Effects of increased regulation on small banks’ management control practices: A case study of a Swedish savings bank

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Abstract

This paper sets out to investigate the effects on small banks’ management control practices from increasing regulation following the 2008 financial crisis. The changes to banks’ management control practices may in turn have implications for banks’ competitive advantages and strategies. A qualitative case study of a Swedish savings bank was carried out, gathering data through six semi-structured interviews of representatives at different levels. Our findings indicate that the increased regulatory pressure has increased both the scope and scale of administrative as well as cybernetic controls. A relative change of focus, from business- to compliance-oriented was also detected in connection with the planning and cybernetic controls. The increase in mainly administrative controls and the resulting regulatory burden suggest that it may be difficult for small and decentralized banks to pursue their chosen strategy unless they are able to find alternative ways of dealing with this burden.

Keywords: regulation, compliance, banks, management control, decentralized, mechanistic

Sammandrag

Uppsatsen redogör för vår undersökning av effekterna av ökande reglering på små, lokala bankers styrning i kölvattnet av 2008 års finanskris. Förändringarna av styrningen kan i sin tur ha betydelse för bankers komparativa fördelar, och deras strategier. En kvalitativ fallstudie av en svensk sparbank genomfördes och innefattade sex semi-strukturerade intervjuer av medarbetare på olika nivåer. Resultaten pekar på att det ökade regleringstrycket har ökat omfattningen av styrning kopplad till governance, organisationsstrukturer, policies och processbeskrivningar men även uppföljning. En förskjutning av fokus, från affärsorienterat mot compliance-orienterat, sågs också i anslutning till styrning som hade att göra med planering och uppföljning. Den betydande ökningen av styrning övervägande kopplad till governance, organisationsstrukturer, policies och processbeskrivningar antyder att det kan bli svårt för små lokala banker att behålla sin strategi om de inte lyckas finna alternativa sätt att hantera den ökade bördan som den förändrade styrningen innebär.

Keywords: regulation, compliance, banks, management control, decentralized, mechanistic
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1 Introduction

1.1 Banks in a time of reregulation

The need for regulation of banks has been widely accepted long before the 2008 crisis. In the US, the Glass-Steagall Act from 1933 regulated banks to prevent “undue diversion of funds into speculative operations”, separated commercial banking from investment banking, and also included the creation of Federal Deposit Insurance Corporation in order to prevent bank runs (Federal Reserve History, n.d.).

A number of reasons have been given for why the banking sector needs regulation. The fact that banks have a large effect on the overall economy by providing financing and facilitating the transmission of monetary policy means that there is a complex web of stakeholders, other than shareholders, that are all dependent on banks’ well-being (Alexander, 2004). Banks also face a number of well-known potential moral hazard problems (Alexander, 2004). There is also an embedded adverse selection in banks’ credit origination, in that the customers willing to accept the highest interest rates, thus offering banks the highest revenue, tend to be those with the highest level of risk (Alexander, 2004). In addition, bank managers and employees are incentivized to increase lending and earnings in the short term, while the credit cycle is long, and exuberant practices may come to light much later (Dalio, 2018). The historic bailout practices of banks which are large enough to pose a threat to financial stability displays the moral hazard situation on a macro level (Allen, et al., 2015).

Since the 2008 financial crisis, banking regulation has been strengthened across the board. While the regulatory focus immediately after the crisis was to avoid future taxpayer-sponsored bailouts through tougher standards on capital and liquidity and the introduction of the Recovery and Resolution framework (Sironi, 2018), regulation has in recent years leaned increasingly towards matters of consumer protection, anti-money laundering, compliance and internal control (Véron, 2018).

Some of the more substantial new regulations which have been imposed on the banks since then include MiFID II (regulating capital markets and savings products), the Mortgage Directive, PSD 2 (payments and account information sharing) and the Insurance Distribution Directive.
Another area in which the regulatory framework has been tightened, and where requirements have become more granular, is Corporate Governance. The European Banking Authority’s (EBA) Guidelines for Internal Governance (GL 11), issued in 2015, outlines direct requirements on banks’ governance, in an attempt to reduce risks in the sector. Apart from outlining fairly detailed prescriptions for how banks should be organized, and how internal control should be exercised, GL 11 (and its predecessor GL 44) has also increased the focus on accountability.

1.2 Looking into the effects of regulation

Previous research has considered the effects of regulation on a range of different aspects, among them banks’ strategy and risk management practices, and points to several important implications in the long run.

An investigation of regulation’s effect on the strategy of a Dutch bank suggests that regulation favors centralization and large size, as this makes it easier to handle the increased costs and burden of governance and control (van der Steen, 2017). This in turn implies that regulation may make the banking industry more homogenous, and as a result increase the level of systemic risk.

The effects of regulation on banks’ risk management practices have also been addressed. Looking into regulation’s effects on the risk management practices of banks of different sizes, Elliot & Cäker (2017) find that smaller banks appear to be more negatively impacted by increased regulation, due to increased costs, and difficulties in keeping its local business model.

The implications are to a great extent similar to those suggested by van der Steen (2017): regulation exerts an isomorphic pressure that threatens the diversity of the industry, consequently putting financial stability at risk and creating a market with less choice for consumers, and reduced competition.

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1 In its press release announcing GL 11, the EBA states that: “Weaknesses in corporate governance in a number of institutions have contributed to excessive and imprudent risk taking in the banking sector…”
Risk management is often considered to be an important part of the larger management control (Mikes, 2009; Kaplan, 2011). However, the importance of considering the entirety of an organization’s management controls has also been stressed, as the different controls of an organization do not operate in isolation (Otley, 2016; Chenhall, 2003; Malmi & Brown, 2008).

As previous studies have predominantly been focused on specific parts of banks’ management control packages, an investigation of regulation’s effects on the management control package in its entirety should be worthwhile in order to get a fuller picture.

In addition, as regulators’ aim is to enhance inward accountability and “…create ‘better’ and more responsible banks and bankers (Stockenstrand, 2017, ch. 1) and management control is often defined as concerned with affecting behavior (Merchant & Van der Stede, 2018; Abernethy & Chua, 1996), the effects on banks’ MCS should also be of interest when considering possible outcomes of regulation.

The nature of management controls may be expected to play an important role in shaping the type of organization. A mechanistic approach to organization may, at least according to the traditional view, result in a “mindless and unquestioning bureaucracy” (Morgan, 2006, p. 42). Even though the view of bureaucracy has been nuanced in later years, to suggest that certain types of enabling bureaucracy may actually have positive effects (Adler & Borys, 1996), important potential challenges with highly bureaucratic organizations remain.

A mechanistic form of management system, with a heavy reliance on formal controls and hierarchy, has been argued to be appropriate for stable conditions whereas the more flexible, organic form is better suited for changing conditions (Burns & Stalker, 1961). Indeed, Elliot & Cäker (2017) point to challenges connected to reconciling the innovative process, with costly, formal controls demanded by regulation. In addition, the negative attitudinal effects associated with coercive types of bureaucracy may limit innovation (Adler & Borys, 1996). Considering the fast-paced environment and rapid technological advances currently seen in banking, mechanistic forms of management and organization could present a challenge to banks’ future competitiveness.

Considering the implications suggested by previous research on small banks as well as management control’s possible implications for behavior and innovation it appears worthwhile to investigate the effects of regulation on small banks’ management control practices, adopting
the package view of MCS. Although the scope of our investigation is limited, we still hope to get indicative conclusions on some of the effects of increased regulation in order to be able to make a small contribution towards a better understanding of the effects of regulation.

