I very much appreciate having the opportunity to participate in today's program. Improving the culture of financial services is an important issue for me and my colleagues at the Federal Reserve Bank of New York, as well as for many senior policymakers both domestically and abroad. As always, what I have to say reflects my own views and not necessarily those of the Federal Open Market Committee or the Federal Reserve System.

Why should we seek better culture in the financial services industry? We do this to achieve better outcomes in terms of conduct and behavior—and, with that, greater trustworthiness in our nation's financial system. Greater trustworthiness will make it easier for the financial industry to perform its role in supporting economic activity and rising living standards. Greater trustworthiness will also make it easier to attract top talent into the industry. Without that, the industry will suffer.

The focus of today’s event is the role you can play as future leaders of the industry. Your firms selected you to attend because of your career success thus far and your potential for senior leadership. It is timely, therefore, for you to consider what type of leader you want to be, what type of firm you want to lead, and what type of industry you want to work in and influence. I have some views on all three, which we will get to in a moment.

I am encouraged that members of the industry have convened here today to engage on these issues. I think it is important that the industry tackle this together. You can learn from one another. And, given the scandals of recent years, you really do have to sink or swim together.

Before the recent spate of conduct problems, there were times when one might be secretly happy when a competitor stumbled through some sort of misconduct. All the better if such a stumble generated negative publicity and headlines. Today, the situation is vastly different. When each new scandal emerges, the industry is painted with the same broad brush. This underscores the importance of taking both individual and collective responsibility for reform. You have a personal stake in improving bank culture. Your firms have a stake too. And so does the industry.

There are three messages I am going to focus on today:

First, stay in banking and be good role models of the behaviors and conduct that we all want to see. It’s important. The banking industry needs your talents. And, if done the right way, it will result in a fulfilling career.

Second, banking does not have its own ethics—nor should it have its own ethics. The qualities that you value in other aspects of your life should be the same qualities you apply at work and encourage in your colleagues.

Third, candid assessment is critical to improving culture. I invite you to think in particular about the incentives and norms of behavior within your organizations. Do they support or impair the qualities and principles that guide you and that your firm espouses?

Before expanding on those points, let me explain why I believe that reforming culture is important, and justifies the time and effort of not only of today’s program, but of the ongoing work at your institutions and collectively across the industry.

The manipulations of LIBOR and foreign exchange rates prompted the New York Fed’s work on culture. Of course, widespread misconduct did not originate with either episode. The timing, however, was significant. Despite the near-death experience of the financial crisis, new rules and regulations, and—in some cases—large fines and penalties, the LIBOR and FX events made clear that serious ethical and behavioral problems had persisted in the industry. I was particularly struck by how the manipulation of foreign exchange rates occurred even after the LIBOR fixing was widely known. The appropriate lessons from the LIBOR scandal did not seem to have been learned. That was both surprising and profoundly disappointing to me.

The LIBOR and FX collusions were not occasional atonalities in an otherwise harmonious financial system. They were not two remote tail risks that both happened to materialize, or just a bad coincidence. There have been too many examples of other misconduct to list. Wells Fargo is the most recent example, but serious misconduct is not confined to a single jurisdiction or a business model. The evidence, which now stretches over a decade, has only reaffirmed my initial belief that there is an industry-wide problem.
In light of these continuing and widespread failures, my colleagues and I recognize the importance of culture—that is the unwritten norms and accepted practices of an organization. The culture of each firm will necessarily be its own. But the pervasiveness of problems—across firms and countries—points to common, industry-wide norms that need attention.

An industry-wide problem needs an industry-wide solution. I also think that, when the problem is cultural, any solution must be industry-driven. It is the public sector’s job to establish and enforce rules, but rules face some inherent limits in shaping conduct and behavior. It is natural to adapt to the behaviors that we observe around us. A common illustration of this point is the speed limit. Most drivers move with the flow of traffic. They pay less attention to a number posted on a sign.

This is not to deny the necessity and importance of regulation, or to criticize any of the particular rules imposed in response to the financial crisis. But, we also must recognize that it is impossible to create a rule for every situation. Also, rules tend to be reactive rather than proactive. Rulemakers—whether they be members of Congress, regulators or judges—are almost always responding to events. And, even if rules could cover every situation, having a rule does not mean that people will always follow it. In many recent examples, the behaviors we observed violated rules already on the books. Thus, more rules and penalties alone will not cure the industry’s underlying problems. They are necessary, but not sufficient.

What’s more, establishment of too many brightline rules may prove counterproductive in encouraging a good culture. For one thing, intricate and detailed rules can be construed as implying that the responsibility for good conduct rests with supervisors and regulators. For another, rules may create opportunities or incentives for legal or regulatory arbitrage—finding creative ways around rules. And this activity may, in itself, have insidious effects on culture.

