How to Succeed in the Senior Civil Service

Module 2 - Understanding Organisations

1.1 Introduction

Senior Civil Servants (the SCS) deal with larger organisations all the time, but those organisations often behave in unpredictable and apparently illogical ways.

Many outwardly respectable executives lead businesses and departments which behave selfishly and unethically. And they employ senior and middle managers who take surprising risks and undertake projects with scant likelihood of success.

These behaviours have resulted in far too many catastrophes. Examples include the 2008 worldwide collapse of financial institutions, numerous scandals involving major UK banks, the 2010 Gulf of Mexico Oil Spill, the Grenfell Tower fire, and the mis-management of several large NHS Hospitals.

All of these failures happened in environments that were supposedly governed and regulated in such a way that such calamities could not arise. Can any general lessons be learned from them? What leads to these bad outcomes? Is there something inherent in the way that organisations behave today that paves the way to disaster?

One key learning point is that many senior managers do not know (and sometimes do not want to know) what is going on outside their head offices, nor what risks (financial, environmental and other) are being taken by their staff. They will not admit to themselves that parts of their organisation are run to some extent in the interest of local employees, not their shareholders or other stakeholders. This phenomenon, and its consequences, are explored in **Chapter 1.2 - Principals and Agents.**

Senior executives also fail to appreciate that front line staff will hesitate to make sensible, practical and achievable plans for fear of being criticised for displaying insufficient zeal, excessive caution and unnecessary delay. This is explored in **Chapter 1.3 - The Prevention Paradox** (also known as **The MacWhirr Syndrome**).

Corporate and other Boards profess - and often believe - that they are excellent corporate citizens. But their principal aim is almost always to maintain the organisation 'as is' - and they usually have a secondary aim: to ensure its further expansion. They will very often use underhand tricks to attract and retain customers. The tobacco and (leaded) petrol industries are known to have spent decades mounting cynical PR and anti-science campaigns so as to postpone the time when the use of their products would become prohibited. When does fierce competition, or loyalty to an organisation, turn into reprehensible behaviour? This discussion is in **Chapter 1.4 - Ethics.**

Other unwelcome behaviour is best explained by psycholgists. **Herd behaviour, groupthink, shared information bias** and **cognitive dissonance** are surprisingly common, and exacerbate the culture and tensions that are typical of most large organisations. I summarise their implications in **Chapter 1.5 - Organisational Psychology.**

I take a quick look at issues such as **fiduciary duty, company law** and **corporate social responsibility** in **Chapter 1.6 - The Legal Environment.**

1.2. Principals and Agents

All larger organisations suffer to some extent from a disconnect between their leadership and their front line staff. The organisation's *agents*, operating at some distance from Head Office, develop their own priorities and often ignore the priorities of their *principal* (their Board or their Chief Executive)[1].

Why does this happen? There are (at least) three reasons.

- Middle and junior managers like to be popular and so try to align their goals and behaviour to that of the team or work group around them.
- They do not understand or share the priorities of the wider organisation. They prioritise their own work objectives over the changing objectives of the wider organisation.
- Head offices often set targets and/or mandate protocols which are impractical, perhaps because they are out of touch with reality or perhaps because they do not allocate sufficient resource to the task.

As a result, organisations often seem to be controlled by local management who naturally focus on what they see as the long term good of their small part of the organisation.

- They fight hard to retain their budget and their staff numbers when asked to find efficiency savings.
- They fail to implement all those 'stupid directives from head office'.

[1] There is a lengthier discussion in Jean Tirole's *'Hierarchies and Bureaucracies: On the Role of Collusion in Organizations*.

- They neglect record-keeping; boxes are there to be ticked whether or not the associated action has been carried out.
- They will often make implicit bargains with their teams, allowing the use of material for personal ends, providing generous expense accounts, etc. so as to generate a better (non-confrontational) climate - often characterised as 'high morale'.

Such teams typically resist change - especially if it might lead to greater efficiency as a result of them having to work harder and/or face redundancies.

Large organisations often also suffer from the physical and geographical separation of head office from operations. Boeing was a particularly tragic example of this, in the years before the 737-Max crashes. Michael Godfrey wrote this in the FT:

> 'The crisis at Boeing had its beginnings in the merger with defence contractor McDonnell Douglas. Prior to the merger, management and engineering at Boeing were all located at the company's headquarters in Seattle and McDonnell Douglas had its headquarters in St Louis. As a result of the merger a compromise was reached: the new management headquarters would be in Chicago. By this choice both parties lost.
>
> By now it is clear that no one in Boeing Chicago has any idea what has been going on in Seattle. This was inevitable. Before the merger, management at Boeing Seattle worked well, including by means of management walking around the engineering areas. It is a long walk from Chicago to Seattle.'

A later expert report into Boeing's safety culture found a "disconnect" between senior management and regular staff, as well as signs that staff were hesitant about reporting problems for fear of retaliation.

Despite the above analysis, it is not appropriate for senior managers to blame their subordinates for failing to be perfect agents, let alone rail against the organisation's 'frozen middle'. They should instead try to understand the real constraints and pressures experienced by their middle managers. Jonathan Slater (Permanent Secretary at the Department for Education) set a good example when he insisted on adding the voice of both teachers and DfE frontline staff to his top table. He also reminded his colleagues that he and they were the overhead - teaching would continue quite happily without them.

Clear evidence of the principal-agent problem - if you want to find it - can often be seen in the way in which new front line staff are inducted into local customs and behaviours. This process should transmit the benefits of experience and local knowledge but it often has a darker side. New recruits are told by experienced colleagues that formal instructions - or things they learned in an induction program - can safely be ignored as out-of-date or impractical. Newbies following proper protocols are easily teased: "Ooh, get them, who do they think they are?"

