/made money      | Costs money                  |                             |              | 8            | l         |
|                               | one off implementation cost | ongoing (e.g. license) costs |                             |              | 0            | l         |
| <b>Education and Training</b> |                             |                              | <b>11</b>                   | <b>10</b>    | <b>27</b>    | <b>M</b>  |
|                               | training provided           | little training provided     |                             |              | 50           | h         |



| Categories | Construct Pairs                 |   | Number of paired constructs | % Constructs | % Similarity | HIL Value |
|------------|---------------------------------|---|-----------------------------|--------------|--------------|-----------|
|            | no training                     | training provided                                     |                             |              | 50           | h         |
|            | self-learning                   | structured training provided                          |                             |              | 42           | m         |
|            | Process could be taught         | Understanding "why" requires experience and judgement |                             |              | 42           | m         |
|            | difficult to implement          | easy to implement                                     |                             |              | 33           | m         |
|            | ease of use                     | specialist training                                   |                             |              | 33           | m         |
|            | uncertainty of results/delivery | results should be certain/straightforward             |                             |              | 25           | m         |
|            | Skills                          | Dumbed down   |                             |              | 17           | l         |

| Categories                | Construct Pairs                            |                            | Number of paired constructs | % Constructs | % Similarity | HIL Value |
|---------------------------|--|----------------------------|-----------------------------|--------------|--------------|-----------|
|                           |  | process                    |                             |              |              |           |
|                           | complexity - many inputs with diversity    | relatively straightforward |                             |              | 8            | l         |
|                           | complexity of delivery                     | lacks complexity           |                             |              | 0            | l         |
|                           | Complex, challenging project               | One off, 1 hour workshop   |                             |              | 0            | l         |
| <b>Ethics and Culture</b> |  |                            | <b>6</b>                    | <b>5</b>     | <b>36</b>    | <b>M</b>  |
|                           | Positive behaviour, desire to get it right | Morally corrupt            |                             |              | 75           | h         |

| Categories | Construct Pairs   |  | Number of paired constructs | % Constructs | % Similarity | HIL Value |
|------------|---|--|-----------------------------|--------------|--------------|-----------|
|            | Should be identified and fixed by management and compliance | Need to consider whistleblowing                          |                             |              | 50           | m         |
|            | Minor issues - volume/frequency being the difference        | More serious omission, message from the top (wrong tone) |                             |              | 42           | m         |
|            | No significant culpability                                  | Consider changes at senior management level              |                             |              | 25           | l         |
|            | concerned with organisational culture                       | process/format point                                     |                             |              | 17           | l         |

| Categories   | Construct Pairs  |   | Number of paired constructs | % Constructs | % Similarity | HIL Value |
|--|--|---|-----------------------------|--------------|--------------|-----------|
|  | Personal integrity                                     | Professional requirement                      |                             |              | 8            | l         |
| <b>Reputation/ Best practice consideration/Proactivity of Management</b> |  |   | <b>15</b>                   | <b>13</b>    | <b>37</b>    | <b>M</b>  |
|  | Viewed negatively at a management level                | Seen as exciting opportunity, positive        |                             |              | 75           | h         |
|  | Senior management actively support corrective measures | Reports, complaints ignored at a senior level |                             |              | 75           | h         |

| Categories | Construct Pairs                    |                                   | Number of paired constructs | % Constructs | % Similarity | HIL Value |
|------------|------------------------------------|-----------------------------------|-----------------------------|--------------|--------------|-----------|
|            | external pressure                  | internal desire to change         |                             |              | 58           | h         |
|            | direct reputational impact         | some limited impact on reputation |                             |              | 50           | h         |
|            | Focused on internal process        | Wholly driven by client           |                             |              | 42           | m         |
|            | protects customer                  | reduces cost (capital)            |                             |              | 33           | m         |
|            | damages reputation to stakeholders | enhances image of organisation    |                             |              | 33           | m         |
|            | must do                            | wish to do                        |                             |              | 33           | m         |