1.3 Purpose and research question

The purpose of our study has been to explore the effects of increasing regulation on management control in smaller banks, or, more specifically:

*What are the effects of increased regulation on small banks’ management control practices: A case study of a Swedish savings bank*

1.4 Disposition of the paper

Next, we go on to provide a definition of Management Control Systems (MCS) and a general overview of banking regulation. These are followed by a non-exhaustive review of the current knowledge on the subject of banks and regulation. The methodological section then goes on to present a conceptual model of our investigation and addresses choices and challenges with the chosen approach in addition to giving the reader insight into the empirical setting. Finally, the findings are presented and analyzed and future implications discussed.

2 Banking regulation and management control

2.1 Management Control Systems (MCS) as a package

There exists a wide range of definitions of MCS in use to date, and there is little agreement on which components are necessary to form a complete system (O'Grady, et al., 2016). For the purpose of this study, we have used the framework presented by Malmi & Brown (2008) to define MCS.

Malmi & Brown (2008, p. 290) suggest that “…systems, rules practices values and other activities management put in place in order to direct employee behavior should be called management control”. Consequently, they point to the importance of making a clear distinction
between systems exclusively used for decision-making or informational purposes, and those used to direct behavior in any way.

The framework of Malmi & Brown (2008) is the result of their analyzing and synthesizing several decades of MCS research and consciously adopts a broad approach to the concept in order to facilitate its use in empirical investigation. The wide scope of the controls in the typology constitute its strength, they argue, while acknowledging that there is of course a lot more to each control than is covered by the framework.

In addition, Malmi & Brown (2008) stress the importance of considering an organization’s collection of individual controls and control systems as a package rather than one system, as this better reflects the facts that its constituent parts do not operate in isolation, very often are not intentionally linked and are the result of incremental changes made by different actors over time.

The framework lists five, non-exhaustive, main types of control; planning, cybernetic, reward and compensation, and administrative controls. Malmi & Brown’s (2008) original figure of the typology (Figure 1) illustrates the roles of the different groups of controls; the broad but subtle cultural controls sit at the top, spanning the entire width and providing the context for the other types of controls. At the center of the figure are the planning, cybernetic and reward and compensation controls that are often tightly linked, presented in the order they usually occur. At the bottom, the administrative controls provide the structural foundation for the planning, cybernetic and reward and compensation controls.

![Figure 1, Management control systems package – Malmi & Brown (2008, p.291).](image)
Each of the framework’s main types of control will be shortly presented below.

**Planning Controls**

Planning is likely to have a major role in directing employee behavior (Malmi & Brown, 2008, p. 292) in the sense that it directs “effort and behavior” through goal-setting and enables coordination between the actions of groups and individuals. Operational planning in the form of task lists serves to guide behavior in a very straightforward way by providing task lists, for example. Planning can be divided into two subtypes, according to the time horizon; action planning deals with the actions and goals for the near future (usually the coming year) whereas long-range planning of action and goals is of a more strategic nature.

**Cybernetic Controls**

Cybernetic control is characterized by a loop in which performance of a system is measured and evaluated against pre-set standards and, if unwanted variances are detected, behavior is changed through the feedback loop. According to Malmi & Brown (2008), there is an important distinction to be made between cybernetic control systems that are used purely for information and decision making and those that are also used to direct and control behavior, as only the latter are considered true MCS Four basic cybernetic systems have been identified in MCS research (Malmi & Brown, 2008): budgets, financial measures such a Cost/Income ratio, Return on Equity and Economic Value Added, non-financial measures and hybrids such as the Balanced Scorecard.

**Reward and Compensation Controls**

Reward and compensation controls are used for motivating individuals and groups to perform better and achieving goal congruence by directing effort and enhancing its duration and intensity (Bonner & Sprinkle, 2002, cited in Malmi & Brown 2008). Usually, they are connected to the achievement of goals defined by the cybernetic controls, but not always. There may be other reasons for providing rewards and compensation; among them retaining employees and encouraging cultural control (Malmi & Brown, 2008).
Administrative Controls

Malmi & Brown (2008) identify three different groups of administrative control systems that direct employee behavior in different ways; organization design and structure, governance structures and the procedures and policies. Organization design and structure directs behavior by way of “encouraging certain types of contact and relationships” (p. 293). Flamholz (1983) argues that organizational structure “contributes to control through reducing the variability in of behavior and, in turn, increasing its predictability” (p. 158).

Governance structures direct employee behavior through establishing formal authority and accountability and include the systems that make sure that “representatives of various functions and organizational units meet to co-ordinate their activities both vertically and horizontally” (Malmi & Brown, 2008, p. 294).

Procedures and policies in turn direct behavior by “specifying the processes and behavior” within the organization though the use of standard operating procedures, rules and policies (Malmi & Brown, 2008, p. 294; Macintosh & Daft, 1987; Simons, 1987).

Cultural Controls

Drawing on the work of Simons (1995), Schein (1997) and Ouchi (1979), Malmi & Brown (2008) suggest there are three aspects of cultural controls to take into consideration; value-based controls, symbol-based controls and clan controls. Mission statements, visions and statements of purpose are examples of value-based controls. Symbol-based controls include work space design, dress codes and other symbolic measures intended to create a certain culture to guide behavior. Clan controls work through ceremonies and rituals that socializes individuals and leads them to adopt the values and beliefs of the group.

The Malmi & Brown (2008) framework has been criticized for not being detailed enough and considered of “limited potential” due to its patchwork nature (Siska, 2015, p. 145). The fact that the framework does not address how the controls may be interrelated or how they should function “as a collective whole” (O'Grady, et al., 2016, p. 3) also constitutes a significant weakness given the argued existence and importance of considering the interdependencies between management controls (Chenhall, 2003; Otley, 1980).
The importance of also being clear on whether one adopts the perspective of a consciously designed, interrelated system of controls or that of a package of controls that may or may not be interrelated has later been stressed by Grabner & Moers (2013). If the aim is to investigate the interdependencies of the different controls the package perspective is not adequate, they argue, as this is only suited for general descriptions of the observed “control environment” of the organization (p. 410).

While aware of the shortfalls of the Malmi & Brown (2008) framework we believed the framework’s broad scope to be suitable for our study as our intention was not to dive deep into the interdependencies of the different controls but rather provide a descriptive overview of the changes to the overall package. As our main aim with using the framework was to create a common understanding of the concept of management control with our interviewees and the framework’s definition has been found to adequately reflect the terms used by management accounting practitioners (CIMA, 2016), we believed it to be suitable for our purpose.

2.2 Banking regulation – an overview

Crawford (2017) defines banking regulation as including all legislative acts, decisions and recommendations that are aimed at reducing systemic risk, enhancing customer protection and the sound operation of financial institutions, whether they are legally binding or not. Elliot & Cäker (2017), similarly, refer to banking regulation as the “general regulatory pressure” facing banks. For the purpose of this study, when talking about regulation in a broader sense, we will adhere to Crawford’s definition.

As pointed out, the need for regulating banks is nothing new. However, the need for increased regulation in recent years has several reasons. The financial crisis of 2008 pointed to obvious structural weaknesses in the industry as well as its regulation (losses amounted to around USD 15trn, according to some estimates), which has led to a wave of re-regulation (Armour, et al., 2016).

Goodhart et al. (1998), in a pre-crisis effort to describe regulation in theoretical terms, describe the relationship between regulators and bank as a principal (regulator) - agent (bank) relationship, with the purpose of protecting society from the risk of the impact on society from a bank failing. Interestingly, they dismiss regulation being too comprehensive, since “if
regulators behave as if any bank, or any bank employee, might offend at any time, regulation becomes impossibly expensive for both regulators and banks. For example, frequent on-site examinations by the supervisors would be very costly.”

This contrasts to the European Central Bank’s (ECB) announcement of its guidelines for on-site inspections, published ten years later (ECB, 2018) stating that “inspections are a critical tool for banking supervision…”, and that “banks are inspected in order to provide an in-depth analysis of different risks, internal control systems, business models or governance”.