Gill Kernick tells how she was asked to work with a team who were making frequent safety-critical errors even though their managers and trainers insisted that staff were trained 'to do it correctly'. All the usual tools and values appeared to be in place to support staff in following correct processes. She then chatted to the front line staff and learned that as soon as they completed their training they were told to forget what they had been taught. If all the instructions were followed it would impossible to complete safe installations within the allocated time.

One example of the new-recruit problem, with far reaching consequences, was the 2020 Minneapolis killing of George Floyd by police officer Derek Chauvin that triggered the Black Lives Matter protests. Mr Chauvin was himself a training officer for new recruits, whilst one of the policemen that failed to intervene in the killing had joined the force only four days previously. The latter's lawyer argued that "They're required to call him 'Sir'. He has 20 years' experience. What is my client supposed to do but to follow what the training officer said?"

Here are some other examples of the principal-agent problem.

Samantha Burrell worked at Repairs Direct: the company that maintained Grenfell Tower. She told the Grenfell Inquiry that call centre staff were expected to maintain customer satisfaction rates of 90% to 95%. The jobs requested by customers to be surveyed were chosen so as to "almost guarantee a positive reaction to the works, for example a tap repair, to bolster that percentage". Asked whether he recognised these methods, the company's Managing Director, Mr Webb said: “Absolutely not. My firm belief was that calls were selected at random.”

Nick Butler said this, in the FT in January 2014, about a profits warning by Royal Dutch Shell:

> 'At the heart of the .. problem seems to be the gap between operational reality and top management, including the board. Big problems capable of triggering a profits warning in a company this size do not arise over 80 days. They grow more slowly and are often invisible to boards meeting every six weeks who have to trust whatever data they are given. .. The rest of the industry should avoid gloating. It would be much more useful for the boards of the other majors to ask themselves if they really know what is happening in the companies for which they are legally responsible'.

It is very common for front line staff to ignore alarms and safety protocols

- Thames Water was fined £14m after a malfunction at a New Malden sewage works triggered nearly 50 remotely-monitored alarms, none of which was checked. 79 million litres of raw sewage flooded local land and a river.
- An HSE Inspector reported that a contributory factor to a serious roller-coaster accident at Alton Towers had been that the frequency of false alarms meant that staff tended to assume that all alarms were false, and so restarted the ride without carrying our proper checks.
- 16 year old mental health patient William Jordan was left unattended for several hours before he hanged himself in a Priory Clinic - despite clear instructions that he was to be checked every 15 minutes. Staff then falsified logs so it appeared as if they had in fact checked he was OK.
- Red Arrows pilots played 'drinking roulette' into the early hours if they thought that day's display would be called off because of bad weather.
- And Buckingham Palace security was famously compromised when Michael Fagan broke in and spent some time talking to Queen Elizabeth in her bedroom. Police ignored several alarms believing them to be faulty.

The principal-agent problem is hardly a new one. CE Montague tells the delicious story, in his book *Disenchantment*, of the old hand sergeant-major who, instead of taking his young recruits on a long training march, takes them to a pub where they are surprised to find that 'arrangements for serving a multitude are surprisingly complete', and that their sergeant-major is clearly well acquainted with the publican. I suspect that armies have suffered from, and Generals will have cursed, this sort of problem right back to the beginning of armed conflict.

What are the consequences for policy-makers, regulators and others?

First, it can be very hard to find out what is really happening inside a large entity, not least because its own senior executives probably do not themselves know what is happening and, if they do, they will be very reluctant to admit their partial loss of control. So don't rely on assertions and reassurances from bosses. Talk to those lower down.

Be aware, too, that out of touch Head Offices often engage in a sort of magical thinking, believing that - by 'banning' something in their organisation - they actually get rid of it, as if they had pointed a magic wand and the 'banned' thing actually disappears in consequence. Spoiler - it doesn't! This lesson applies just as much within government as outside it.

It is also often unwise to place a great deal of faith in compliance officers, whose creation is too often regarded by their Board as a box which has been ticked, and so then a good reason to ignore regulatory issues. Outside observers, including regulators, need to question the accuracy of any second hand information provided by compliance teams and ask themselves whether it appears likely to be even broadly accurate. You certainly need to discount any suggestion that the organisation is staffed by saints who never make mistakes and who always put the interests of their customers before their own.

Second, if you do identify failures of front line staff to comply with safety, financial and other protocols, you should not jump to any assumptions about the causes of this behaviour. It may be because they are responding to pressure from above, such as to meet financial or other targets, to complete work quickly, to maintain production etc. But leaders of rule-bending teams may themselves be keen to get through work quickly, and/or to impress seniors with their achievements, or maybe simply to get home on time, or to avoid a small amount of work running over into the next day. It is truly very difficult for regulators and company directors to know that this is happening unless there are robust and unpredictable inspection arrangements backed up by a strong compliance culture, and opportunities for whistle-blowing.

Third, you need to be aware that agents and their teams - front line staff and their immediate managers - will often resist the introduction of (what they see as) tedious protocols aimed at improving quality or safety. Rail and marine accident reports include many examples of such behaviour. It is quite common for teams to falsify data, including quality and safety data.

The principal-agent problem also means that regulators need to take into account how the middle and lower reaches of an organisation might react to regulatory pressure. The need for change and/or improvement may be accepted by senior executives, but this does not mean that the necessary changes will be accepted or implemented at the working level. Regulatory and other interventions need to be designed with this problem in mind.