| Categories | Construct Pairs  |  | Number of paired constructs | % Constructs | % Similarity | HIL Value |
|------------|--|--|-----------------------------|--------------|--------------|-----------|
|            | Senior individuals not wishing to follow a compliance agenda | Senior management vest control in compliance       |                             |              | 33           | m         |
|            | Different agendas - conflict                                 | Business wishes compliance to effect this function |                             |              | 33           | m         |
|            | longer 'term' issue  | short term   |                             |              | 25           | m         |
|            | protects customer  | protects bank                                      |                             |              | 25           | m         |
|            | commercial necessity   | commercial 'nice to have'                          |                             |              | 25           | l         |

| Categories  | Construct Pairs                      |                                    | Number of paired constructs | % Constructs | % Similarity | HIL Value |
|---|--------------------------------------|------------------------------------|-----------------------------|--------------|--------------|-----------|
|   | seniority of management input        | limited senior engagement required |                             |              | 17           | I         |
|   | deal with identification of customer | monitors customer activity         |                             |              | 0            | I         |
| <b>Skills and Status of Compliance - experience, knowledge, education and hierarchy within organisation</b> |                                      |                                    | <b>3</b>                    | <b>3</b>     | <b>11</b>    | <b>L</b>  |
|   | Personal integrity important factor  | Lower key - face less challenge    |                             |              | 17           | I         |
|   | Compliance experience and            | Specialist knowledge not required  |                             |              | 17           | I         |



| Categories  | Construct Pairs                                |                                       | Number of paired constructs | % Constructs | % Similarity | HIL Value |
|---|--|---------------------------------------|-----------------------------|--------------|--------------|-----------|
|   | competence                                     |                                       |                             |              |              |           |
|   | skilled judgement and expertise required       | more process based - standardised     |                             |              | 0            | l         |
| <b>Stakeholder Considerations - Input from external departments/resource/consultants. In-house, in comparison with shared services/outsourcing considerations</b> |  |                                       | <b>18</b>                   | <b>16</b>    | <b>33</b>    | <b>M</b>  |
|   | Looking outwards to third parties (not client) | Close direct relationship with client |                             |              | 75           | h         |
|   | emotional                                      | more                                  |                             |              | 67           | h         |

| Categories | Construct Pairs                      |  | Number of paired constructs | % Constructs | % Similarity | HIL Value |
|------------|--------------------------------------|--|-----------------------------|--------------|--------------|-----------|
|            | element to delivery                  | factual/straightforward                          |                             |              |              |           |
|            | Compliance only involved in activity | Bigger impact on non compliance resource e.g. IT |                             |              | 50           | h         |
|            | Involved many stakeholders           | Involved 5-6 stakeholders only                   |                             |              | 50           | m         |
|            | in house                             | consultant led                                   |                             |              | 42           | m         |
|            | Working with experts                 | Yes - but business take on team only             |                             |              | 42           | m         |
|            | major system development             | single aspect IT development                     |                             |              | 33           | m         |
|            | could outsource                      | in house   |                             |              | 33           | m         |

| Categories | Construct Pairs   |  | Number of paired constructs | % Constructs | % Similarity | HIL Value |
|------------|---|--|-----------------------------|--------------|--------------|-----------|
|            | consultancy firm could do this (simple tasks, easy to spot mistake) | complex, need to keep focus                    |                             |              | 33           | m         |
|            | organisation wide   | contained in compliance                        |                             |              | 25           | m         |
|            | emotional debate  | little emotion                                 |                             |              | 25           | m         |
|            | procedures to follow  | project management required                    |                             |              | 25           | l         |
|            | procedures to follow  | engages stakeholders with different skill sets |                             |              | 25           | l         |

| Categories | Construct Pairs              |   | Number of paired constructs | % Constructs | % Similarity | HIL Value |
|------------|------------------------------|---|-----------------------------|--------------|--------------|-----------|
|            |                              | (e.g. IT customer facing)               |                             |              |              |           |
|            | complex stakeholders         | limited local stakeholders              |                             |              | 17           | l         |
|            | broad range of stakeholders  | relatively narrow range of stakeholders |                             |              | 17           | l         |
|            | info stored on bank systems  | no system storage required              |                             |              | 17           | l         |
|            | wide ranging project teams   | focussed project development            |                             |              | 17           | l         |
|            | major system change required | off shelf compatible software           |                             |              | 0            | l         |

