

# Putting Culture Risk on the Board Agenda

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**Culture is important, and the board sets the tone from the top. More than that, the board needs to actively ensure that the company has a positive healthy culture, and not a toxic one that leads to unethical behaviour and overly risky activities.**

**C**ulture is the system of values, beliefs, and underlying assumptions that shape behaviour, both in the workplace and the surrounding environment in which a company operates.

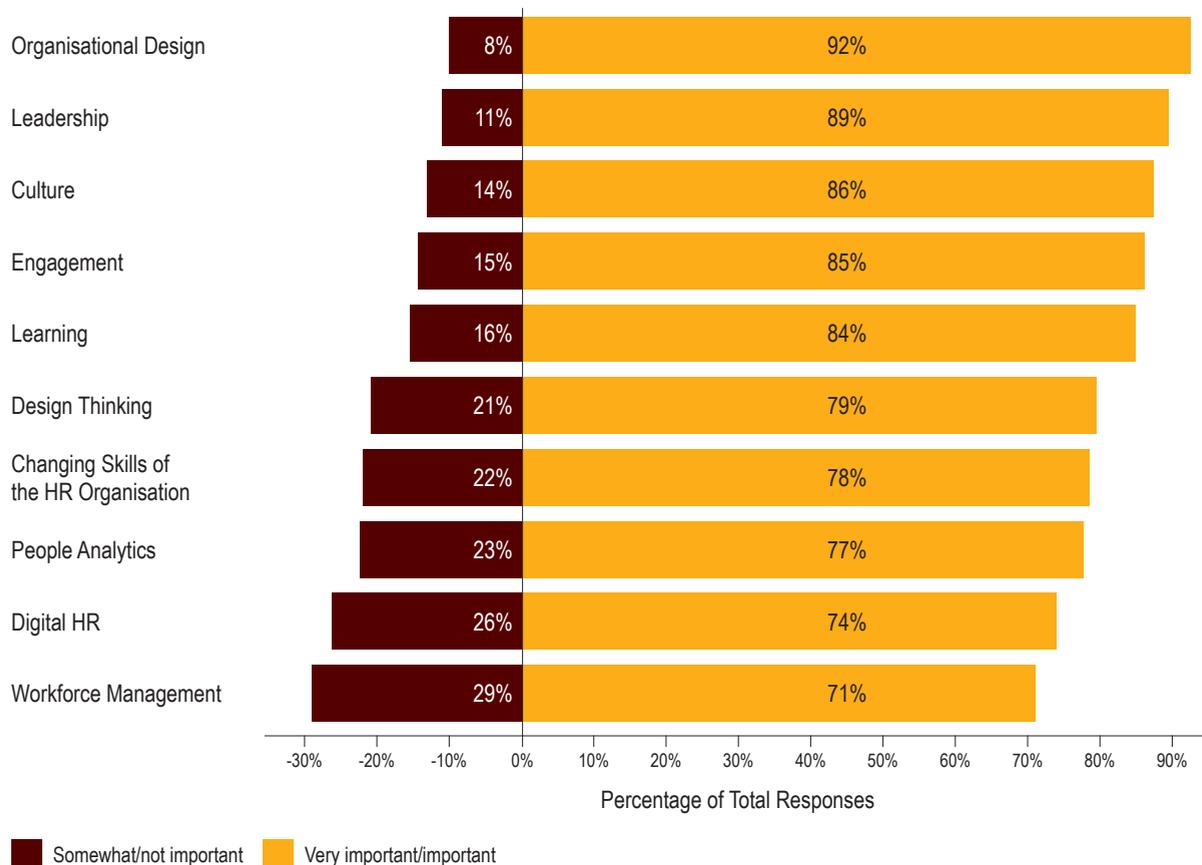
Promoting the right culture is important for companies. A global human capital survey by Deloitte shows that an overwhelming 86 per cent of business and HR leaders rate culture as either important or very important (see chart, “Top 10 Human Capital Trends”). A further 82 per cent agree that culture is a potential competitive advantage. However, only 12 per cent believe their company is driving the right culture.

### Culture continuum

Culture is a continuum ranging from highly positive to highly toxic. It is shaped by a number of factors, many of which cannot be controlled by or even known to the company. For instance, people’s individual values, attitudes, and behaviours, which may widely vary in an increasingly diverse workplace, all play a role.

Complicating matters is the fact that most companies contain multiple sub-cultures that vary from one operating region, business unit, or working team to another. This is why the “tone at the top” may be much different from the “tone in the middle” in each of the latter.