Kellerman & Mosch (2013) point to banking supervision2 historically having been focused around certain backward-looking statutory requirements. However, due to many of the failings in the crisis having to do with business models, strategy, conduct and culture, they argue for a more forward-looking approach. In short, they define “good supervision” of banks as being:

1. Intrusive
2. Sceptical but proactive
3. Comprehensive
4. Adaptive
5. Conclusive (here defined as resulting in action).

Another reason for why increased regulation is justified, other than the industry and supervisory failings becoming apparent in the financial crisis (Kellerman & Mosch, 2013), is presented by Armour et al (2016). The growth of financial markets and financial market investments has been significant, driven by various reasons such as demographics. In addition, Armour et al (2016) argue that the globalization of financial markets since the de-regulation in the 1980’s and 1990’s, and the subsequent increased international flows of investment has increased the contagion risks from adverse financial events.

Engwall (2017) describes a framework suggesting that banks’ governance is impacted by coercive regulators, mimetic market actors and normative scrutinizers, such as media or other reviewers or inspecting bodies, and that all of these interact, as they influence each other, and rely on each other’s efforts. As an example, “alarms from scrutinizers may lead to regulation

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2 Kellerman & Mosch include both the regulatory framework, as well as the act of supervising, in their broader definition of supervision
as well as new models among market actors”. Assuming that not only regulators changed their approach following the financial crisis, Engwall’s (2017) work suggests that looking at the impact of regulation only, may not give the whole picture of how banks’ governance may have been impacted since then, which needs to be considered as a caveat in our study.

The focus on accountability in the regulatory framework has increased (Kashyap, 2017). Partly, Engwall’s (2017) framework can help explain this, as a consequence of the “public rage about the lack of responsibility of managers and auditors” (Stockenstrand, 2017, ch. 1).

Davies & Green (2008, p. 12) argue that regulation happens in cycles – a point also highlighted by Stockenstrand (2017). Typically, negative events such as a financial crisis lead to a demand for tightened regulation either by regulators, or as Engwall (2017) points out, other stakeholders impacting regulators. After a number of years, the effects of the negative event fades, and regulations are viewed as damaging business efficiency, after which de-regulation follows.

Financial regulation can be divided into five main sub-sections (Davies & Green, 2008, pp. 34-93):

**Banking**, being one of the larger ones, includes loans and deposits, payments, the regulation of money laundering, and other items. Within this category we would find substantial individual regulations, such as the Capital Requirements Directive, which apart from regulations on capital and liquidity includes GL 11 mentioned above, the Mortgage Directive, and the Payment Services Directive. **Securities markets**, including stock exchanges and credit rating agencies; **Insurance regulation**, including regulation for insurance mediation; **Pension regulation**, **Financial reporting**, including accounting rules, as well as the regulation of auditing activities.

Most larger banks may well be impacted by all five sub-sections, since they trade in securities, and all have insurance and pension subsidiaries. This is, for example, the case in all of the four large Swedish banks, according to their respective annual reports for 2018 (Nordea, 2019; SEB, 2019; Swedbank, 2019; Handelsbanken, 2019).

While smaller banks may not own insurance subsidiaries, they may be indirectly impacted by the insurance regulation since it includes the Insurance Mediation Directive covering the selling of insurance or pension products. And while they do not necessarily themselves trade securities
in financial markets, the Markets in Financial Instruments Directive also covers advice of savings products, which the bank may engage in.

It is also worth looking at little bit closer on European Banking Authority’s guidelines for internal governance, GL 11 (EBA, 2017). The 57 pages of guidelines in GL 11 are detailed, and includes sections such as “Role of the risk committee”, “Role of the chair of the management body”, “Outsourcing policy” and, in a two-page annex, “Aspects to take into account when developing an internal governance policy”.

It also includes a number of guidelines which may require meticulous effort, if at all possible, to follow up on. Examples are that the chair of the management body should “encourage and promote open and critical discussion and ensure that dissenting views can be expressed and discussed within the decision-making process”, or that “Institutions should develop a risk culture through policies, communication, and staff training regarding the institutions’ activities, strategy and risk profile…”.

Interestingly, from the perspective mentioned above, about increased regulation possibly resulting in bureaucracy and more mechanistic organizations, there are aspects in GL 11 resembling some of Fayol’s 14 Principles of Management (Fayol, 1949):

Authority and responsibility – GL 11 says that “An institution should have a clear, transparent and documented decision-making process and a clear allocation of responsibilities and authority within its internal control framework”.

Scalar chain – GL 11 prescribes in detail how the management body should work in paragraph 23, both in its management and supervisory capacity, describing a clear scalar of command.

Unity of direction – a number of articles in GL 11, not least 1:23 prescribing management’s responsibilities in 13 different areas, and 1:27 prescribing that management has to “monitor,

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3 “The management body in its management function should constructively challenge and critically review propositions, explanations and information received when exercising its judgement and taking decisions. The management body in its management function should comprehensively report, and inform regularly and where necessary without undue delay the management body in its supervisory function of the relevant elements for the assessment of a situation, the risks and developments affecting or that may affect the institution, e.g. material decisions on business activities and risks taken, the evaluation of the institution’s economic and business environment, liquidity and sound capital base, and assessment of its material risk exposures.”
periodically review and address any weaknesses identified regarding the implementation of processes, strategies and policies related to the responsibilities listed in paragraphs 23…”.

Subordination of individual interest – in GL 11, section 12 lays out over three full pages how banks should deal with the risk of conflicts of interests for employees.

In addition to all of the above mentioned rules, there is a 61 paragraphs long section prescribing details of the control functions (risk, compliance and internal audit) of a bank, which, together with all the prescriptive policies, procedures, and indirectly documentation needed to show that GL 11 is in fact complied with, a certain Order is created too, even if it is a different kind than what Fayol (1949) intended. One can also argue, that GL 11’s detailed descriptions of responsibilities and how they should be divided throughout the organization, and the increased focus on accountability mentioned above, means that organizations need to fulfill the Unity of Command rule, where Fayol (1949) states that each employee can have only one line manager.

GL 11 (as many other regulations or guidelines) states explicitly that it should be implemented with a view of proportionality\(^4\). It has been pointed out in previous research, however, that this principle is currently surrounded by opacity and uncertainty (Elliot & Cäker, 2017), and hence, small banks seem to struggle with finding the right level of ambition when implementing new regulations. Considering that GL 11 is still fairly new, it may be that the regulators’ view of proportionality may be clarified or altered over the coming years, which one should bear in mind when investigating how smaller banks deal with regulation.

In our study, we have found it appropriate to look at the impact of the general increase (as in the volume and complexity) of regulation, in addition to the impact stemming from the content of those regulations. In particular, we are interested in the implications from GL 11 on management control practices, as it directly regulates banks’ governance, and certain controls which are important aspects of the chosen definition of management control packages.

\(^4\) GL 11 states that “The proportionality principle encoded in Article 74(2) of Directive 2013/36/EU aims to ensure that internal governance arrangements are consistent with the individual risk profile and business model of the institution, so that the objectives of the regulatory requirements are effectively achieved.” and that “Significant institutions should have more sophisticated governance arrangements, while small and less complex institutions may implement simpler governance arrangements.”
A brief and non-conclusive overview of some of the substantial recent, or changed, regulations which have been introduced in the last five years is available in appendix III.

2.3 Previous research on regulation’s effect on banks

As the focus of our study mainly concerns the effects of re-regulation in recent years, the literature search has been limited to the last 20 years. This is of course not to say that there have not been valuable contributions to the subject before that time, but it seems likely that the impact of contingencies like a very different regulatory environment, increasing globalization and digitalization that have been facing banks in later years, lessen the applicability of research carried out on banks’ management control in a significantly different time and environment.