| Categories                                 | Construct Pairs                        |                                      | Number of paired constructs | % Constructs | % Similarity | HIL Value |
|--|--|--------------------------------------|-----------------------------|--------------|--------------|-----------|
| <b>Communication and Knowledge Sharing</b> |  |                                      | <b>4</b>                    | <b>3</b>     | <b>33</b>    | <b>M</b>  |
|  | No opportunity to sell skills/services | Potential to sell products/service   |                             |              | 50           | h         |
|  | Process based on factual data          | Rationale may require outside advice |                             |              | 33           | m         |
|  | Communication skills and effectiveness | Question of knowledge                |                             |              | 25           | l         |
|  | Liaison with other firms               | No liaison                           |                             |              | 25           | l         |
| <b>Regulatory risk</b>                     |  |                                      | <b>8</b>                    | <b>7</b>     | <b>36</b>    | <b>M</b>  |

| Categories | Construct Pairs                                   |  | Number of paired constructs | % Constructs | % Similarity | HIL Value |
|------------|---|--|-----------------------------|--------------|--------------|-----------|
|            | potentially serious consequences                  | consequences are less impactful                                    |                             |              | 50           | h         |
|            | event   | regulatory requirement, procedure                                  |                             |              | 42           | h         |
|            | low risk as no penalties                          | if outsource, to high risk (serious regulatory fines if get wrong) |                             |              | 42           | h         |
|            | Safer activity as following explicit instructions | Risk of legal exposure if it goes wrong                            |                             |              | 42           | m         |
|            | financial impacts                                 | little direct financial  |                             |              | 33           | m         |

| Categories   | Construct Pairs                  |  | Number of paired constructs | % Constructs | % Similarity | HIL Value |
|--|----------------------------------|--|-----------------------------|--------------|--------------|-----------|
|  |                                  | input  |                             |              |              |           |
|  | risk involved in making progress | little risk involved                         |                             |              | 33           | m         |
|  | Directly involved regulator      | didn't involve regulator                     |                             |              | 33           | m         |
|  | Same regulation                  | Commercially driven, not regulation specific |                             |              | 17           | l         |
| <b>Principles, as opposed to rule based – spirit, as opposed to, letter of law (judgement)</b> |                                  |  | <b>9</b>                    | <b>8</b>     | <b>54</b>    | <b>H</b>  |
|  | common sense approach            | unhelpful approach                           |                             |              | 83           | h         |

| Categories | Construct Pairs   |   | Number of paired constructs | % Constructs | % Similarity | HIL Value |
|------------|---|---|-----------------------------|--------------|--------------|-----------|
|            | formal structure  | not formalised                                  |                             |              | 83           | h         |
|            | exhibits lack of foresight                              | based on sound principles                       |                             |              | 67           | h         |
|            | vague information                                       | Focussed  |                             |              | 67           | h         |
|            | Required to follow law/instructions without own thought | Skills required in creating system – experience |                             |              | 58           | h         |
|            | Contact may be motivated by confidentiality             | Rationale is never confidentiality itself       |                             |              | 42           | m         |



| Categories   | Construct Pairs                                 |   | Number of paired constructs | % Constructs | % Similarity | HIL Value  |
|--|---|---|-----------------------------|--------------|--------------|------------|
|  | Judgement Required                              | Black and white   |                             |              | 33           | m          |
|  | procedural                                      | No two procedures the same                              |                             |              | 25           | l          |
|  | use past editions (procedures) to update to now | specialised - starting from scratch (no starting point) |                             |              | 25           | l          |
| <b>Barriers to compliance - internal processes and procedures issues not addressed in above categories (i.e. not ethics/culture, skills, resource)</b> |   |   | <b>14</b>                   | <b>12</b>    | <b>41</b>    | <b>M/H</b> |
|  | change process                                  | barriers to change                                      |                             |              | 92           | h          |

