NACD NATIONAL ASSOCIATION OF CORPORATE DIRECTORS

PART 1

Catalysts for Transforming Culture Risk into Culture Value

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It seems recently that one can't escape reading stories about poor leadership gone wrong. It's time for action from the boardroom, and it's no longer good enough to ask unstructured questions about a company's helpline. Nor is good enough to rely on one's own experience, instinct, and blind spots in the boardroom to hold management accountable for a healthy culture.

Trust-but-verify culture might be a good way for boards to move forward. While it is critically important to have trust in the CEO, blind trust can only lead to blind alleys where bad cultures can fester and become toxic. The board needs to be equipped with a way to periodically and in a customized and simultaneously adaptable manner understand the company's culture.

The need for directors of companies to get under the skin of the culture of their organization has never been greater—or more necessary and daunting. Witness the many culture disasters we have recently seen from Uber, Wells Fargo & Co., The Weinstein Co., and Wynn Resorts. Over the past 25 years as a corporate executive, advisor, and board member, I have witnessed and advised on responses to similar instances of culture gone wrong—the good, the bad, the ugly, and, in one or two cases, the uglier. And I have also seen what a good culture can do to propel a company to greater reputational and financial heights (and returns).

It is important to share some of the tools, lessons learned, and insights on how the board can peel back the layers of the culture onion to begin to understand what is going on inside their companies, above and beyond the surface that boards are usually privy to. We start with a look at what happened in 2017 to understand the workplace culture maelstrom that the #MeToo moment has ushered in and crystallized.

A Year in Culture Dysfunction

2017 was a year filled with tales of organizational culture gone wrong. We learned about negative and destructive behaviors in the workplace, mostly perpetrated by powerful leaders, causing serious human, economic, and reputational costs for people and organizations. The toxic workplace cultures extended from the pinnacles of political power to the front lines of manufacturing facilities.

Powered by the ubiquity and raw reach of social media, the #MeToo story quickly became universal—told first by the more glamorous denizens of Hollywood and then extending to the most vulnerable hotel, restaurant, and factory floor workers. All of them were victims of a toxic workplace culture of abuse of power, shame, and lies. Worse still, many victims are submitting to terrible work conditions, are sidelined from needed jobs, or are permanently derailed from pursuing desirable careers and professional passions.

Time magazine's choice for the 2017 Person of the Year, the "Silence Breakers," said it all. Though sparked by the Weinstein exposé, the #MeToo story represents the culmination of decades of pent-up workplace silence, lies, cover-ups, manipulation and anger. The overwhelming impact of the #MeToo phenomenon can only be explained by the explosion and maturation of social media, which has led to the amplification and acceleration of reputation risks tied to workplace culture.

Why 2017 Stands Out

Two other relatively recent periods of corporate cultural moments, if we can call them that, come to mind: 2002 and 2008. The downfall of Enron, WorldCom, and others resulted in an uproar about financial accountability and the adoption of Sarbanes–Oxley in 2002. Nearly six years later, we witnessed the downfall of financial giants Lehman Brothers Holdings and Bear Stearns Cos., leading to the humiliation of the U.S. financial sector in general for the massive mortgage and derivative-related scandals, leading to social awakenings such as Occupy Wall Street and the adoption of the Dodd-Frank Act.

While these two watershed moments were important, 2017 was arguably the most momentous year yet for matters of corporate culture. In both the 2002 and 2008 cases, the cultural issue revolved around financial malfeasance. The cultural issue of 2017 is qualitatively different. Challenges are being made against toxic personal behaviors in the workplace perpetrated mainly by leaders against their subordinates, and those actions demand a qualitatively different approach to oversight that is more proactive and requires the ability to look behind the numbers and the dashboards.

By 2017 we had also arrived at the convergence of two other significant developments not fully present or developed before:

1. the rise of the importance to business of environmental, social and governance (ESG) issues (especially in the US, as Europe has long focused on ESG); and
2. the acceleration and amplified impact of reputation risk associated with ESG risk (which includes workplace cultural issues) because of the age of social media and hyper-transparency.

Companies can no longer reactively manage their reputation in this hyper-transparent environment. Companies have to earn it proactively and watchfully, and getting to the bottom of the culture of their organization is of paramount importance for the C-suite and board.