There seems to be a time lag between the imposition of regulations and organizations’ adaptation (Crawford, 2017). However, considering the importance of the banking industry to society at large, and the fact that some years now have passed since the introduction of important regulations (eg GL 44 in 2011 and the Capital Requirement Directive IV in 2013), we had expected even more research to have been done in this area.

Our search in a number of top-ranked journals5 on the topic of regulations’ effects on banks generated a limited amount of results. Widening the search to the library database of Uppsala University6 yielded more results as it included a greater variety of sources such as books and thesis papers as well as specialized publications with a specific focus on the financial industry. The searches were performed using the search terms regulation and bank with wildcard endings in an attempt to try and cover various forms of the words. Subsequently the search term management control was added in order to search for results more closely related to our research question.


6 Swe. Bibliotekets söktjänst
Among the topics covered were regulations’ effects on banks’ efficiency (Barth, et al., 2013); (Kalyvas & Mamatzakis, 2014); (Lotto, 2018), performance (Cornett, et al., 2002), structure (Hodder, et al., 2003); and risk (Klomp & de Haan, 2012).

Closing in on the internal processes of banks in general and regulations’ effects on banks’ management control systems in particular, we found a number of studies concerned with the effects of regulation on different aspects of banks’ risk management practices and financial accounting.

Hodder et al (2002) look into regulations’ effects on accounting choices and risk management decisions in 230 American banks following the adoption of the “Statement of Financial Accounting Standards No. 115” regulation in 1993. The authors undertake an extensive quantitative analysis and point to economic as well as accounting consequences stemming from the adoption of the regulation. Hodder et al’s (2002) research represents a quantitative approach to the issue of regulation’s effects on financial accounting and risk management. However, in order to gain a more well-rounded understanding of the complex issue of regulation’s effects on banks’ internal processes, there are likely aspects of these issues that demand exploration using a qualitative approach.

Mikes (2009) provides an investigation into risk management practices within two banks. The regulatory framework in question (Basel II) appears to permit interpretation when designing risk management practices which has led to a divergence into two models of risk management, with differing characteristics. Mikes (2009) identifies a model influenced by a more “quantitative” culture (“risk management by numbers”) as well as a one connected to a more “holistic” calculative culture that is also concerned with non-financial risks and that which is not easily quantified (p. 36). Whether these models represent different schools of thought or different stages in the evolution of risk management practices remains to be seen (Mikes, 2009). In the article, the connection between regulation and the development of differing risk management models is not treated in any detail. Rather, the causal connection is more or less treated as a given and the main focus rests on the empirical observation and identification of the two models. Still, when setting out to investigate regulations’ effects on management control systems in a wider context, the different calculative cultures identified by Mikes (2009) may provide important input for the analysis as it has been argued that risk management should
be considered part of the larger management control systems package (Mikes, 2009); (Kaplan, 2011).

The book *Bank Regulation: Effects on Strategy, Financial Accounting and Management Control* (Stockenstrand, A-K; Nilsson, F (editors), 2017) provides a collected account of many different angles on the subject. An overarching theme is the tension that arises from external “demands for uniformity” and internal “demands for uniqueness” (Stockenstrand, 2017, ch. 1). One of the aims of the regulations of later years is improving comparability between banks for investors. This unintentionally drives banks toward uniformity as it was designed with the average bank in mind (Elliot & Cäker, 2017) and appears to favor certain structures over others (van der Steen, 2017).

The demands for uniqueness, on the other hand, stem from individual banks’ needs to be able customize and align structure, strategy and management control, following the reasoning of contingency theory. This conformism tends to negatively impact banks with a unique business model or way of operating the hardest (as opposed to banks with a high degree of scale, standardization and formalization).

A study that illustrates this tension was conducted by van der Steen (2017), investigating regulation’s effects on strategy at the Dutch cooperative Rabobank. Regulation affects strategy through, among other things, the need for changes in management control. Increasing costs and regulatory burden have gradually forced the bank to become more centralized, as it is cheaper and easier to work with regulatory compliance at large headquarters than at the level of every local bank. This development is counter to Rabobank’s long-standing tradition of being a decentralized cooperative of autonomous local banks and lessens the value of the bank’s previous competitive advantage built on a strategy where the decentralized format is key. In this case, regulation appears to render a proper alignment of strategy, structure and management control difficult, if not impossible.

Elliot & Cäker (2017) have looked into how regulation affects the risk management systems of two comparable banks of different size. As risk management is often considered an important part of the entire MCS-package (Mikes, 2009; Kaplan, 2011) their findings are of great interest when considering regulations’ effects on banks’ MCS-packages in their entirety. In short, Elliot & Cäker (2017) describe a situation where the big bank has greater resources and therefore is capable of shielding its internal processes and culture from the negative impact of regulation by negotiating with regulators and dealing with compliance issues at the head office. The small
bank, lacking resources as well as weight in negotiating with regulators, adopts a more passive approach to regulatory demands that are imposed on them. The small bank is to a greater extent negatively affected in terms of costs, difficulties with recruiting qualified personnel and an increasing misfit in alignment between strategy and management control. Elliot & Cäker (2017) make the case that regulation intended to increase transparency may have unfortunate and unintended consequences for financial stability and sound competition as it tends to make banks more similar and favoring bigger actors. Their suggested solution is not refraining from regulating the industry altogether but rather modifying regulation according to size in order to maintain diversity.

The only contribution appearing in our searches that explicitly sets out to investigate regulations’ effects on the different management control functions in general is that of Zeman et al (2018). Through the analysis of previous research (CIMA, 2016) and logical reasoning, Zeman et al (2018) assess regulations’ effects on the different management control functions (adopting the framework of Malmi & Brown, 2008) by comparing them before and after the 2008 crisis. Zeman et al (2018) find that in the case of financial controls, new budgeting practices have been adopted, and that administrative controls now include more comprehensive risk controls, governance and compliance management as well as and improved internal audit process. In addition, the Reward and Compensations control function appears to have grown in importance. The method employed; analyzing previous research for data could imply that the data has a poorer “fit” or is of less value as the original studies may not have been conducted with the same goal or questions in mind as the ones the authors have set out to answer (Saunders, et al., 2009). This unfortunately seems to be the case as the CIMA (2016) study that Zeman et al (2018) base their analysis on does not explicitly make a connection between regulation and the changes in MCS, and instead simply deals with the changes that have occurred since the crisis. In this respect, there appears to be a mismatch between the secondary data used and Zeman et al’s objective. There is also the obvious risk of the data not coming across as “rich” as it would had it been first-hand. The short and concise account provided by Zeman et al (2018) on the topic perhaps reflects this fact, even though it should be acknowledged that their assessment of regulations’ effects on constitutes only one of several objectives of their article.

The studies in Bank Regulations: Effects on Financial Accounting, Strategy and Management Control are focused on regulation’s effects on specific aspects of management control such as financial accounting and risk management, and none take a wider approach to regulation’s
effects on the entire MCS-package. This might be a result of the fact that it appears hard to connect regulation to internal processes (Crawford, et al., 2017) and that a more general inquiry considering the real-life MCS package in its entirety risks being less stringent, making the connections between concepts less clear. Still, Kaplan (2011b, p. 371) argues that an approach more connected to “clinical knowledge” also has merits as to consider as the foundations of knowledge rests on “systematic observation, description and classification”. In our view, both approaches are valid as long as the trade-off is duly recognized. Different approaches towards the study of the same phenomenon should ideally complement each other, adding to a more comprehensive picture. With this in mind, and while acknowledging the difficulty of connecting regulation and management control practices, we argue that an attempt should at least be made to look into the impact of regulation on banks’ MCS at a more general level as the impact of regulation on the management control practices overall is likely an important determinant of individual banks’ ability to compete.