### Top 10 Human Capital Trends



Source: Global Human Capital Trends Report 2016 by Deloitte

This means that though a company may want to proactively shape a desired culture, changing existing cultural habits often takes considerable time. On the other hand, it may need to mitigate the risk of a positive culture “tipping” into a toxic one, since decay can happen quickly.

### Board considerations

An important consideration for the board is being able to recognise the signs of a culture at risk – for instance, when the company’s values and beliefs are not embedded or when the prevalent values, are not the right ones. This could result in behaviours that do not respect stakeholders such as customers, employees, suppliers, investors, and business partners.

One warning sign of a culture at risk is when financial, sales, production, or other performance measures become the primary business purpose.

Another is when undue pressure is placed within the company to achieve those metrics. When this occurs, employees could find themselves engaging in unethical or overly risky activities in an attempt to align correct management incentives with their compensation. In other cases, employees may fear losing their jobs if they fail to meet aggressive sales, production, or financial targets.

As boards begin to prioritise corporate culture, they should start looking at the considerations set out in the box, “Key Factors for the Board on Corporate Culture”.

## Key Factors for the Board on Corporate Culture

- **Culture governance.** Boards should ensure they devote sufficient time for discussions on culture. This may vary depending on circumstances. Mergers, acquisitions, or other restructurings that will have an impact on culture may require greater attention. Or perhaps the lead oversight responsibility for culture should be assigned to a board committee.
- **Monitoring culture.** A board should be satisfied that it is getting the right amount and quality of information about the company’s culture necessary for their oversight purposes. It should also consider the impact of its decisions on the company’s culture.
- **Public commitment.** What information does the company disclose about its culture and values internally to employees, and externally to stakeholders through its filings, website, or other disclosures?
- **Compensation practices.** The board’s remuneration committee should review senior management’s compensation to ensure that inappropriate activities are not inadvertently being incentivised.
- **Board and management oversight.** Boards and senior management must set the appropriate “tone at the top” through their words, actions, and behaviours.
- **Follow-through.** While it is important that management keeps the board updated on the company’s culture, boards should undertake their own analysis to ensure that the tone at the top established by management and the board is actually cascading through the company.

## Shaping corporate culture

A toxic culture can undermine a company's values, impede change, and support behaviours that damage financial performance, reputation, and brand. It is the management's job to build and manage a healthy culture, but the board plays an important role. Directors must therefore choose between working with management to properly shape the company's culture, or let the culture evolve on its own and shape the company.

The board's first task is to work with the CEO to develop and agree on the company's core values and the desired culture, and also to develop a compelling mission and vision. Great companies tend to have a "purpose beyond profit" which helps develop the kind of culture that attracts top talent, and motivates people. It also creates a powerful force for meaningful performance, not just within the company, but also in the communities and countries in which the company operates.

It is also important to have a clear and meaningful code of conduct that articulates the values needed to achieve the company's strategies, and to build its reputation and brand. Together with a compelling mission and vision, this code forms the foundation of the board's expectations of organisational culture; and helps ensure that, in the midst of the challenges of daily operations, all are mindful of the board's expectations of the way business is to be conducted.

The third point to make is that an integral part of organisational culture is implementation and enforcement. Obviously, a code of conduct alone is not enough. Many of the companies at the centre of scandals boasted impressive codes of conduct filled with all the key values one would expect. The problem was essentially one of

people not following those codes. An important test of any code of conduct, in other words, is the way it is enforced, and non-compliance issues are resolved. That means the code has to be universally applied across the company without exceptions.

## Walking the talk

Now, if getting everyone on board is a crucial part of the process of shaping the organisational culture, it is equally clear that the board must walk the talk and set the tone from the top.

This is easier said than done. To operate according to the company's purpose and core values without compromise, or adaptation to local conditions, is not a straightforward task. The challenge is compounded by the changing demographics in the workforce, and the increasing proportion of women in the workplace and in leadership roles, all of which impact organisational culture because of the different expectations, behaviours and lifestyle of workers and leaders within the company.

A healthy culture is a winning culture. It is one that achieves the company's purpose and strategies, and generates energy, excitement, and ongoing innovation. It can even create a competitive advantage though there are low barriers to entry. But creating a healthy culture requires hard work and leadership. The board needs to ask questions like: do we have the leadership and talent to execute on our strategies? Are we organised in the right way to achieve our strategies and to develop the capabilities of our people? ■

*This article has been adapted with permission by the author from a previously published article, "On the board's agenda - Would you recognise the warning signs of a toxic culture?" by Deloitte Global Center for Corporate Governance.*