

The way banks are organised makes it hard to hold directors and executives criminally responsible

Written by Andrew Linden, Sessional/ PhD (Management) Candidate, School of Management, RMIT University

The [Financial Services Royal Commission](#) has [seen evidence](#) that bank directors and executives deliberately put in place policies to ignore the law.

But research suggests the very organisational structure of banks [makes it difficult](#) to hold directors and senior executives criminally responsible for [systemic misconduct](#).

The way [corporations are arranged](#), how decision-making is delegated, and information is gathered and distributed, appears to fragment and diffuse individual responsibility.

This makes it hard to establish criminal culpability (the standard of proof is “beyond a reasonable doubt”), even if directors and executives remain in control of processes and are paid bonuses based on organisational performance.

Certain clauses in commercial contracts and the structuring of corporate groups across multiple jurisdictions can also be used to frustrate investigations.

In cases where corporate criminality can be more directly tied to decisions by executives or directors, subsidiaries (or internal divisions) can be dissolved or sold.

Read more: [***What the Royal Commission can do if the banks don't play ball on evidence***](#)

A senior ANZ executive [admitted to the Royal Commission](#) that the bank has no process to verify income and expenditure statements in loan applications.

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This is despite [laws](#) requiring lenders to take reasonable steps to establish borrowers' ability to service loans.

Moreover, this was not an oversight [but a deliberate decision](#) to substitute regulatory requirements for less rigorous internal practices.

This is an example of “[decoupling](#)”.

Decoupling occurs when corporations say publicly that they follow the law, and even create policies to tick regulatory boxes, but then do something entirely different as a matter of standard practice.

With existing corporate governance structures in place decoupling is [extremely difficult to detect](#) from the outside. [It takes](#) active oversight by regulators, internal whistleblowing or public inquiries with coercive powers to gather evidence to identify it.

Read more: [***The Financial Services Royal Commission highlights the vulnerability of many older Australians***](#)

Certain types of (re)organisation also [enable systemic misconduct](#) because they diffuse responsibility and diminish individual culpability.

These [include](#) sub-contracting, the use of consultants, creation of subsidiaries and transnational structures, relocating work to low transparency jurisdictions, and the use of [franchising systems, dealer networks and agents](#).

These decisions about organisational structure are made at the board or senior executive levels.

Implications for the Royal Commission

The banks have [publicly asserted](#) that their boards are focused on ensuring good corporate governance, and that they have the structure (explicit policies, clear lines of reporting/delegation) to ensure regulatory compliance.

But what has emerged at the Royal Commission shows these structures either don't exist or don't function as they should.

Although Australia has [strong laws](#) to jail company directors for policies that facilitate systemic misconduct, this rarely occurs.

The lack of prosecutions, convictions and commuting of jail time [embolden other senior executives](#) and help them rationalise away the seriousness and impact of similar conduct.

Read more: [***Why don't we read the fine print? Because banks know the pressure points to push***](#)

There are a number of factors that the Royal Commission and federal government should address to prevent future systemic misconduct, beyond just [creating a temporary lull](#) before a return to business as usual.

Australian companies [only have one board](#) and that is at the heart of the problem. While all board directors are responsible for the management and governance of corporations, in practice

they delegate authority to executive directors who then operate with wide discretion. This includes enacting policy and reorganising the corporation in ways that diffuse accountability and criminal culpability.

While all corporate governance systems have their weaknesses, in [two-tiered boards](#) , executive directors are overseen by supervisory boards who appoint their own auditors. These kinds of boards constrain executive director discretion, making decoupling more difficult.

This is one possible reason why countries like Germany, with two-tiered boards, have [fewer and less costly systemic governance failures](#)

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The use of executive performance incentives has also been strongly associated with [corporate criminal behaviour](#)

. Evidence suggests remuneration should be [fixed and capped](#)

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In addition to changing the governance of organisations, regulators must be given more resources, greater powers to collect evidence and [explicit directions](#) to mount investigations before and not after the systemic misconduct has been identified.

The use of consultants and the rapid expansion of their business model which bundles accounting, audit and legal services together presents is [another threat](#) to accountability and transparency. It is also an obstacle to investigating and successfully prosecuting systemic corporate misconduct.

Governments may have to legislate to outlaw the bundling of consultancy services, and abandon [accounting industry self-regulation](#) .

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Read more <http://theconversation.com/the-way-banks-are-organised-makes-it-hard-to-hold-directors-and-executives-criminally-responsible-93638>