3 Methodology

3.1 Conceptual model

An organization’s MCS-package is shaped by the interaction of different factors, external and internal, and is under continual development (Otley, 2016). Regulatory pressure, trends in management control, personal preferences of managers and board members, and the digitalization of bank services, among others, are all contextual factors that may have an impact on the development of an organization’s MCS package. In order to explore the effects of regulation on banks’ MCS practices, we performed a qualitative case study in which employees at different levels of a chosen bank were interviewed and asked to report perceived changes to the package resulting from added regulation during the ten-year period following the 2008 financial crisis. By identifying and examining the nature of these changes to the organization’s MCS practices we have attempted to gain a better understanding of regulation’s effects on the development of the package. Our line of reasoning is illustrated by the simple model below, in which the framework of Malmi & Brown (2008) is used to provide a general definition of the concept of a package of management controls.
3.2 Research design

Qualitative research emphasizes words and individuals’ interpretations of their social world when collecting and analysing data (Bryman & Bell, 2015). In addition, when a proper appreciation of the context is important, a case study strategy is suitable (Morris & Wood, 1991). With this in mind, a qualitative case study was chosen in response to the rich and complex nature of management controls and because we believed context to be important given its probable implications for the development of the organization’s set of management controls.

While allowing for the collection of rich data and contextual understanding, qualitative research and the case study format are criticized for being too subjective, impossible to replicate and not providing generalizability (Bryman & Bell, 2015). Still, given the difficulties with isolating variables and defining concepts discussed in section 2.3, the qualitative case study appears to provide a viable though admittedly imperfect alternative for investigating the effects of regulation on the package of management controls.

To match the wide approach taken to investigating the presumed changes to the control practices while still providing some direction to the conversation, the interviews were of semi-structured character. This allowed us to vary the order of the questions depending on the interviewee, to probe answers and ask follow-up questions. (Saunders, et al., 2009). The framework of Malmi & Brown was used to provide a general definition of the concept of management controls when designing an interview guide and eventually ordering and analyzing the collected data.

The interview format has some inherent risks. An interviewee may modify his or her answer in order not to appear disloyal to the organization, and the interviewer may unintentionally influence the interviewee. There is also the issue of the interviewer’s subjective interpretation.
of the words used and what follow-up questions to ask, as well as the non-verbal communication. Still, given the advantages of a semi-structured interview to a standardized survey in establishing personal contact and commitment on the part of the interviewees (Saunders, et al., 2009) the interview strategy appeared preferable for finding out how the effects on management control practices were perceived by the individuals whose behavior the systems are intended to control.

In order to be able to judge which changes could be attributed to regulation, we relied on the interviewees to make the distinction after having made clear that this was the criterion for inclusion. This approach entailed the additional risk that the interviewees misjudged or were unaware of the connection, and thereby included or excluded changes on erroneous grounds. Although by no means foolproof, the semi-structured interviews did permit us to ask additional questions where the connection was not evident and hopefully also served to make interviewees somewhat more aware of their own opinions and of causal connections they might not previously have considered.

3.3 Choice of study object

The bank was selected for the case study based on its specific characteristics; its small size\(^7\), informal style and local presence, all of which we believed to be factors that would make changes in MCS-practices stand out more clearly given the implications of size and decentralization suggested by van der Steen (2017) and Elliot & Cäker (2017).

The Swedish savings banks constitute a separate legal form and are governed by democratically elected representatives from the local community. They do not have any shareholders and profits are either reinvested in the business, or they are shared in the form of grants and sponsorship to the local communities. The savings banks have a strong local focus and are actively engaged in supporting their local communities also in other ways than financial contributions. The banks are independent but cooperate with each other through the National Association of Savings Banks (Sparbankernas Riksförbund), and jointly also have an agreement

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\(^7\) < BSEK 10 in total assets and < 120 employees in 2018
with Swedbank under which Swedbank is to provide products, IT infrastructure and services to all savings banks.

The savings banks’ customer satisfaction is significantly higher than that of the large four Swedish banks, but their profitability is similar, with an aggregated operating profit in relation to total assets of on aggregate 1.0% in 2018 for all savings banks (Sparbankerna, 2019), compared to an average of 0.93% for the four large Swedish banks as reported in their full year reports for 2018 (Swedbank 2019, SEB 2019, Handelsbanken 2019 and Nordea 2019).

3.4 Selection of interviewees

Six interviews were conducted with representatives from different levels of the organization. The request for interviews was directed at the chairman and the CEO. The request was for interviews with those two, the Chief Compliance Officer, and business representatives from both the corporate and the personal banking business lines. The CEO suggested who those business representatives were; the Head of Corporate Banking, the Deputy Head of Personal Banking, and one Personal Banking advisor. All interviewees have more than 20 years’ experience from the banking or financial industry and all but one have been with this bank for more than 10 years, which was helpful since the objective was to capture changes in management control practices over time.

Gathering input from representatives of different levels was deemed to be important as the magnitude and nature of changes are both often viewed and expressed differently at different levels (Marshak, 2002; Nadler & Nadler, 1998). It could of course be argued that as regulation gets more overbearing and complex, insight into its workings and impact diminishes at lower levels (Crawford, 2017). Even if that were the case, by also interviewing those who could be expected to possess rich insight into regulatory matters - the chairman, CEO and CCO - and thus diversifying perspectives, we hoped to gain a more balanced picture. In addition, even if the full overview and understanding of all regulatory changes may be known by client advisors, the impact on management control practices may well be.
3.5 Design of the interview guide

The conceptual model presented in 3.1 formed the basis for the general interview guide (appendix II). The typology of the Malmi & Brown (2008) model was slightly modified and translated into Swedish in order to try to reflect the terms and divisions commonly used in the industry and with which the interviewees were likely to be familiar.

3.6 Data collection

Four of the six one-hour interviews were held at the bank’s head office, and the other two were conducted over the telephone during a week in late May 2019. At the start of the interview, the background and purpose of our study was described, and the interview guide was presented and elaborated on. The interviews took departure in the interview guide but were also allowed to digress from the specific questions to a large extent in order to stay open to unexpected insights. We made a choice not to record the interviews, in order for all interviewees to feel more at ease, and the discussions to be more candid. Instead, extensive notes were taken by both of us and compared for content and accuracy directly following the interview. Four of the interviews were made without any other representative from the bank present other than the interviewee. The interviews of the personal banking advisor and the Head of Corporate Banking however were done jointly. These two had no manager/subordinate or other dependence to each other within the bank however, other than being colleagues.

Our choice not to record the interviews was made after weighing the risks of potentially losing data and not being able to go back and make sure that we had interpreted what was said correctly against the expected benefits of interviewees feeling less monitored and being more willing to share sensitive information. As we believed genuine content of interviews to be the primary determinant of the value of results, the risks mentioned of not recording the interviews were judged to be of less importance than the expected benefits.

3.7 Data analysis

The interview data in the form of notes was processed by sorting the reported changes and associated bits of data into the corresponding categories defined by the Malmi & Brown (2008)
framework. The changes were then considered category by category and the extent and nature of the changes to the overall package assessed.

4 Results

The results are presented in accordance with the Malmi & Brown (2008) framework for defining different types of management control; administrative, cybernetic, planning, rewards & compensation and cultural controls.

4.1 Administrative controls

Internal policies and procedures directing action have increased greatly. In order to fulfil the procedural requirements a customer advisory meeting now takes twice as long as before due to the added administrative controls, the personal banking advisor says. This increase is also felt by both the Chairman and the CEO:

“...initiating and updating the internal regulatory framework has become a major task in itself for management and board.”