Culture: A New and Urgent Focus for Boards

As the ***NACD 2017 Blue Ribbon Commission Report on Culture as a Corporate Asset*** was prescient in addressing, boards and executive teams must immediately focus on understanding the culture of their workplaces as part of the value chain and strategy. But they must also understand how to get to the root of any workplace culture dysfunction that may exist.

In this era, the excuse that only shareholders matter no longer holds. Boards and management are responsible to all of their stakeholders for ESG results as well (shareholders, employees, customers, and beyond), which include proactively maintaining and nurturing a healthy workplace culture. In the age of hyper-transparency, it does not pay to turn a blind eye or to wait for a crisis to hit. The rapid-fire downfall of not only Harvey Weinstein but of his entire company, including its damaged board and board members, is the cautionary tale of the day.

On the positive side, there is plenty of evidence that while a toxic culture destroys value, a strong and resilient culture fully championed and embodied by the very top of the organization (read: CEOs and directors) can and will add long-term sustainable value to the company's reputation and financial bottom line. Such values protect the organization from the crises that will inevitably come and add bottom line financial value, as the famous Johnson & Johnson Tylenol case first demonstrated.

Is our Current Culture Moment Fleeting or Momentous?

We are certainly witnessing a cultural moment. The real question is this: will this moment pass with no more than a whimper, or will it become momentous?

The 2017 stories have definitely awakened awareness at the very top of corporate leadership—at least for now. In one day in December at two major governance gatherings sponsored by NACD in New York City—at Leading

Minds of Governance and the NACD Director 100 Gala—this author witnessed how the #MeToo movement was top of mind for directors in general and dominated discussions both public and private throughout that day. Energized directors and experts who were present underscored the importance of action in this moment for the boardroom, and how this topic must be addressed in the long term as part of the board's responsibility.

Thus, I would argue that this moment is not a fleeting one. The importance of this moment cannot be over-emphasized. It's one that will be captured by responsible leaders and boards. Indeed, this is a unique time for leaders to step up to their responsibility for creating and owning a healthy workplace culture and for boards to acknowledge and embrace their responsibility: exercising proactive oversight of—and holding management accountable for—creating and maintaining a healthy workplace culture.

The Culturally Attuned Board

The culturally attuned board is one that is organized to understand the company in depth and to leverage that understanding for the success of all its stakeholders. What does that mean in real terms? It means, first, that the board has the tools necessary to understand what the culture really is—to peel that onion to get to the heart of what the tone is not only at the top (in the C-Suite), but also at the grass roots—including among entry-level employees. Second, it means that the board is aware of the red flags that might tip them off to a culture issue or problem. And third, it means that the board does not rest on its laurels but makes the culture conversation a permanent fixture of its work with the CEO, C-suite, and employees generally.

The next blog in this series will describe three specific tools that boards should implement, as well as the ten questions the board should ask to dig deeper and what should be on the board's culture dashboard.

Dr. Andrea Bonime-Blanc is founder and CEO of GEC Risk Advisory, a strategic governance, risk and ethics advisor, board member, and former senior executive at Bertelsmann, Verint, and PSEG. She is author of numerous books including The Reputation Risk Handbook *(2014) and* The Artificial Intelligence Imperative *(April 2018). She serves as Independent Ethics Advisor to the Financial Oversight and Management Board for Puerto Rico, start-up mentor at Plug & Play Tech Center, life member at the Council on Foreign Relations and is faculty at the NACD, NYU, IEB and Glasgow Caledonian University. She tweets as @GlobalEthicist. All thoughts shared here are her own.*

PART 2

Three Tools for Overseeing Corporate Culture

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Now is the time for boards to take culture risk seriously and begin to find ways to understand it in advance of a toxic culture truly damaging an organization. The recent examples of bankruptcy at The Weinstein Company and the rapid loss of $2 billion in market cap at Wynn Resorts only serve to underscore the close connection between leadership and culture and toxic leadership and toxic culture with reverberations and repercussions not only on shareholders but stakeholders of all types.

In this second part of this blog series addressing culture oversight, I suggest three practical tools for boards to exercise proactive oversight on culture issues to enhance discussions that may already be in process. Embedded in these tools are the top ten questions the board should ask management about culture, as well as some of the key dashboard metrics a board should consider getting.