1.3. The Prevention Paradox (The MacWhirr Syndrome[2])

[2] John Kay was the first person to use the MacWhirr analogy when writing about what others call the Prevention Paradox.

Joseph Conrad told the story[3] of *Captain MacWhirr*, who chose to sail straight through a devastating storm because he recognised that his employers would criticise him for delaying their cargo if he sought to sail round it:-

> "Suppose", he says, "I went swinging off my course and came in two days late, and they asked me 'where have you been?' 'Went round to dodge the bad weather,' I would say. 'It must have been dam' bad, they would say. 'Don't know,' I would have to say, 'I've dodged clear of it.'"

Similar behaviour is often exhibited by politicians, senior executives and many others.

MacWhirr in Politics

Janan Ganesh saw the Prevention Paradox at the highest level of western politics. He notes how the 'global elites' responded very effectively to threats as acid rain and the punctured ozone layer, but some commentators then claimed that these threats had been exaggerated. He argued that:-

> 'Sensible leaders prevent a chronic problem reaching its acute stage. The public are spared grievous suffering. But they also miss out on a demonstration of how vital it is to choose sensible leaders. As nothing ever goes existentially wrong - no world war, no depression - politics starts to feel like a simulation. The stakes start to feel liberatingly low. Vote for a rogue, by all means, or a charlatan. What is the worst that could happen?'

US Congress Representative Barney Frank spotted the paradox when analysing Hank Paulson's dilemma in the middle of the Lehman crisis:

> "The problem in politics is this: You don't get any credit for disaster averted ... Going to the voters and saying, 'Boy, things really suck, but you know what? If it wasn't for me, they would suck even worse.' That is not a platform on which anybody has ever gotten elected in the history of the world".

Further back in history, President Kennedy said this when talking to journalist Charles Bartlett in 1963:

> "We don't have a prayer of staying in Vietnam. We don't have a prayer of prevailing there. These people hate us. They are going to throw our tails out of there at almost any point. But I can't give up a piece of territory like that to the Communists and then get the American people to re-elect me"
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> (The Vietnam War continued until the Americans abandoned Saigon in 1975. Estimates of the number of Vietnamese soldiers and civilians killed vary from 1.0 to 3.8 million. Some 300,000 Cambodians, 20,000–60,000 Laotians and c.60,000 U.S. service members also died in the conflict.)

The implementation of the Brexit referendum strikes me as another example of the syndrome, whatever you thought of the original decision. Theresa May announced the decision to leave the Single Market and Customs Union shortly after the Brexit referendum even though many 'leavers' had argued that it would be a mistake. But it was much easier for Mrs May to sail into

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[3] In his short novel 'Typhoon'

that economic storm rather than face the accusations from her right wing that she had bottled Brexit.

Others have noted that if Margaret Thatcher had acted to deter Argentina from invading the Falklands, rather than ordering a taskforce to remove the occupying forces after they had landed, she would probably have been remembered as an unsuccessful one-term Prime Minister.

MacWhirr in The Navy

Perhaps appropriately, the armed forces - and particularly the Navy - offer other dramatic examples of the paradox.

Andrew Lambert, discussing the 1812 loss of HMS Guerriere and the deaths of 21 seamen, noted that "Facing an opponent 50% more powerful in guns, tons and men, [the captain's] only hope of avoiding defeat lay in running away, a tactical choice that would have seen him cashiered, or shot."

The classic example was the sinking of HMS Victoria in 1893 with the loss of 358 lives. The collision resulted from Admiral Markham following an order which he knew to be catastrophic. As another admiral wrote some time later:

> "Admiral Markham might have refused to [obey the order but he would] have been tried by court martial, and no one would have sympathised with him as it would not have been realised that he had averted a catastrophe".

The Spanish lost a galleon, the Nuestra Senora del Juncal - and gold etc. now worth £ billions - after she set sail in October 1631 despite it being the hurricane season and the ship being badly loaded and leaking even before she set sail. Its skipper was under pressure to get the wealth to Spain to fund her response to the Dutch War of Independence.

MacWhirr in Business

Many modern executives mimic Captain MacWhirr because their bosses and stakeholders are very likely to criticise caution, delay and expense even if the organisation eventually achieves its objective. Executives therefore prefer to take uncertain and dangerous risks rather than face certain (unjustified) criticism.

There were, for instance, a number of senior financiers who understood that they were running their companies into serious trouble in the years before the 2008 financial crisis, but felt they would face unacceptable criticism if they were to follow a less risky course. Citibank's Charles Prince famously told the Financial Times that "As long as the music is playing, you've got to get up and dance. We're still dancing."

This led the same paper's John Kay to conclude that "The man who held the most powerful position in the financial services industry was the prisoner of his own organisation." And Andrew Ross Sorkin, in *Too Big to Fail* notes that Lehman's Dick Fuld "had known for years that Lehman Brothers' day of reckoning would come ... But, like everyone else on Wall Street, he couldn't pass up the opportunities."

There was a classic example - back at sea - when Shell chose to tow the drilling rig Kulluk through treacherous waters, in winter, all the way from Alaska to Seattle at least in part to ensure that they avoided a $6m Alaskan tax charge which would otherwise have fallen due a few days later. The tow ropes eventually parted, the rig went aground, and it had to be written off, costing Shell around $200m.

There is Occasional Resistance

There are some interesting examples of individuals and organisations resisting the Prevention Paradox, even though they were bound to be criticised for their behaviour.