The governance structure has developed over the last few years, as compliance and risk functions, as well as an administrative support function for regulatory documentation, have been installed. This represents a 10% increase of the total work force, and the group dealing with compliance issues may well continue to grow even more in the future in order to be able to deal with all regulatory demands according to the Chief Compliance Officer.

The CCO also pointed to significant efforts to create a more complete internal policy and regulation documentation framework, specifically pointing to GL 11 being a strong driving force for increased administrative controls.

Both of the interviewees working with private customers mentioned how there is now a template, instruction, or manual, for almost every activity they undertake.
4.2 Cybernetic controls

There has been an increase of non-financial measurements related to regulatory compliance while less emphasis is placed on financial and other business KPIs. The CEO noted:

“The number of KPIs has increased ten-fold, and the entire increase is related to regulatory compliance”.

The customer representatives also reported the introduction of more formal follow-ups, in the form of binary checklists, mostly related to compliance matters. The CCO pointed out that more stringent follow-up of activities is needed to show that there is internal control following up the adherence of the regulations.

4.3 Planning controls

There has been a decrease in strategic planning controls and instead more activity planning in direct response to the need for handling the increased, compliance-related, administrative burden. The chairman and CEO report spending a lot more time dealing with regulatory issues and less time on strategic business issues. In the words of the CEO:

“I used to have to spend about 30% of my time on administrative matters and was able to focus on business matters for the remaining 70%. Nowadays, it’s the other way around!”.

4.4 Reward and Compensation controls

There have not been any changes to the reward and compensation control practices yet but the CCO indicated that this might be coming. At present the variable reward system is not contingent on individual achievement, but the CCO said that in the future, compensation has to be more tightly linked to an individual’s adherence to compliance rules to be fully regulatory compliant.

4.5 Cultural controls

There has been a slight change to the cultural controls in the sense of a change to the practice of reinforcing shared values used to guide behavior. When hiring new staff, the earlier grounds for hiring, the applicant’s values, local origin and culture have become of less importance and second to new requirements of formal competence. These requirements are
directly tied to regulation as many employees have to possess certain certificates but also indirectly as the management points to the added complexity of the business brought on by the added regulation. As one interviewee puts it:

“Before we used to hire locals, people who knew what we as a local savings bank were about and shared our values and concern for the local communities. Nowadays that’s often no longer possible as it is quite hard to find local applicants who also possess the formal qualifications.”

5 Discussion

5.1 Interpretation of results

Even though the components of the MCS-package do not readily lend themselves to being quantified and it is difficult to define a starting point in absolute terms, it is still possible to make out general trends as the relative changes to the different types of control can be detected.

We were able to make out three main effects of regulation on the bank’s management control practices: significant increases in scope and scale of administrative and cybernetic controls, a slight decrease in cultural controls as well as an altered internal composition of the cybernetic and planning controls, with a stronger bias towards regulatory compliance. These changes to the composition of the cybernetic and planning controls in turn suggest a shift in the overall focus of controls, going from business-oriented to being more concerned with compliance matters. GL 11 specifically was pointed out as a driving force behind much of the increase in administrative control, and also in the increased focus on accountability, both on the management body, and on individual employees.

5.1.1 Effects on administrative control practices

The scope and scale of the administrative control practices have increased significantly, due to development of both the governance and organizational structures as well as the internal policies and procedures.
5.1.2 Effects on cybernetic control practices

The scope and scale of the cybernetic control practices have also increased, though mainly due to an increase in non-financial performance measures. This also entails that the internal composition of the category of cybernetic control practices has changed as the number of business-related financial measures remains unchanged, thus signaling a shift in focus from business to compliance.

5.1.3 Effects on planning control practices

There has been a change to the internal composition of the planning control practices in the sense that the strategic planning to some extent has been replaced by activity planning in order to deal with task of ensuring regulatory compliance. As the strategic planning had more of a business-oriented focus, the shift in focus is visible in these controls as well.

5.1.4 Effects on cultural control practices

The cultural controls are the exception as there appears to be a slight decrease to their scope and scale. This can be attributed to the fact that the organization is not able to make full use of its value controls when recruiting new staff as it is now forced to prioritize formal qualifications and proficiency.

5.1.5 Effects on reward and compensation control practices

The rewards and compensation controls are yet unaffected, but as noted earlier there are indications that this is about to change. If the changes do entail that individuals will be rewarded contingent on their compliance with regulatory demands as has been suggested, this would also of course add to the impression of a shift in focus from business considerations to regulatory compliance.
There are a number of connections to be made to the previous studies concerned with the effects of regulation on banks.

Zeman et al (2018) also noticed an increase in administrative controls in the aftermath of the 2008 crisis. Whether or not his effect was due to regulation was not made clear, but the fact remains that it aligns with our observations of the changes in administrative controls. The growth in importance of Rewards and Compensation control as a tool to achieve regulatory compliance mentioned in the 2008 study could not be found in our study, nor the changes to cybernetic controls in the form of changed budget practices. However, we note that changes to the Rewards and Compensations controls were considered, according to the CCO in the savings bank.

The increase of administrative controls that we have observed also appears to connect closely to the discussions of van der Steen (2017) and Elliot & Cäker (2017) on centralization and the implications of the size of bank, respectively. By way of increasing costs for ensuring regulatory compliance and the overall regulatory burden, the changes to administrative controls have made the bank even more dependent on Swedbank for compliance matters and it is evident that this is not an area that the bank easily could manage on its own. In this respect, the cooperation with Swedbank is reminiscent of centralization in the sense of Rabobank, and it could also be viewed as an attempt for the small bank at attaining the shielding effect of the large bank noticed by Elliot & Cäker (2017). Whether this will be enough to safeguard its individuality with respect to internal processes and culture remains to be seen.

The results from our interviews echo some of the concerns raised by small banks in Elliot & Cäker’s (2015) interviews where an increased focus on regulation is viewed to have been introduced at the expense of customer focus. A concern regarding the perceived change in focus from business to compliance was also voiced in several of our interviews, and visible in the changes to administrative controls as well as in cybernetic and planning controls. In addition, the great difficulty recruiting people that fulfill the requirements of regulation and the financial supervisory authorities in a small community voiced by the CEO of Small Bank (Elliot & Cäker, 2017) also came up during our interviews.
Another connection to Elliot & Cäker’s study, relates to the way in which the banks responds to regulatory changes. During our interviews, there was no mentioning of an active approach to mitigate the effects of regulation. In this way, the savings bank in our study came across as similarly passive as Small Bank in Elliot & Cäker’s study.

When considering the results of our study in connection with bureaucratic types of organization (Morgan, 2006) and mechanistic management systems (Burns & Stalker, 1961), the significant increase in administrative controls, both structure-wise as well as at the level of policies and procedures, does indeed suggest a shift towards a more mechanistic-bureaucratic type of organization. This impression is reinforced by the increase in cybernetic controls connected to employees’ regulatory compliance and the slight decline in the importance of cultural value controls.

Whether this shift has been accompanied by the negative effects on attitude or capacity for innovation associated with coercive types of bureaucracy (Adler & Borys, 1996) is unclear. Unfortunately, an investigation into the nature of the increased bureaucracy is well beyond the limited scope of our study. However, one of our interviewees did reflect on the massive increase of policies and procedures and commented that there appears to be a risk that employees exclusively focus on following the prescribed procedures without reflecting over the bigger picture. This risk, the interviewee reflected, was likely to be the greatest for inexperienced employees struggling with coping with the extensive bureaucracy.