Tool One: Arming the Board With the Right Information From the Right Members of the Management Team

Your chief ethics and compliance officer (CECO) and another executive (perhaps the chief learning, human resources or talent officer) are all good resources to report to the board from time to time and regularly on issues of culture. Indeed, an empowered CECO may be the best bet as she should be reporting to the board (or a committee thereof) on a quarterly basis anyway. His or her dashboard of ethics and compliance metrics should also include some of the key culture metrics described in tool two, below.

Moreover, the board or appropriate committee (audit, risk, compliance, regulatory affairs) should have regular executive sessions with the CECO and perhaps develop more informal methods of regular communication such as a phone call check-in between the CECO and the chair of the audit committee, for example, something I have done in my executive career and to great benefit of the organization.

When a company of a certain size, maturity, and complexity does not have an executive of the appropriate stature taking care of culture issues, it may indicate that the CEO doesn’t think culture is that important. Moreover, if there is an executive who should be thinking about culture issues proactively but is not or is not allowed the ability and resources to do this (for example, budget for a culture survey), that presents another potentially serious culture red flag. Last, other red flags may emerge when senior executives are not able to provide the arguably correct answers to the top ten culture questions the board should ask (listed below).

The Top Ten Culture Questions the Board Should Ask:

1. For the CEO: What does culture mean to you, and what is the importance of culture to you personally as the leader of the company? How would you, as the CEO, characterize the culture of the organization? Is it healthy, improving, ailing, or under serious stress?
2. Does the company have an explicit culture program in place and, if so, what does it consist of? Is it intertwined and integrated with the company's mission, vision, values, and strategy?
3. If there is no current culture program in place, what is management's plan to deploy one? What is the plan's timing, budget, leadership, and details?
4. How do you measure culture at the company?
5. How do you keep management at the highest and middle levels accountable on culture issues?
6. Is there a member of senior management or the c-suite with an explicit remit to manage corporate culture?
7. Does the company's performance management program and incentive structure incorporate cultural considerations and metrics? If so, how? If not, what is the plan to incorporate such considerations?
8. What are the top culture issues at the company today (good, bad, or ugly)?
9. When there are difficult culture issues (the bad and ugly kind), how does management handle them?
10. Is management aware of investor, employee, customer, and other stakeholder concerns or perspectives regarding corporate culture? Has there been any stakeholder reach-out on this issue?

Tool Two: The Customized Culture Dashboard

The company's board should be reviewing a customized dashboard that is updated regularly. Such a dashboard should be unique to each organization but should include many of the following qualitative and quantitative considerations and metrics.

- Ethics and Compliance (E&C) Metrics
    - E&C risk assessments – key data, key topics
    - Helpline or hotline trends and key issues
    - Training and communications trends and topics
    - Pulse surveys on ethics and compliance program
    - Investigations – type, process, and outcome

    - Periodic internal and external evaluations of the effectiveness of the E&C program
- Employee and Culture Survey Metrics
    - Culture climate metrics geared at workplace issues including supervisory relationships
    - E&C program benchmarking against peers
- Human Resources Data
    - Intake interviews
    - Exit interviews
    - Performance management results (with financial and non-financial metrics, as well as environmental, social, and governance metrics, included)
    - 360 leadership assessments or the like

Tool Three: Benchmark Your Company's Culture and be Prepared to Intervene

Understand where your organization fits in the spectrum of workplace culture. An example of useful benchmarking may involve using the **Ethics Research Center's Global Business Ethics Survey**. Get a culture survey done. Slice and dice it, and work to understand its results. Ask management about the culture climate, the temperature and how it is reflected at different divisions, business units, and more. Do your company's culture surveys have consequences or are they merely window dressing? If the latter, why do them? If the former, what are the actual concrete consequences? Do "golden boys/girls" who are abusive get counseled, disciplined, or terminated when infractions occur? Or are they ignored or merely slapped on the wrist for things that get others fired?

If and when a culture issue threatens to suffuse the wellbeing of an organization and its leadership, the board must be prepared to intervene in a crisis—before or after it unfolds. The board's keeping its finger on the cultural pulse and temperature of the company is vitally important to the long-term viability and sustainable profitability of a company.