| Categories | Construct Pairs             |                                     | Number of paired constructs | % Constructs | % Similarity | HIL Value |
|------------|-----------------------------|-------------------------------------|-----------------------------|--------------|--------------|-----------|
|            | No job satisfaction         | Major achievement                   |                             |              | 83           | h         |
|            | Limited value               | Compliance, Governance improvements |                             |              | 83           | h         |
|            | money laundering prevention | security prevention issues          |                             |              | 58           | h         |
|            | process                     | errors occurred                     |                             |              | 50           | h         |
|            | lending scenarios           | non lending scenario                |                             |              | 33           | m         |
|            | clear process               | complex (undefined) process         |                             |              | 33           | m         |
|            | process to return           | overview                            |                             |              | 33           | m         |

| Categories | Construct Pairs                       |  | Number of paired constructs | % Constructs | % Similarity | HIL Value |
|------------|---------------------------------------|--|-----------------------------|--------------|--------------|-----------|
|            | funds                                 |  |                             |              |              |           |
|            | Objective is identity data collection | Client is not relevant. Objective is understanding "why" |                             |              | 33           | m         |
|            | non lending process                   | lending process  |                             |              | 25           | m         |
|            | customer facing process               | non customer process                                     |                             |              | 17           | l         |
|            | specific process                      | generic process  |                             |              | 17           | l         |
|            | related to products                   | non product specific                                     |                             |              | 8            | l         |
|            | manual use                            | automated  |                             |              | 8            | l         |

| Categories                     | Construct Pairs  |   | Number of paired constructs | % Constructs | % Similarity | HIL Value |
|--------------------------------|--|---|-----------------------------|--------------|--------------|-----------|
| <b>Nuisance/Inefficiencies</b> |  |   | <b>9</b>                    | <b>8</b>     | <b>59</b>    | <b>H</b>  |
|                                | efficient  | inefficient   |                             |              | 92           | h         |
|                                | bad experience   | good experience   |                             |              | 92           | h         |
|                                | good to deal with  | unhelpful   |                             |              | 83           | h         |
|                                | Clear understanding and desire to follow policies and procedures | Ignoring policies and procedures where it suits                   |                             |              | 83           | h         |
|                                | Appropriate balance between performance targets and              | Focus on profit/income without any consideration for policies and |                             |              | 83           | h         |

| Categories                  | Construct Pairs                         |                                 | Number of paired constructs | % Constructs | % Similarity | HIL Value |
|-----------------------------|---|---------------------------------|-----------------------------|--------------|--------------|-----------|
|                             | getting it right                        | procedures                      |                             |              |              |           |
|                             | different in each case (demographics)   | personal to each individual     |                             |              | 42           | m         |
|                             | disrupts                                | assists                         |                             |              | 25           | l         |
|                             | too many checks                         | fully automated process         |                             |              | 25           | l         |
|                             | Demonstrable outputs (policy/documents) | None - assisted decision making |                             |              | 8            | l         |
| <b>Ritualism and Gaming</b> |   |                                 | <b>3</b>                    | <b>3</b>     | <b>33</b>    | <b>L</b>  |
|                             | opinion self-                           | Responsible                     |                             |              | 42           | m         |

| Categories | Construct Pairs   |                                    | Number of paired constructs | % Constructs | % Similarity | HIL Value |
|------------|---|------------------------------------|-----------------------------|--------------|--------------|-----------|
|            | regulating  |                                    |                             |              |              |           |
|            | No obligation to report as long as action taking place to fix | Report to risk and audit committee |                             |              | 33           | I         |
|            | Liaison with regulators                                       | No liaison                         |                             |              | 25           | I         |

## Appendix 2 Content of feedback email

**From:** Wendy Mason Burdon

**Sent:** 14 April 2015 14:44

**Subject:** Regulatory Compliance Research - The compliance trust model

Dear All,

You have all kindly contributed your time to consider my research into models of regulatory compliance. In order to finalise my project I would like to share some of the key findings that have arisen from my work. I would also like to present a proposed conceptual model, and would appreciate your views on whether this model would work in practice.