Other than this observation, there were no indications of any negative behavioral effects in connection with the mechanistic shift. Nor did the issue of innovation come up during the interviews. Considering that the bank relies on Swedbank for much of its product offering and IT, the negative implications of regulation for innovation may not be of great concern in this specific case. The increased resources demanded for the development of new products may not pose a competitive problem for bigger banks within the traditional banking industry as all its competitors are facing the same regulatory conditions. However, with the emergence of FinTech-companies that are not subject to the same regulation yet partly compete with traditional full service-banks this might well change.
5.3  Strengths, weaknesses and limitations of the study

The study has served its purpose of providing an overall picture of the effects of regulation on the bank’s management control practices. Having said this, it is important to recognize that due to the general and somewhat superficial nature of the Malmi & Brown (2008) framework, there may be aspects of the organization’s management control that have not been captured in our study. Nor have possible interdependencies between controls been addressed, as this was judged to be outside of our scope of providing a general overview of the entire package of controls.

Our study would clearly have benefited from the use of an additional, less subjective source than interviews in order to be able to triangulate the data and provide more explicit examples of changes to controls. This would have served as a complement to the selective human memory and likely mitigated the risk that the interviewees exaggerated the extent of changes to those controls of which they are most aware and/or affected by. It would also have made the causal connections between regulation and changes clearer and more reliable. Unfortunately, our attempt at collecting information on changes in MCS in the annual reports and other available documentation\(^8\) failed as the information proved too general to be of value. Given more time and resources, it might have been possible to dig deeper in the organization’s internal documentation in order to find additional evidence of changes to the management control practices. This would likely have increased the validity of the results.

On the flip side, the interview data did in fact turn out to be as rich as we had hoped for, as the interviewees were very generous sharing their views and surprisingly candid. Although no significant ethical issues arose during the interviews, the presentation of results required careful consideration in order to reconcile a critical analysis and diplomatic account.

The case study design does not as such permit us to generalize the results of our study (Bryman & Bell, 2015). However, when considering the results in light of earlier studies that deal with related effects of regulation (Elliot & Cäker, 2017; van der Steen, 2017) they appear to align quite closely which could suggest that the experienced effects are not an isolated phenomenon.

\(^8\) Mål och Riktlinjer för Riskhantering (Pelare III)
6 Conclusions and further implications

The study set out to explore the effects of increasing regulation on the package of management control practices of a small savings bank. The effects of the increasing regulatory burden on the package of management control practices were found to consist of a significant increase of the administrative and cybernetic controls, a slight decrease in the importance of cultural controls and an overall shift from a business-oriented to a more compliance-oriented focus.

Though we approached the question of the effects of regulation from a somewhat different angle, we arrived at many of the same conclusions as previous studies considering regulation’s effect on strategy and risk management (Elliot & Cäker, 2017; van der Steen, 2017). In particular, the substantial resources needed for implementing and operating the controls demanded by regulation are not easily mustered by a small rural bank. This might in turn favor larger banks with greater resources, leading to the elimination of smaller actors.

In addition, by adopting a package view of the control practices and thereby getting a general picture of the bank’s control environment we were able to discern a move towards more mechanistic-bureaucratic form of organization. Whether this shift has led or in time will lead to the negative consequences associated with coercive bureaucracy (Adler & Borys, 1996) is yet unknown.

At this point, though, it should be worthwhile to investigate whether these effects of regulation on the management control practices can be observed in a larger number of banks with differing characteristics. The use of secondary data in conjunction with interviews would make it easier to more precisely gauge the nature of the changes to the management control practices, thereby improving accuracy. A larger study would hopefully also provide the additional benefit of finding out if a mechanistic shift is indeed occurring in other banks of different sizes as well.

If a mechanistic shift of banks’ management control practices, induced by regulation, does indeed prove to be a wider phenomenon it might also be worthwhile to look into what effects this mechanization appears to have had on bankers’ attitudes in the long run and whether regulation appears to promote coercive or enabling bureaucracies (Adler & Borys 1996). This should be of interest as it is likely an important determinant in whether regulation will succeed at reaching the goals regulators were aiming for or not.
7 References


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Appendix I

Interview guide

- Bakgrund och syfte
- Nya regleringar, som successivt blivit hårdare, några exempel är:
  - GL11
  - Mifid 2
  - AML directive
  - Personligt ansvar för styrelse
  - GDPR
  - Vi kommer att fokusera på GL 11 som handlar om governance och styrning
- *Management control* definierar vi enligt modellen nedan (modifierad version av Malmi & Brown, 2008):

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<td>Budget</td>
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- Vi är ute efter att förstå hur dessa aspekter har förändrats på grund ökade regleringar under de senaste 10 åren.
- Vikten av att skilja på vilka förändringar som orsakats av regleringar och vad som beror på annat.
Frågor:


2. Hur har ovan påverkat din roll specifikt?

3. Har de ökade regleringarna påverkat vad du lägger din tid på, idag jämfört för tio år sedan?

4. I avvägningen mellan styrning å ena sidan (påverkan av beteende genom hur man mäter och följer upp, t ex uppföljning av finansiella siffror, icke-finansiella mål som t ex antal kundmöten, individuella mål, osv), och kontroll å andra sidan (ex ante och ex post kontroll) – hur har MCS utvecklats?

5. Fråga till VD, Ordförande och Compliancechef: Hur många människor arbetar idag med compliance och riskkontroll i banken, jämfört med för 10 år sedan?

6. Fråga till VD, Ordförande och Compliancechef: Vilket av ovan nämnda regelverk har haft störst effekt på MCS (andra kan såklart ha haft påverkan på processer kring kundrådgivning och annat)? Vilka andra regelverk i övrigt upptar tid och fokus för er?

7. Upplever ni att regelverken gör det svårare att vara en liten bank, eller vägs de större bankernas skalfördelar upp av att kraven och komplexiten är högre?
8. Sparbanker har historiskt sett skiljt sig från konkurrenterna genom sin lokala närvaro och informella stil. Upplever ni att regleringarna påverkat era möjligheter att behålla er särart?
9 Appendix II

Below is a brief summary of some of the new regulations impacting banks in the last few years, taken from various regulatory bodies’ and consultant’s web pages. This appendix is merely intended to provide a description of the areas covered in each of the regulations.

An important aspect of all regulations, from a resource perspective, is that banks not only need to comply with them, they also have to show that they have controls in place to ensure that they comply with them. Hence, a bank cannot trust its strong culture, organizational learning or other informal mechanisms, but need formalistic top-down controls to ensure compliance. In addition, in many cases, the reporting, disclosure and documentation requirements are also vast.

It is also important to note that these brief descriptions do not fully reflect the magnitude of the new regulations. One example is that only the Swedish legislative bill to turn MiFID 2 into law was more than 700 pages (the full descriptions including the directive, the EU Market Abuse Regulation, the Swedish FSAs rules and guidelines, etc, are many thousands of pages). Another example of the detailed scope of the regulations is that within GL 11, only the section describing the role and responsibilities of the management body and its committees, is more than 10 pages long.

9.1 CRD IV – 2014

The Capital Requirements Directive IV (CRD IV) is an EU legislative package that contains prudential rules for banks, building societies and investment firms.

Most of the rules in the legislation have applied since 1 January 2014.

CRD IV is made up of the:

- Capital Requirements Directive (2013/36/EU) (link is external) (CRD), which must be implemented through national law, and
- Capital Requirements Regulation (575/2013) (link is external) (CRR), which applies to firms across the EU
CRD IV is intended to implement the Basel III agreement in the EU. This includes enhanced requirements for:

- The quality and quantity of capital.
- A basis for new liquidity and leverage requirements.
- Rules for counterparty risk.
- Macroprudential standards including a countercyclical capital buffer and capital buffers for systemically important institutions.

CRD IV also:

- Makes changes to rules on corporate governance, including remuneration.
- Introduces standardised EU regulatory reporting, referred to as COREP and FINREP. These reporting requirements will specify the information firms must report to supervisors in areas such as own funds, large exposures and financial information.