Various governments and most businesses were to be congratulated for taking action to near-eliminate the Y2K 'Millennium Bug'. Chrysler Corp. were one of many organisations that realised the need to update their systems when they briefly closed a plant in 1997 and turned the plant's clocks to 31 December 1999. "We got a lot of surprises. Nobody could get in or out of the plant ... and you couldn't have paid people because the time clock systems didn't work".

Subsequent evaluations[4] have confirmed that the Y2K effort had been very worthwhile. And yet some bugs still got through. It was reported in 2018 that the Swedish Unemployment Agency had recently encountered a bug when the first people born in 2000 applied for benefits. But much of the public and the media had concluded that it had all been a waste of time and money because so few examples of the bug had been discovered on 1 January 2000. This is a classic example of commentators not realising that disaster might well have ensued had no avoiding action been taken.

Lord Jellicoe's caution throughout World War I, and in particular in the Battle of Jutland, offers a final telling example. He knew that he could have lost the war through one disastrous engagement with the German fleet. But his failure to take unnecessary risks was much criticised, especially by the British press. His actions nevertheless preserved the fleet and ultimately helped win the war.

Lessons for Civil Servants

Politicians are increasingly inclined to complain that 'the blob', 'the Establishment' and the Mandarins are too resistant to change, too cautious and insufficiently enthusiastic when implementing Ministers' initiatives. There is often some truth in that, but the bigger problem is that modern politicians too often require their MacWhirr subordinates to sail into storms without properly thinking through the consequences, and without providing sufficient time and resources to ensure they come out the other side. The resultant policy failures include social care, immigration, drugs and many others, as well as those listed earlier in this chapter.

There are no easy solutions, of course, and frequent rushed attempts at 'civil service reform' are perhaps other examples of the paradox in action[5]. It might help if today's senior officials could re-learn their traditional ability to speak truth to power[6]. But there have been some recent developments (some welcome, some not) in the relationship between civil servants, Ministers and Parliament. I explore these separately[7].

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[4] See for instance https://www.regulation.org.uk/library/2017-y2k_bug_evaluation.pdf

[5] See also https://www.civilservant.org.uk/csr-homepage.html

[6] Speaking Truth to Power: How to have people listen to your advice and act on it':- https://www.amazon.co.uk/dp/1838467971

[7] Civil Servants, Ministers and Parliament:- https://www.civilservant.org.uk/westminster_model-homepage.html

1.4. Ethics & Avoiding Reputational Damage

Most of us seem readily to accept that businesses and other organisations will sometimes behave badly. But why do we do this? After all, we live in societies that, on the whole, tend to abide by the rules.

Let's first recognise that we ourselves know how we *should* behave but we also know that we will sometimes behave badly. Tony Coady points out that:

> '... the demands of morality are often enough overridden by other persuasive demands, such as imperatives of self-interest, careerism, political advantage and friendship.'[8]

When selling a car or a house, for instance, individuals seldom hesitate to behave unethically. We might, for instance, feel temporarily guilty but soon forgive ourselves for failing to tell a prospective purchaser that we have unpleasant neighbours (who are the main reason we are selling the house) or that there is dry rot in a hard-to-access roof space. '*Caveat Emptor*' – 'Buyer Beware!', we cheerily tell ourselves. (See also **6.2** below)

We do - sometimes - expect to benefit from consumer protection legislation[9]. But we are nevertheless surprisingly tolerant of companies that are economical with the truth. We do not expect shops to tell us that we could buy better or cheaper products elsewhere. And we accept that companies will offers initial discounts or attractive interest rates that disappear after 12 months, knowing that a significant proportion of customers will fail to switch to shop around. Indeed, many of us work for such companies.

Politicians and 'Dirty Hands'

So we forgive ourselves for our trespasses - and we are also ready to forgive - and arguably too ready to forgive - politicians who behave unethically. We do not dispute Machiavelli's advice that his Prince must learn how not to be good. Neuro-ethicist Neil Levy says that 'Dirty actions are part and parcel of ordinary political life. … Politicians must make deals, compromise with interests they abhor, distribute favours and neglect relationships.'

We seem therefore to expect our political leaders to balance the advantages and disadvantages of different courses of action, one or maybe all of which may contravene some ethical duty. They need to weigh the importance of each duty and some – such as preserving life – will have very high weights indeed. But they expect to be forgiven if they regret what they felt forced to do.

Are Business and Other Leaders Allowed to have 'Dirty Hands'?

Given our acceptance of our own, and politicians', unethical behaviour, it is perhaps unsurprising that many business owners, hospital chief executives and the like feel that they, too, should be allowed to engage in unethical behaviour if it reduces risks to their organisations, to the livelihoods of their employees, and of course to themselves. It is not difficult to spot such behaviour which takes several forms, some more reprehensible than others.

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8 Tony Coady - https://plato.stanford.edu/entries/dirty-hands/

9 https://www.regulation.org.uk/specifics-consumer_protection.html

First, there is a natural tendency for businesses to engage in a 'race to the bottom 'so as to compete with rivals who are taking similar decisions. Corners and costs will be cut, and customers complaints ignored. The result, absent other pressures (including regulation) is that 'bad drives out good', with mixed effects not just for their customers but also for the efficiency of the wider economy. Michael Skapinker pointed out that 'retail banks' [main] aim is to sell you products you don't want and to rip you off when you are not looking'. This not just bad for banks' customers. It is bad for the whole economy.

We all hope, though, that competition will eventually ensure that the best products and business practices survive. Robust competition, involving a range of offerings, is clearly a key part of a dynamic economy.