As I see it, the problem occurs when an organization’s culture equates “what is right” with what is legally permissible, and when “what is wrong” becomes equivalent to what is legally impermissible. The technical legality of the rule, not the propriety of our conduct, becomes the arbiter of our actions. A proliferation of rules may prompt us to ask first what we can do, not what we should do. Legal arbitrage is intellectually energetic, but ethically lazy.

And, as U.S. Attorney for the Southern District of New York Preet Bharara has observed, if you spend your time thinking about how close to the line you can get, it is inevitable that you will at some point cross that line. No one gets the arbitrage right 100 percent of the time. When you make that mistake, you will not only have a bad culture, but you will also have to deal with Preet Bharara’s office.

Therefore, what’s needed is a better culture. Culture can help to fill in the spaces between and beyond rules. Culture also shapes our attitude toward rules. A strong, ethical culture is one in which individuals within an organization demonstrate to each other a commitment to certain first principles. These principles must align with both the private purpose of the organization and the public rules governing its operations.

Of course, it is possible for principles to conflict. When that occurs, determining the right course will be difficult. But, the more you wrestle with that conflict, the better you will become at resolving ethical quandaries. Aristotle called this aspect of ethics “habit,” but I prefer to think of it as ethical muscle memory. The more practice you have in thinking about it, the better you will be at determining what is right.

Bankers will be more likely to think about what is right, as opposed to what is merely legal, the more often they observe their colleagues doing the same. I doubt that rules alone can accomplish this. Telling people to be ethical doesn’t make it so. Seeing others engage in ethical decision-making is, by contrast, quite powerful.

With that prologue, let me turn to my first message: Stay in banking. This might be a surprising message in light of my introduction. Nonetheless, banking is important work. Society relies on its financial system to “create substantial value for our society.” As investor and author John Bogle has written:

>“(Banking and finance) facilitate the optimal allocation of capital among a variety of users; it enables buyers and savers to meet efficiently; it provides remarkable liquidity; it enhances the ability of investors to capitalize on the discounted value of future cash flows, and other investors to acquire the right to those cash flows; it creates financial instruments [..] that enable investors to assume additional risks, or to divest themselves of a variety of risks by transferring those risks to others.”

To fulfill its potential for creating value for society, the financial system needs talented and dedicated people at the helm. This is especially true for banks, which are indispensable to our economic system.

As the philosopher Onora O’Neill has observed, banking requires more than just technical competence. Bankers must reproduce their efforts and results with reliability. And, above all, bankers must be honest. They must do what they say and say what they mean. This is necessary for the financial system to be viewed as trustworthy. Without that, the financial industry cannot be effective in performing its key roles.

Cultivating these three traits emphasized by Onora O’Neill—competence, reliability and honesty—will help enable you to have a personally fulfilling career. The best doctors or lawyers do their work not only because it pays well, but because it is interesting and
Candid self-assessment is essential to knowing where you stand and how you are progressing toward your goal. Industry groups contribute an important service to society. I hope you feel the same about what you do. And if you don’t, I urge you to consider how your industry can become more professionally fulfilling. What is needed for you to feel better about your work, to sleep more soundly, to worry less about the risk posed to your business by potential misconduct?

Your professional fulfillment will grow if you also contribute to promoting these qualities in others—that is, by helping to improve the culture of financial services. It is easier to be smart, dependable and trustworthy when you are surrounded by other people who also fit that description.

My second message is to reject the idea that a separate regime of ethics or morality applies in banking. I’m sure you have heard this, or perhaps even thought this, at some point in your career. Let it end there. We often teach our children by asking them if they would engage in that type of behavior at home. This is good professional advice as well.

Bankers have been criticized for their ethical and moral shortcomings. That criticism has legitimate grievances at its roots. There have been far too many instances in which bankers have not lived up to expectations. But it is also true—and I’m sure you have experienced this—that you have advanced in your careers because you have demonstrated personal attributes that anyone would be proud to possess. I mentioned before honesty, competence and reliability. You could add to that list hard work, perseverance and responsiveness.

Moreover, if you are like me, your careers will have benefitted from teamwork—the good fortune to work with capable colleagues. Individual effort is essential, but success often depends as well on the contributions of others. Whatever list you have come up with, make sure that teamwork is among your core personal principles.

I would also like to make a slightly different observation on banker ethics. What’s missing is not so much a personal commitment to good conduct, but rather a commitment to call out bad conduct observed in others. You might think it is a paradox or a contradiction to praise teamwork in one breath, and then in the next breath to call for raising the red flag when you see bad conduct in others. I do not see it that way.