With Gloom Also Comes the Promise of Light

With all the doom and gloom that toxic workplace culture issues raise, I would also underscore a hopeful note to boards and executives struggling to deal with the organizational cultural issues so clearly brought to the fore in 2017. Unlike the regulatory responses to the excesses of 2002 (Sarbanes Oxley) and 2008 (Dodd-Frank), I would suggest that the appropriate response to cultural issues that are emerging is not new regulation but self-regulation, a voluntary upping of the corporate cultural ante by elevating the importance of ethics, compliance, and risk management within organizations, powered and driven by a strong culture of accountability and "walk the talk" from the top. This entails a voluntary, value-creation mindset at the executive and governance levels of an organization that aligns a strong and resilient culture with sustainable profitability and that likewise recognizes that a toxic culture will in the short and long run lead to value and reputational erosion and possibly destruction.

Thankfully, there are positive tales to be inspired by. A case in point: Microsoft Corp. Under its relatively new CEO, Satya Nadella, who recently wrote **a book** on the company's culture, has instigated culture change there that by all accounts has had dramatic and beneficial impacts on all stakeholders, internally (employees) and externally (customers) alike. Nadella's moves have also benefitted shareholders. When he became CEO in 2014, the share price was around $35; today, Microsoft's share price is at $92.

With all the negative news, 2018 represents a rare opportunity for management and boards to understand, acknowledge, and tackle workplace cultural issues head on and in a more systematic and conscientious way. Culture is the fabric of an organization and that fabric can either be healthy and sustainable, able to contribute to the development of resilience and creation of value, or brittle, weak, and toxic, leading to financial and reputational vulnerability, value erosion, or even ruin. It is the direct responsibility of leaders—both management and board—to make the right choices on workplace culture.

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PART 3

Culture and ESG Governance: Inseparable In the #MeToo Era

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While I am not sure that it should be a radical idea, the following concept seems radical to some: internal organizational culture and external environmental, social, and governance (ESG) matters are, and should be, intimately and inextricably interconnected. They're two sides of the same coin. I believe that it is not only time for boards to get cracking on internal culture governance, but that it is also a core part of good modern governance for directors to know the key ESG and corporate responsibility issues relevant to their companies. By tying the two together, boards can proactively and carefully oversee management's efforts to act on these often siloed, disparate, or even ignored and untreated parts of a more resilient organization.

#MeToo, #TimesUp, and #NeverAgain

In the first and second installments in this series, I discussed these movements, context around them for corporate governance, and what directors might do to best oversee these risks. It has grown apparent that these movements also are related. So, what do the #MeToo, #TimesUp, and #NeverAgain movements have in common? Beyond simply being hashtags, they are movements that emerged in reaction to perceived and real decades of troubling policies, behaviors, and practices in both the private and public sectors. They represent both external stakeholders' reactions as well as potential reputation risk and attendant financial losses to companies and their leaders (including boards).

These movements also represent a singularly contemporary phenomenon which both management and the board should proactively respond to: the intricate and deepening interrelationship of internal corporate culture and external ESG and stakeholder issue management. These two aspects of running a business have been long ignored or sidelined as not important to a business, but they are now emerging and, arguably, merging before our eyes. It is the job of management and the board to understand, manage, and oversee these governance imperatives effectively.

Mini-Case Studies

A company's treatment of external stakeholders is a mirror of its culture. The following four cases offer stark examples of the two extremes of how companies treat their stakeholders.

Cautionary Tales

- **The Weinstein Company** The toxic culture spread by its CEO and founder Harvey Weinstein was ignored, supported, tolerated, and proactively encouraged by its executives and board for many years. **Take a look at this "Frontline" documentary** to understand the full extent of the actions that led to the bankruptcy of this Hollywood film powerhouse. This case illustrates the intertwining of toxic culture on the inside with no sense of corporate responsibility. It also demonstrates disrespect for outside stakeholders such as established and aspiring actresses and other key third parties.
- **Wynn Resorts** The news out of this company affords another example of a long-standing toxic culture initiated and vitiated by the CEO and apparently supported or ignored by his handpicked board. Key stakeholders such as employees and third parties were adversely affected. Now the **ex-wife of the deposed CEO and chair is leading the charge** to create positive change at both management and board levels with an aggressive plan to cleanse and grow a healthy culture from the boardroom down into the organization.
- In both of these cases it's likely that neither board ever asked the CEO or management questions about internal culture or exercised oversight of ESG and stakeholder issues. It would not be surprising in both cases to learn that the board actively or passively ignored culture and responsibility issues while focusing exclusively on the financial bottom line.