Next, the reflex instinct of many leaders is to protect their own reputations and those of their organisations. At a minimum, those inside an organisation seldom perceive faults - such as poor service - to be as serious as they seem to outsiders. This is just as much a problem - and maybe more of a problem - in the public sector as in the private sector.

Even more seriously, senior executives sometimes take extraordinary and often unethical steps to cover up rotten decision-making.

Some examples:

- the unlawful killing of the 97 football fans who died as a result of a crush in the stands at Sheffield's Hillsborough football stadium;
- the Post Office scandal involving the wrongful prosecutions of hundreds of post office operators falsely accused of fraud, leading to imprisonments of the innocent, sackings, bankruptcies, ill-health and suicides;
- Senior doctors at the Countess of Chester Hospital Trust began to be concerned in June 2015 that nurse Lucy Letby might be responsible for a spate of unexpected baby deaths. But the hospital's managers - most of whom had either a nursing or non-medical background - feared that calling in the police would mean "the end of the unit as well as the trust's reputation". 12 babies died, or nearly died, before the police were finally contacted (and Letby arrested) in May 2017;
- "Scotland Yard hid the damning contents of a report … from the public and its own officers. Senior officers were preoccupied with restricting access to Sir Richard Henriques' report on the bungled investigation into false allegations of an establishment paedophile ring rather than implementing its 25 reforms;"[10]
- Last, and certainly not least, it was hard not to be appalled by the way the Foreign Office obstructed a parliamentary inquiry into the 2021 evacuation of Kabul. The MPs reported[11] that:

    - 'The Foreign Office has not been open about [its] failings. In the course of the inquiry, it has given us answers that, in our judgement, are at best intentionally evasive, and often deliberately misleading. Those who lead the department should be ashamed that civil servants of great integrity felt compelled to risk their careers to bring to light the appalling mismanagement of the crisis, and the misleading statements to Parliament that followed.

[10] *The Times* 13 March 2020

[11] https://committees.parliament.uk/work/1465/government-policy-on-afghanistan/publications/

- The fact that nobody can state who made [one particularly controversial decision] suggests at best that the political leadership was chaotic and at worst that senior figures are not telling the truth ... we repeatedly received answers that appeared calculated to mislead or to evade our questions and that were contradicted when new facts came into the public domain.'

Although self-preservation is usually a primary motive, excessive defensiveness sometimes results from fear of being sued. And I suspect that CEOs sometimes hesitate to address obvious problems, correct mistakes or improve the behaviour of their organisation because they fear facing criticism that previous behaviour was in some sense faulty which might sometimes lead to claims for compensation.

The lesson for civil servants is obvious. We must never fail to respond to complaints and other expressions of concern because we are concerned about your department's reputation. It is always better to apologise and make improvements than to pretend there was no error in the first place.

Third, organisations are often reluctant to admit that their plans have turned out to be overly optimistic, or that they have run into unexpected problems. Others deliberately push ethical, accountancy and regulatory limits and then find that they have accidentally strayed to the wrong side of those boundaries: transgressions to which, for obvious reasons, they are unwilling to confess. However, once organisations have begun to hide bad news, it can become increasingly hard to 'come clean', even though the consequential damage continues or gets worse. So there comes a point when unwillingness to confess to temporary problems becomes dangerous self-delusion and likely fraud on the public. Enron, RBS, OneCoin[12], and Theranos[13] are multi-billion examples of where that can lead.

Within the public sector, I was struck by the failure of the Director of Public Prosecutions and the Chief Executive of the Courts Service to admit (and hence address?) the failures of the criminal justice system in the early 2020s despite their being well documented by *the Secret Barrister* and many others;

The **fourth** category might be the classic 'dirty hands 'scenario. To what extent is it acceptable for a business to thrive (good!) by taking advantage of its customers' weakness or ignorance (bad!)?

This moral dilemma was postulated by medieval theologian St Thomas Aquinas:-

> A merchant in a sailing vessel arrived at an island with a cargo that the islanders had not received for many months. The cargo was accordingly very valuable in the market. What, however, if the merchant knew that coming behind them was a large number of ships laden with similar cargo? Were they morally obliged to tell the islanders or could they exploit their ignorance by maintaining a high price?

Modern businesses face a similar dilemma when faced with very high demand. Their natural reaction is to raise prices and make a quick buck, but when does that become unethical price gouging?

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[12] BBC Sounds - *The Crypto Queen* - https://www.bbc.co.uk/sounds/brand/p07nkd84

[13] https://www.policy-making.org.uk/speaking_truth-over-powerful_executives.html

Businesses selling PPE and disinfectant/cleaning materials found that they could make huge profits in the early days of the Covid pandemic. Although much criticised, those profits undoubtedly encouraged many manufacturers to enter the market and boost supply. Acceptably dirty hands?

But some business practices are surely totally unacceptable. **My final category** consists of those companies that persist in behaviours or sales which are known to cause serious illnesses and/or social problems.

- The tobacco and (leaded) petrol industries are known to have spent decades mounting cynical PR and anti-science campaigns so as to postpone the time when the use of their products would become prohibited.
- It is even harder to forgive those senior executives who authorised the incorporation of a special testing mode in VW's diesel engines so as to cheat emissions tests ...
- nor Boeing's repeated failure to tell its regulator about the risks associated with the 737-Max's MCAS system.
- According to the *Guardian,* Uber flouted laws, duped police, exploited violence against drivers and secretly lobbied governments during its aggressive global expansion. Leaked messages suggested that its executives were under no illusions about its law-breaking. "We're just fucking illegal."
- Nearer home, we wait to hear the conclusions of the Grenfell Inquiry which heard numerous accusations that cladding manufacturers were well aware that they were selling highly flammable material.