CRD IV strengthens the prudential framework for individual institutions and responds to financial stability concerns that arose during the latest banking crisis.

The CRD IV is a large package of regulations, including capital and liquidity regulation, rules for the recovery and resolution of banks, macroprudential standards for systemically important banks, governance regulation, regulatory reporting, and more. GL 11 is a response to the language in CRD IV around governance and control.

(Financial Conduct Authority, 2018a)

9.2 EBA Guidelines on Internal Governance (GL 11) - 2017

These Guidelines aim at further harmonising institutions' internal governance arrangements, processes and mechanisms across the EU, in line with the new requirements in this area introduced in the Capital Requirements Directive (CRD IV) and also taking into account the proportionality principle. Effective internal governance is fundamental if individual institutions and the banking system as a whole are to operate well.
Weaknesses in corporate governance in a number of institutions have contributed to excessive and imprudent risk-taking in the banking sector, which has led to the failure of individual institutions and systemic problems in Member States and globally. In order to address the potentially detrimental effects of poorly designed corporate governance arrangements on the sound management of risk, and to take into account the new requirements introduced in the CRD in this area, the EBA has updated its Guidelines on internal governance, originally published on 27 September 2011.

The Guidelines put more emphasis on the duties and responsibilities of the management body in its supervisory function in risk oversight, including the role of their committees. They aim at improving the status of the risk management function, enhancing the information flow between the risk management function and the management body and ensuring effective monitoring of risk governance by supervisors. The 'know-your –structure' and complex structures sections, especially following the ‘Panama events’, have been strengthened to ensure that the management body is aware of the risks that can be triggered by complex and opaque structures and to improve transparency. In addition, the framework for business conduct has been further developed and more emphasis is given to the establishment of a risk culture, a code of conduct and the management of conflicts of interest.

(European Banking Authority, 2017)

9.3 MiFID II – 2018

MiFID is the Markets in Financial Instruments Directive (2004/39/EC). It has been applicable across the European Union since November 2007. It is a cornerstone of the EU’s regulation of financial markets seeking to improve their competitiveness by creating a single market for investment services and activities and to ensure a high degree of harmonized protection for investors in financial instruments.

MiFID sets out:

- conduct of business and organizational requirements for investment firms;

- authorization requirements for regulated markets;
• regulatory reporting to avoid market abuse;

• trade transparency obligation for shares; and

• rules on the admission of financial instruments to trading.

On 20 October 2011, the European Commission adopted a legislative proposal for the revision of MiFID which took the form of a revised Directive and a new Regulation. After more than two years of debate, the Directive on Markets in Financial Instruments repealing Directive 2004/39/EC and the Regulation on Markets in Financial Instruments, commonly referred to as MiFID II and MiFIR, were adopted by the European Parliament and the Council of the European Union. They were published in the EU Official Journal on 12 June 2014.

MIFID II IMPROVEMENTS

MiFID II and MiFIR will ensure fairer, safer and more efficient markets and facilitate greater transparency for all participants. New reporting requirements and tests will increase the amount of information available, and reduce the use of dark pools and OTC trading. The rules governing high-frequency-trading will impose a strict set of organisational requirements on investment firms and trading venues, and the provisions regulating the non-discriminatory access to central counterparties (CCPs), trading venues and benchmarks are designed to increase competition.

The protection of investors is strengthened through the introduction of new requirements on product governance and independent investment advice, the extension of existing rules to structured deposits, and the improvement of requirements in several areas, including on the responsibility of management bodies, inducements, information and reporting to clients, cross-selling, remuneration of staff, and best execution.

(ESMA, 2018)


Core aspects from the 3rd EU Money Laundering Directive remain unchanged, such as record keeping, verification of businesses and people, and the establishment of beneficial ownership.
The new Directive does, however, implement the following changes:

- Risk assessments: Every financially regulated organization must have written and documented Anti-Money Laundering/Counter Terrorism Financing (AML/CTF) risk assessments, policies and procedures. They must have a process which has been tested to assess their effectiveness and implementation, which is proportionate to the size of the organization.

- Enhanced due diligence: The definition of a Politically Exposed Person (PEP) is being enhanced: - organizations will now need to consider if a beneficial owner is a PEP - people with high level appointments in the UK will now be PEPs - enhanced measures will need to apply for at least 18 months (rather than the former 12) after a PEP leaves office.

- Beneficial ownership: There is a new requirement for all companies, legal entities and trustees to hold adequate, accurate and up-to-date information on their beneficial owners. They are also required to make this available to those involved in AML/CTF due diligence and law enforcement agencies.

- Simplified due diligence: Simplified due diligence provisions are no longer specifically contained in the 4th Directive, although individual countries may permit simplification following an evidence-based assessment within their jurisdiction.

- Record keeping: Further clarity around record keeping requirements is included to attempt to make them more consistent with the requirements of the data protection legislation.

- Scope and minimum sanctions: The current limit on cash transactions of €15,000 will change to €7,500. Legal entities will be required to keep a record of who their beneficial owners are, and the scope of money laundering regulations maybe extended beyond casinos to other forms of gambling. Minimum sanctions for breach of AML/CTF requirements have been outlined, including public reprimands, removal from practice, and financial sanctions of up to 10% of total annual turnover or €5 million.

(Grant Thornton, 2017)
9.5 Insurance Distribution Directive (IDD) – 2018

The Insurance Distribution Directive is EU legislation which sets regulatory requirements for firms designing and selling insurance products.

The Insurance Distribution Directive (IDD) replaces the Insurance Mediation Directive (IMD). It aims to enhance consumer protection when buying insurance – including general insurance, life insurance and insurance-based investment products (IBIPs) – and to support competition between insurance distributors by creating a level playing field.

Like the IMD, the IDD covers the authorisation, passporting arrangements and regulatory requirements for insurance and reinsurance intermediaries. However, the application of the IDD is wider, covering organisational and conduct of business requirements for insurance and reinsurance undertakings. The IDD also introduces requirements in new areas, including product oversight and governance, and enhanced conduct rules for IBIPs.

Source: (Financial Conduct Authority, 2018b)

9.6 General Data Protection Regulation (GDPR) – 2018

Under the GDPR, the data protection principles set out the main responsibilities for organizations.

The most significant addition is the accountability principle. The GDPR requires you to show how you comply with the principles – for example by documenting the decisions you take about a processing activity.

Article 5 of the GDPR requires that personal data shall be:
(a) processed lawfully, fairly and in a transparent manner in relation to individuals;
(b) collected for specified, explicit and legitimate purposes and not further processed in a manner that is incompatible with those purposes; further processing for archiving purposes in the public interest, scientific or historical research purposes or statistical purposes shall not be considered to be incompatible with the initial purposes;
(c) adequate, relevant and limited to what is necessary in relation to the purposes for which they are processed;
(d) accurate and, where necessary, kept up to date; every reasonable step must be taken to ensure that personal data that are inaccurate, having regard to the purposes for which they are processed, are erased or rectified without delay;

(e) kept in a form which permits identification of data subjects for no longer than is necessary for the purposes for which the personal data are processed; personal data may be stored for longer periods insofar as the personal data will be processed solely for archiving purposes in the public interest, scientific or historical research purposes or statistical purposes subject to implementation of the appropriate technical and organizational measures required by the GDPR in order to safeguard the rights and freedoms of individuals;

(f) processed in a manner that ensures appropriate security of the personal data, including protection against unauthorized or unlawful processing and against accidental loss, destruction or damage, using appropriate technical or organizational measures.

Article 5(2) requires that “the controller shall be responsible for, and be able to demonstrate, compliance with the principles.”

(Information Commissioner's Office, n.d.)