Model Responses

- **Merck & Co.** The pharmaceutical company has for decades had a succession of great CEOs who have led the company to financial success while building a strong culture of integrity and social responsibility. Witness the crisis management of the complicated Vioxx case by former CEO Ray Gilmartin who voluntarily withdrew the medication, in contrast to Merck's competitor with equivalent challenged medications. The explanation? Merck did not want to adversely affect their most important stakeholders: customers and patients. Current Merck CEO, Ken Frazier, continues their long-standing tradition of having both a strong internal culture and being a leader on **cutting-edge ESG issues externally.**
- **Starbucks** A company with leadership that for years was known for having an enlightened corporate culture and for proactively managing its corporate social responsibility (CSR) initiatives may weather its current Philadelphia store racial incident better than most because of this close interrelationship. Starbucks' ingrained, demonstrated care for its stakeholders were like muscle memory, allowing their management team

to respond in lockstep with their lived values. How else does a company's reputation survive this kind of incident and go further than probably any other company would by shutting down 8000 stores country-wide for a day for implicit bias training?

The Role of the Board

In the face of this challenge and opportunity, what should boards do? First, they should oversee the internal culture of the organization which we talked about in **part 2 of this series**, and which the ***NACD Blue Ribbon Commission Report on Culture as a Corporate Asset*** discusses at length.

Second, boards must get much more involved in overseeing and ensuring that management has the right ESG and stakeholder relations program in place. The right program will embrace the interests of important stakeholders like customers, regulators, the media, suppliers, and current and future employees, among others.

And third, any discussion at the board level of culture or ESG should connect the two topics. Culture is part of ESG, and ESG is part of culture.

Crises that are not well managed can mean the difference between value creation and value destruction. Organizations need to forge a culture that is consistent both on the inside and the outside. When something critical happens, an organization that has forged a robust and resilient culture on the inside is more likely to weather the storm than a company that has paid little or no attention to laying a sound culture of values. Indeed, such enlightened companies may even have a reputation and value creation advantage, as I have discussed at length in my book ***The Reputation Risk Handbook: Surviving and Thriving in the Age of Hyper-Transparency***.

Seven Critical Questions the Board Should Ask Management

As boards wrap their minds around the oversight of internal and external culture, they should consider asking the CEO and management the following critical questions:

1. Does the leadership (CEO/C-Suite) ever discuss culture?
2. If so, is it only culture talk (nice speeches, pretty pictures, glad-handing) or does it include culture walk (budgets, resources, reports)?
3. Is there at least one high level executive who has "culture" explicitly included in his or her portfolio of responsibilities? If not, why not?
4. Is there at least one high level executive who is in charge of managing ESG issues that are critical and important to the mission, vision, values and strategy of the company? If not, why not?

5. Have ESG issues been identified as core and critical to the wellbeing of shareholders and key stakeholders (employees, customers, regulators)?
6. When there has been a crisis involving ESG issues (e.g., a chemical spill, an allegation of executive harassment, an accusation of corruption) what is the track record of the company in handling that crisis? Were they prepared or did they manage the crisis by the seat of their pants?
7. Is there an effective integration of key roles on ESG issues between human resources, legal, ethics and compliance, risk, public relations, and others that are relevant? Or is the management of such issues siloed, fly-by-night, or otherwise non-existent?

The answers to these and additional questions will lead to a holistic look at the culture of the organization, and will allow the board to understand what buttons need to be pushed to help the organization attain consistency, synchronicity, viability, transparency, and value in the marketplace.

The way a company treats its external stakeholders starts with its internal culture. And the internal culture of an organization starts and ends with leadership. The greatest responsibility of the board at the end of the day is to hold the CEO and the executive team responsible and accountable for all aspects of strategy—not just financial results.

#TimesUp for boards that are ignorant, negligent, or oblivious to these central issues.

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