We hear often that integrity is a corporate value. I think what is often meant by this is honesty—doing what you say, and saying what you mean. But integrity, to me, has an additional meaning. It means operating according to a single, internally consistent set of principles. If you are honest only in some places or circumstances, but not others—or only with some people, but not others—then honesty is hardly integral or integrated into your life and work.

The importance of this particular meaning of “integrity” was made apparent to me on a recent visit I made to the United States Military Academy at West Point. The faculty and students there believe that strong individual ethics are what make large organizations like the U.S. armed forces succeed. The commitment of cadets to living the ideals of the institution was impressive and humbling. They embodied the word integrity—alignment of word and deed in all aspects of life.

Another lesson that I took from West Point is that cadets commit to integrity because their careers—and, in combat, their lives—depend on others. We are in this together—this city, this industry, this country. And if we’re in it together, we all have to behave in ways that benefit the group. We have to behave in ways that merit the trust of others.

Whether we are citizens or soldiers, the most important relationships in our lives are built on trust. In our personal lives, we take action when our trust has been betrayed. To reform financial services, we need to bring the same expectations of trust—and the consequences of a breach of that trust—to the office each day. If you would not tolerate a practice in your personal life, do not tolerate it in the office.

Calling out bad conduct is not easy. Let me share with you another observation from Preet Bharara. A common element in many of the frauds his office has prosecuted is the failure of colleagues to call out bad conduct by raising their hands. This is so telling of a culture that condones or promotes misconduct. People see something, but do not say something. And, it is so shortsighted. It prevents problems from being addressed while they are small. By not raising their hands, these colleagues are “quietly adding risk to your books [and] invisibly enlarging your liabilities.” They are also tacitly encouraging bad conduct by skewing incentives.

There may be many reasons for choosing silence over raising your hand. You may face a conflict of loyalties. It’s uncomfortable to tell on a colleague. You may think that the problem will just go away, or that calling attention to a problem will harm the firm. Raising your hand is difficult. But, it is also absolutely necessary. As rising leaders in the industry, you need to lead by example. In doing so, you will make it easier for others to follow your lead.

My final message is a request that each of you commit to a candid assessment of yourselves, your firms and your industry. For Adam Smith, candid observation was a cornerstone of economic behavior:

> “We suppose ourselves the spectators of our own behavior, and endeavor to imagine what effect it would, in this light, produce upon us. This is the only looking glass by which we can, in some measure, with the eyes of other people, scrutinize the propriety of our own conduct.”

Candid self-assessment is essential to knowing where you stand and how you are progressing toward your goal. Industry groups
here and in other financial centers are working on useful ways to measure culture—consistent with the maxim, “if it’s important, you will measure it.” But, assessment cannot stop there, and it cannot be the job of someone else—such as management, compliance, audit or a regulator. Each of us must also be reflective about our own faults. We must also commit to do better going forward.

When it comes to making a candid assessment of your group, your firm and your industry, I would like to suggest that you devote significant attention to incentives. I believe that incentives shape behavior, and behavior drives culture. If you want a culture that will support your long-term business strategy, you need to align incentives with the behaviors that will sustain your business over the long haul.

There are many ways of encouraging certain behavior through incentives. Promotion is quite powerful, as is compensation. They are powerful, in part, because they convey values and community esteem. People work hard to earn money. But, most also work hard to earn the trust and respect of colleagues, peers, subordinates and seniors. If you want to know what behaviors are valued or esteemed in reality, look to see who is promoted and well-compensated and the behaviors that they embody. Do the results match what is said? Do they match your expectation of fairness? Do you aspire to be one of these individuals, not because of their status and compensation alone, but because of the esteem you hold for them and their values?

Over the long haul, the economy needs a vibrant and trustworthy financial sector in order to thrive, just as the financial sector needs a vibrant economy to thrive as well. You are the rising leaders of your firms. You can help accomplish these aims. A strong and ethical culture in the banking industry will make it more trustworthy, and therefore more effective in performing its mission. It will also help the industry be held in higher esteem and this will help attract the talent needed to sustain the industry. I am encouraged by today’s gathering, and hope you will take heart that an improved culture in the financial services industry is both necessary and possible. Thank you for your continued efforts and your kind attention.

1 Stephanie Chaly, James Hennessy, Thomas Noone, Joseph Sommer and Joseph Tracy assisted in preparing these remarks.
4 See Bogle, 45-46.
8 See Criminal Accountability and Culture, Remarks by Preet Bharara, Reforming Culture and Behavior in the Financial Services Industry: Expanding the Dialogue, October 20, 2016.
9 See Adam Smith, The Theory of Moral Sentiments, Section III.1.5.