The traditional models of regulatory compliance within financial services include in-house compliance (or risk management functions), using consultants, shared service arrangements or outsourcing. The results of this study, which has collated the views of financial service professionals, show that 'barriers to compliance' exist within the sector.

The proposed alternative model results in a 'compliance community' which would operate independently from the financial service firms that they serve. This model differs from traditional commercial consultancy or outsourcing. Budgets would be controlled through a 'trust' structure, following the principles of a cost controlled service centre serving all of its stakeholders, rather than a 'profit' making entity. Decision making on operations and appointments would remain within the 'trust' structure based on open communication and dialogue with a range of stakeholder including regulators and international industry leadership i.e. G30, and the multiple financial service firms that the trust would serve. This model will also differ from banking forum groups which are already in existence (such as the BBA) as the compliance officers community would be fully independent from the banking organisation that they would serve (and hence issues surrounding confidentiality/trust would exist within the resulting compliance community, rather than the individual banking organisations). The compliance trust would also benefit organisations they serve, via rotation of experience and knowledge sharing between organisations.

The key attributes (arising from this research) and underpinning theoretical rationale are summarised in the table below. Please could you add your comment to the final column of the table in response to the following questions for each attribute:

- Do you agree that the stated attribute benefits compliance/risk management officers in pursuit of regulatory compliance?
- Are there remaining barriers to regulatory compliance in the presented model/attributes?

- Are the theoretical attributes of the model feasible in practice? (i.e. when considering the bullet points/comments in blue in the second column of the table below)

**NOTE A TABLE OF KEY ATTRIBUTES AND SUMMARY OF DATA COLLECTION WAS INSERTED HERE (for brevity of this appendix, please refer to Table 22 in Chapter 8)**

Of course this email provides a summary only of the data collected and analysis thereon (which actually runs to around 15,000 word or so), so if you would like to receive any clarification, or indeed view the expanded and collective results of the study please let me know. Also feel free to give me a call if any of the above is unclear (see details below). I am going to try to draw together my results by mid-May so I would appreciate if you could try to reply before May 12<sup>th</sup>.

I appreciate the time you have taken to read and reply with comments!

Kind regards,

Wendy



### Appendix 3 Summary of personal construct theory corollaries, from Kelly (1963, pp. 103-104), interpretation of corollaries by Fransella, Bell and Bannister (2004, pp. 9-12) and Jankowicz (2004, Appendix 6), and application in this thesis

| Personal Construct Theory Corollaries | Kelly's statement  | Summary of Fransella, Bell and Bannister/Jankowicz interpretations   | Application in this thesis   |
|---------------------------------------|--|--|--|
| <b>Fundamental Postulate</b>          | "A person's processes are psychologically channelized by the way he anticipates events"  | People operate based on in built representations of phenomena they experience, in order to actively predict what happens – "man as scientist".   | Compliance officers learn (and adapt behaviours) in response to regulatory and business needs.   |
| <b>Construction Corollary</b>         | "A person anticipates events by construing their replications"   | By recognition of regularities/recurring patterns in their experience, people develop internal representations (constructs)  | Personal compliance experiences discussed with constructs elicited during repertory grid interview.  |
| <b>Individuality Corollary</b>        | "Person's differ from each other in their construction of events"  | Individuals develop their own meanings for the same event. Aim to "get beyond the words".  | Compliance officers' interpret and adapt to their personal experiences. Grids have been analysed both individually and collectively (see commonality corollary). |
| <b>Organisation Corollary</b>         | "Each person characteristically evolves, for his convenience in anticipating events, a construction system embracing ordinal relationships between constructs"               | Constructs are hierarchical (subordinate and superordinate relationship).<br>Constructs should be viewed as pyramidal in relation to each other (laddering).                                     | Some constructs carry more importance than others (see also Honey's Content Analysis applied Section 7.3).   |
| <b>Dichotomy Corollary</b>            | "A person's construction system is composed of a finite number of dichotomous constructs"  | Constructs are reference axes – to understand a person's meaning fully, you need to know 'both ends'.  | See Figure 16 – participants asked to describe construct in terms of similarity/differences.   |
| <b>Choice Corollary</b>               | "A person chooses for himself that alternative in a dichotomised constructs through which he anticipates the greater possibility for extension and definition of his system" | The main motivational corollary of personal construct theory. The choice (conscious or unconscious) to choose a pole of a construct. Helps explain why individuals may provide lopsided ratings. | Participants were asked to rate constructs against an overall provided construct (See also Section 6.6 for analysis thereon).                                    |
| <b>Range Corollary</b>                | "A construct is convenient for the anticipation of a finite range of events only"  | With reference to "range of convenience" - a construct is not used for all things in all   | In instances when constructs could not adequately relate to all experiences, then  |