These were not five examples of men and women forced to dirty their hands for good reasons. They were allowed to get away with their unethical behaviour for far too long.

The lesson for politicians, policy analysts and regulators must be that they should be ever vigilant in seeking to identify such behaviour before it can do huge damage.

And, again, don't rely on denials, assertions and reassurances from bosses. They are far too likely to be over-interested in their, and their organisation's, reputation. Talk to those lower down.

1.5. Organisational Psychology

It is important to be aware of the many ways in which human psychology impeeds good decision making. I have written separately about the difficulty of speaking truth to power, and suggested how to persuade powerful people to listen to your advice and act on it.[14]

Others have written extensively about the following behaviours, so these notes offer only brief introductions to:

5.1 Herd Behaviour
5.2 Groupthink
5.3 Shared Information Bias, and
5.4 Cognitive Dissonance

[14] Available as an inexpensive paperback, or on Kindle, here:-
https://www.amazon.co.uk/dp/1838467971

1.5.1. Herd Behaviour

Herd behaviour is not always irrational. Herds run together for a good reason, and there is nothing irrational about humans seeking to watch and learn from what others are doing.

But herds of animals - like groups of colleagues - can also get it badly wrong, running blindly into danger rather than away from it. Rational investors in an efficient market will for instance produce frenzies and crashes from time to time. As John Maynard Keynes observed:

> 'A sound banker, alas, is not one who foresees danger and avoids it, but one who, when he is ruined, is ruined in a conventional way along with his fellows, so that no-one can really blame him.'

More generally, Charles Mackay commented that

> 'Men, it has been well said, think in herds; it will be seen that they go mad in herds, while they only recover their senses slowly, and one by one.'

Herd behaviour contributed to one of the most devastating regulatory failures ever. By the end of the 2008 financial crisis, UK taxpayer support for the banking sector totaled £850 billion, and the cost of the consequential economic recession was estimated by the Bank of England to be up to £7,400 billion.

One important cause of the crash was that the majority in government, in regulation, and in the financial services industry shared a very rosy view of the 1990s financial world. Although this majority appeared to share a rosy view of current corporate behaviour, and of the virtues of 'light touch regulation', there were a good number of perceptive commentators who did their best to warn of the forthcoming catastrophe. But they were ignored by the herd.

Such blinkered vision can be exacerbated by a fear of missing out (FOMO). Charles P. Kindleberger had a nice line on this: ' There is nothing as disturbing to one's wellbeing and judgment as to see a friend get rich!'. This concern was familiar to all of us who watched friends invest in Bitcoin.

It follows that regulators have a difficult but important role to play in ensuring that herds do not crash over cliffs and take lots of innocent (customer and taxpayer) victims with them. This can lead to regulators facing considerable criticism, especially as those leading the herds will be surrounded by very committed followers because FOMO drives many of us to want to associate with the rich and famous, even when the latter appear to have an obviously shady or unethical side to them.

As such, regardless of the flak they might receive, policy makers and other analysts must be forever sceptical and hold tight to the ability to think for themselves. They should not let their political leaders or colleagues override their doubts and fail properly to analyse alternative courses of action.

1.5.2. Groupthink

Groupthink is similar to herd behaviour but has different causes. It is the unquestioning acceptance of colleagues' beliefs, assumptions or conclusions - regardless of whether they are obviously wrong - simply to avoid social pain. While it is easy to mock such actions, groupthink, much like herd behaviour, is far from purely irrational. Humans, as social animals, must work in groups to achieve their goals and a certain amount of conformity helps.

Large organisations require a good deal of conformity, of course. You can't have every single person asking questions. Decisions have to be made and implemented. And if everyone you know, every newspaper you read, every person you once admired, are all saying the same thing, it takes a real effort of will, and real courage, to argue back. But there are times when talking truth to the crowd is vital to protect the crowd from itself or from a harmful reality that the group refuses to see. That being said, it is uncomfortable, or worse, to be a contrarian.

As discussed further in Part 3 (*Speaking Truth to Power*) most senior leaders prefer not to face serious challenge. Discussing the appointment of independent directors, Warren Buffett noted that "CEOs don't look for pit bulls. It's the cocker spaniel that gets taken home".

Beyond silencing dissent, groupthink can lead to it being very difficult to hold decision makers to account. This is because it is often hard to identify those making (or sustaining) the very largest decisions.

It would be difficult, for instance, to say that the (commercially and financially disastrous) decision to build Advanced Gas-cooled Nuclear reactors in the UK was made by anyone at all. The decision maker was certainly not Minister Fred Lee whose inexperience and lack of technical knowledge meant that he could in practice do little more than act as a mouthpiece for what was in practice a collective decision of the Atomic Energy Authority, the Central Electricity Generating Board and civil servants. Those who expressed doubts, or provided negative feedback on the program, found their career progression blocked or terminated.

Corporate cultures feed into this, as well as the British reluctance to offer challenge or criticism. Industrialist Sir Denys Henderson was famed for his unforgiving tongue but appears to have had little impact as a non-exec of the Board of Barclays Bank. One scholarly director told him "You are essentially an *oratio recta* [direct talking] man but Barclays is essentially an *oratio obliqua* [indirect talking] company." No doubt this contributed to Barclays' subsequent troubles.
The Senior Civil Service, too, suffers from too much indirect talking. All new recruits must quickly learn its over-polite 'Mandarin' language[15].

And it's not just a British problem, of course. After Credit Suisse lost billions in 2021 by making obviously risky loans, Patrick Hosking noted:-

> If ever a bank seemed plain incompetent at weighing up risk, it would appear to be Credit Suisse. Yet that is the one thing that the bank purports to be expert at. It mentions the word "risk" 2,381 times in its annual report. It has a board risk committee and an executive risk forum and dozens of other risk committees. It lists 12 pages of risk factors. It has risk limits, risk tolerances, risk parameters, client risk profiles, risk mitigation instruments and risk-sniffing algorithms. And, of course, a chief risk officer at the top.
>
> Yet it can barely go more than a couple of months without falling flat on its face. Something isn't working. As Katherine Griffiths points out on these pages today, this may be partly about a culture that went astray years ago.

[15] https://www.civilservant.org.uk/misc-humour-homepage.html

> There is something suspect, too, about the entire process of risk assessment — adopted by all banks, but particularly Credit Suisse. It is too process-driven, too bureaucratic and too bogusly scientific. When things go wrong, it ends up reeking of complacency and hubris. Is it possible that the entire machinery of risk assessment is somehow counter-productive, giving bankers a false sense that they are being prudent? There can be only one chief risk officer — the chief executive. Everything else can look like box-ticking to please regulators.
>
> Credit Suisse is like a cliff-top rambler who fanatically documents the hundreds of different ways he might stumble and fall off, instead of just keeping a sensible distance from the edge.

Margaret Heffernan offers an interesting - almost hilarious - analysis of group-think in her excellent book *Wilful Blindness*.

> "I've even heard boards discuss how, and why, they are invulnerable to groupthink, oblivious to the irony inherent in their confidence. ... Dennis Stevenson, then chairman of HBOS, eulogised the outstanding board he chaired [at a time when] everyone knew the bank teetered on the edge of collapse. ... [Lord Stevenson cited as evidence] the fact that, even in this crisis, 'we are as one'. He seemed oblivious to the notion that the unity of his board may have been a contributory factor to the bank's mess in the first place."

It looks as though groupthink was very much in evidence in the early stages of the Covid pandemic in the UK when Ministers and their advisers did not consider adopting the east Asian approaches to containment which might have bought valuable time and avoided countless deaths.

The late Peter Drucker noted that the first rule in decision-making was that one should not make a decision without disagreement. Drucker went on tell how General Motors' Alfred P Sloan Jr., upon being informed that his management committee were all in complete agreement on a decision, insisted that the matter be further discussed at their next meeting. This was to provide time for members to develop disagreement and greater understanding of what the decision was all about.

1.5.3. Shared Information Bias

Shared information bias is a closely related problem - maybe even a subset of Groupthink.

It arises (all too frequently) when groups spend too much time sharing unimportant information rather than exploring and challenging each individual's knowledge and perspective. The main reason for this is (again) politeness. People like to get along and have a low tolerance for conflicting views. In a crisis, experts may be particularly keen to be helpful by reaching consensus quickly, which increases the pressure to suppress doubts and questions. This creates a situation best summed up by the Ian McEwan line: "everyone nodded, nobody agreed".

1.5.4. Cognitive Dissonance

Cognitive dissonance is the other side of the above coins. We all become stressed if forced seriously to consider two incompatible views at the same time. We therefore fiercely hold onto beliefs - including beliefs derived from herd behaviour and groupthink - even in response to intense external pressure.

One particularly dangerous result is that - as we believe ourselves to be good, honest people - we find it very hard to admit to ourselves that we or our organisation are behaving badly. Senior executives therefore typically push back very hard against any suggestion (from the media, regulators or others) that their actions maybe doing unnecessary harm, including risking their own business.

Cognitive dissonance almost certainly accounts for the failure of many, including Alan Greenspan - a deep believer in the power of the markets, and a fan of financial instruments such as derivatives - to react to all the warnings that something was going very badly wrong in the period before the 2008 financial crisis.

Indeed, without wishing to question the Brexit decision itself, I do wonder whether cognitive dissonance lay at the heart of many Brexiteers failure to engage with serious criticism of the subsequent decisions (such as to leaving the Single Market) chosen by both the Theresa May and Boris Johnson governments.

1.6. The Corporate Environment

Larger entities exist in complex and interesting legal, regulatory and social environments. Their boards have to negotiate these environments whilst also trying to build robust, efficient and effective organisations. External observers do not need to be familiar with the detail, but it helps if they are familiar with the broad principles of some of the most important tensions, pressures and constraints:-

Let's first look at **Fiduciary Duty** & **Company Law**.

Private sector CEOs often argue that their primary duty is to generate profits for their shareholders. Non-profits and public sector organisations may not be profit focussed, but they too need to deliver value by generating income and/or reducing expenditure.

From here, the argument sometimes goes, this legal 'fiduciary' duty takes total precedence over any consequences for the environment, for healthy and fair competition, for customers, for employees, and for wider society. You should not hesitate to challenge this if necessary.

The law, to begin with, is not on their side. UK company law supports the 'enlightened shareholder value' approach. This requires companies to be responsive to a wider group of dynamics than the single-minded pursuit of profit.

The relevant legislation is in S.172 of the Companies Act 2006 which says that company directors must act in the way that they consider, in good faith, would be most likely to promote the success of the company for the benefit of its members as a whole - but they must also have regard to such matters as

- the likely consequences of any decision in the long term
- the interests of the company's employees
- the need to foster the company's business relationships with suppliers, customers and others

- the impact of the company's operations on the community and the environment
- the desirability of the company maintaining a reputation for high standards of business conduct, and
- the need to act fairly between members of the company.