| <b>Personal Construct Theory Corollaries</b> | <b>Kelly's statement</b>  | <b>Summary of Fransella, Bell and Bannister/Jankowicz interpretations</b>   | <b>Application in this thesis</b>   |
|--|---|---|---|
|  |   | circumstances.  | rating was nil (and no further analysis performed).   |
| <b>Experience Corollary</b>                  | "A person's construction system varies as he successively construes the replication of events"  | Constructs are open to amendments based on experience of person (in light of events).   | The average experience of participants (20.1 years) indicates the depth and quality of personal construct data in this thesis (see Section 6.5).  |
| <b>Modulation Corollary</b>                  | "A variation in a person's construction system is limited by the permeability of the constructs within whose range of convenience the variants lie"                                     | Some constructs can accommodate a greater range of events (e.g. good/bad), whereas others are less permeable covering a limited range of convenience e.g. fluorescent/incandescent).                | In instances when constructs could not adequately relate to all experiences, then 'rating' was nil (and no analysis performed).                   |
| <b>Fragmentation Corollary</b>               | "A person may successively employ a variety of construction subsystems which are inferentially incompatible with each other"  | Although there is tendency towards consistency within construct system (especially core constructs (personal values) and their subordinate constructs) – this may vary due to circumstances/events. | Initial Eyeball analysis of grid is recommended to identify inconsistencies in constructs. See Section 6.6 for analysis of grids data.            |
| <b>Commonality Corollary</b>                 | "To the extent that one person employs a construction of experience which is similar to that employed by another, his psychological processes are similar to those of the other person" | Contrast to the individuality corollary. Corollary has direct relevance for research conducted with groups of people using the same grid (i.e. this research thesis on compliance).                 | Honey's Content Analysis is applied to grid data (See Section 6.6.2) to identify themes within elicited constructs.                               |
| <b>Sociality Corollary</b>                   | "To the extent that one person construes the construction processes of another, he may play a role in a social process involving the other person"                                      | Describes how we try to understand others, and relationship of interaction with others.   | The relational aspect of constructs has been interrogated during repertory grid interview with participants, by exploring a range of experiences. |

## Appendix 4 Examples of prior use of repertory grid in business research

| Researcher                 | Research discipline                                | Number of participants   | Overview of repertory grid method   | Overview of analysis   | Other modifications   |
|----------------------------|--|--|---|--|---|
| Girard (2013)              | Sustainability issues                              | Four working groups, involving range of 5-10 participants                              | Iterative process of categorisation of stakeholders.                              | Mapping stakeholder practice by 2 step process, to build collective perception.  | Semi directive interviews, participation in group by researchers (considered innovative adaptation of repertory grid to practice mapping) |
| Wright et al. (2012)       | Strategic Management research                      | 46 full time managers (cross industry) enrolled on Strategic Management Masters course | Elements supplied to participants. Constructs formed and scoring by participants. | Excel data collection and thematic analysis. Further analysis in REPGRID program. Listing of key findings side by side.                                    | Overall "preferred" element to be envisioned by participants  |
| Goffin et al. (2012)       | Supply chain management research                   | Two case studies: Case 1, 39 repertory grids; Case 2, Ongoing                          | Elements supplied to participants. Constructs formed and scoring by participants. | Case 1: Grouping of constructs by coding. Average normalized variability (ANV) compared. Case 2: Pareto analysis to ensure theoretical saturation reached. |   |
| Thota (2011)               | Information Systems Research                       | Over 2 cycles, 29 repertory grid participants  | Elements supplied to participants. Constructs formed and scoring by participants. | Use of REPIV program. Content analysis of grids (based on Honey technique). Quantitative analysis using SPSS (Krippendorff's Alpha).                       | Constructs categorised, mean percentage similarity scores computed to estimate relative importance of each category.                      |
| Kneiding and Tracey (2009) | Community development finance/stakeholder Research | 18 repertory grid participants   | Elements developed from literature. Three overall constructs                      | Analysis of interview transcription. Content analysis. Multidimensional  | Two part interview: Interviews recorded and data analysed in  |

| Researcher   | Research discipline                     | Number of participants  | Overview of repertory grid method  | Overview of analysis  | Other modifications   |
|--|---|---|--|---|---|
| Alexander, Loggerenberg, Lotriet and Phalamohlaka (2008) | Information Systems Research            | Workshop of 4 researchers   | provided.<br>Eliciting both elements and constructs from participants.                                   | Scaling (MDS) for grid analysis, and cluster analysis.<br>Goal to reach a shared understanding – used communication to compare individual grids.    | combination with constructs from grids<br>New application of grid – Reflection and Construction of Shared Meaning |
| Song and Gale (2008)                                     | Project Management Research             | 18 repertory grid interviews  | Elements supplied to participants.<br>Constructs formed and scoring by participants.                     | Content analysis.   |   |
| Crudge and Johnson (2007)                                | Search Engine User Perspective Research | 10 repertory grid interviews  | Elements supplied in form of search engines. Constructs formed and scored by participants.               | Qualitative content/thematic analysis.  |   |
| Panagiotou (2007)  | Strategic Management Research           | 24 participants (20 completed repertory grid – dyadic approach to compare competitor companies).<br>Elements (companies chosen by researcher – constructs elicited by participants. | Elements (competitor companies), chosen by researcher.<br>Constructs formed and scoring by participants. | Varied between each hypothesis.<br>Qualitative data analysed by content analysis.<br>Quantitative data analysed using SPSS/Manova.                  | Interviews, followed up by questionnaire  |
| Senior and Swailes (2004)                                | Performance management                  | 60 repertory grids  | Elements formed in conjunction with participants.<br>Constructs formed by participants.                  | Factor analysis (principal component analysis, using specialized GAP (Grid analysis programme). Formation of group constructs (construct clusters). | Team cognitive maps prepared during analysis  |

| Researcher                           | Research discipline                        | Number of participants                              | Overview of repertory grid method   | Overview of analysis  | Other modifications  |
|--------------------------------------|--|---|---|---|--|
| Oppenheim, Stenson and Wilson (2003) | Information management                     | 5 repertory grid interviews                         | Element categories (nine) supplied in advance. Constructs formed by participants. | Cluster analysis and content analysis using WebGrid II programme. |  |
| Lee and Truex (2000)                 | Information systems                        | 74 grids completed                                  | 11 "critical" elements and 10 constructs supplied from literature for scoring.    | Statistical analysis of construct ratings.                        |  |
| Duberley et al. (2000)               | Performance evaluation and control systems | 29 repertory grid interviews                        | Not clearly stated in paper.  | Not clearly stated in paper.                                      | Combining technique of case study and repertory grid technique |
| Langan-Fox and Tan (1997)            | Culture survey                             | 13 repertory grid interviews, with follow up survey | Elements provide, constructs formed by participants.                              | Content Analysis.   |  |
| Honey (1979)                         | Attitude Survey, Manufacturing Business    | 73 repertory grid, performed in groups of approx. 8 | Elements type specified. Constructs formed by participants.                       | Manual Review – seven stage process.                              |  |

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