The courts have, for instance, sided with company directors who sold a property at undervalue, where they did so in order to protect the jobs of the company's employees[16].

Fiduciary duty is anyway a long-term concept. Anyone can maximise short-term profits at the expense of customers and other stakeholders, but iti s the duty of directors and executives to maximise the value of the company in the longer term.

The advice provided by Farrer & Co (Solicitors) for the Tax Justice Network in September 2013 makes that point very well indeed:

> In circumstances where a director decides that the company will eschew tax avoidance, he or she may do so for reasons that he or she considers to be aligned with the long-term success of the company, including for example:
>
> (i) the adverse risk profile of tax-structured transactions in the long term,
> (ii) the desirability of investment in public health, education, infrastructure &c in the jurisdictions where the company's employees live and work,
> (iii) the need to foster the company's relationship with tax authorities and with consumers,
> (iv) the impact of tax avoidance on the wider community of taxpayers and users of public services, and
> (v) the desirability of the company maintaining a reputation for high standards of business conduct.
>
> … Our view that other kinds of impact may constitute a legitimate basis for a director's decision notwithstanding an adverse financial impact may be derived from the clear meaning of the [Companies Act] but it is also supported by the pre-existing case law on the corresponding common law duty …

Blueprint for Business, a charity which seeks to create a better society through better business, argues that UK company law requires a (longer term) purpose-led approach:

> Section 172 of the 2006 Act makes clear that the primary duty of the director is the success of the company, and that in discharging [said duty] they have to take account of the Interests of shareholders (which may well vary between them) and have regard to a bunch of other stakeholders too.
>
> Although it is often interpreted as a duty to maximise shareholder value, our view (supported by legal opinion) is that they are not agents of shareholders but true fiduciaries, who have to set out what they think success means.

[16] Re Welfab Engineers Ltd (1990) BCLC 833

> The law is certainly not as clear as it could be but it is often narrowly interpreted and poorly understood. For us a key shift in thinking is where profit is not seen as the purpose but one outcome of living out a purpose that serves society.

Blueprint for Business also makes a strong second point about motivation. Their view is that:

> Organisations implicitly operate with a view of the human person, usually unstated, and typically that people are self-interested, motivated by money and status. A heuristic then operates to reinforce this as people respond accordingly. ...
>
> What we are proposing, drawing on a strong multidisciplinary body of learning and everyday experience is a different view. This is that people are hard wired to seek meaning and fulfilment through work and that the quality of relationships is intrinsically important to us. The link to purpose is then that organisations with a pro-social purpose whose relationships are founded on respect and co-creation will 'crowd in' intrinsic motivation.
>
> People associated with it will lean in because they care. This is hard to introduce in large organisations but the conversations are fascinating because people are not used to being asked about what view of the person does the business have. This is a powerful agent of change.

What about **Buyer Beware?**

'Caveat emptor' is a well-established business principle. Before spending your shareholders' money you should satisfy yourself as to the value, quality, and, suitability of whatever you're buying.

Despite the many laws in place to protect consumers, there is no shortage of companies happy to shoulder their customers with the same responsibility. They seem to feel no little or no obligation to behave ethically, even when their customers are buying complex financial products, for instance, which they are unlikely to fully understand.

Legally, an important case is *Hedley Byrne v. Heller* which held that all businesses have a general duty not to mislead their customers – but this does not extend to a duty to protect customers from making a mistake (such as paying too much for a product) unless the customer is relying on the skill and judgment of the business's employees. There is, for example, no non-regulatory protection for the naive individual who expects their energy supplier to reward their loyalty by ensuring they are always on the best available tariff.

It can be hard to persuade keen marketing directors that they should not boost their profits by encouraging their customers to make obvious mistakes. But it can be worth pointing out that noticeably egregious behaviour has too often, in the past, led to a strong regulatory response and hundreds of pages of irksome rules to be followed. So they might pause and wonder whether the long term health of their enterprise might not be better served by treating their customers fairly, and with respect. ... which leads naturally to ... **Corporate Social Responsibility**

Social and environmental responsibility sounds good, and some companies stuff their annual reports with information about their good deeds, considerate behaviour, and corporate conscience. But these are often no more than fashion statements.

It was telling that the US Business Roundtable listed CSR as one of the four core functions of company boards as long ago as 1978 but it had disappeared by 1990. The latest incarnation of this phenomenon is ESG: *Environmental, Social and Governance investing*. Sadly, however, much ESG activity remains no more than trying (and often failing) to add value to a brand without making any substantive changes to company behaviour.

Ian King of *The Times* enjoyed reporting on:

> …a company that won six awards in only one year from the US Environmental Protection Agency. It won a "corporate conscience" award from the US Council on Economic Priorities. It published a *Corporate Responsibility Annual Report* solemnly detailing its philanthropic activities and its pursuit of "Respect, Integrity, Communication and Excellence" that would "integrate human health, social and environmental considerations into our internal management and value system". And it placed on the desk of every executive a framed copy of its corporate values. It sounds impressive, until you learn that the company was Enron, the American energy giant whose collapse in October 2001 was followed by revelations that it had been fiddling its figures for years.

Arconic - a building cladding supplier - is another example. Counsel for the survivors of the 2017 Grenfell Tower fire said that the company's "lack of candour is an affront to the dead, to the bereaved, and to the former residents of Grenfell". And yet Arconic was in 2020 named by *Newsweek* as one of America's most responsible companies.

END OF MODULE 2