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The Role of the Board in Corporate Culture

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The American management guru Peter Drucker is believed to have said that "culture eats strategy for breakfast". By this, he meant that strategies, even the most well developed, can be resisted, and execution can fail, in the face of an unsupportive culture.

And yet, even though strategy is (quite rightly) analysed in depth alongside corporate governance, culture is rarely the subject of much consideration at the board level. This, despite the consensus about its importance to sustainable success. If anything, any question or debate about culture tends to be squeezed off the agenda.

Against this context, we need to ask: What role does the board have in relation to the culture of the company?

One view argues that corporate culture is more appropriately set by the CEO and senior management as they face the company's staff, clients, suppliers and other stakeholders on a daily basis.

The opposing view, and one taken by regulators in some countries, sees it as fundamentally a board responsibility. This is because when something goes wrong, the board will be held accountable by shareholders and regulators.

Thus, Australian regulators are increasingly holding boards directly responsible for the oversight of corporate culture, while their British counterparts have now added the subject to the UK Code of Corporate Governance.

So, if directors accept that they are, for all intents and purposes, the custodians of their company's culture, how then should they act as a positive influence, but without interfering in the management of the company?

One of the board's key responsibilities is to select the CEO. That decision will usually have a profound impact on culture simply because the fastest way to change culture is to change the CEO.

BOARD'S AGREEMENT

However, the actions of any CEO will only be possible with the tacit understanding and agreement of the board. This would have been conveyed to the new CEO appointee via a set of values that the board and senior management agree upon, imparting to the CEO how things are done in the company, and how the board expects the CEO and his or her team to act in their daily running of the business.

The reverse is true. Any scandal, crisis or fraud by the CEO and senior management is likely to take place with the complicity of the board, even if it was complicit by omission.

Enron Corporation is an example of that. Former Enron CFO Andrew Fastow (who was in town last month to give a talk at the Singapore Institute of Directors) provided a stark revelation of what went on behind the scenes. He admits that he knowingly misled investors, but what he did was known and approved by the board (and the auditors and lawyers). In fact, he was praised by the board for his clever financial engineering which eventually led to Enron's collapse in 2000.

The Enron board turned a blind eye and deaf ear to its culture of extremism embodied by the unethical pursuit of profit at all costs, rewarding such behaviour handsomely, and placing a high value on the cleverness of its people rather than on their integrity.

The irony was: Enron appeared to be an excellent corporate citizen, with all the corporate social responsibility (CSR) and business ethics tools in place. The Enron board then was content that the company ticked the right boxes – without necessarily ensuring that the right culture flowed through the organisation.

Corporate culture and style over integrity and substance was what led to the unravelling of the Enron façade and exposed the business catastrophe within.

It is therefore important that the board – especially the chairman, who sets the tone for the entire board – clearly demonstrates to the CEO what values are considered important and by which the CEO's performance will be evaluated. The chairman and CEO must both walk the talk on shared values.

For example, the board of a construction or manufacturing company with a focus on health and safety should insist on the minimising of accident rates in its review of the CEO's performance. Customer complaints and customer loyalty indices provide clues to cultural changes, while board site visits and meet-the-staff sessions give directors the chance to gauge the mood in the middle.

Hiring and compensation policies should be reviewed for the corporate culture the board seeks to promote. Directors must be especially cautious of bonus schemes that encourage recklessness or hinder teamwork; or of commissions that encourage unhealthy sales techniques. And, above all, the board should ensure that their whistleblower policy is accessible and dependable.

For the board to be effective in setting and guiding corporate culture, the chairman should put an emphasis on director training to better prepare them for their role in this.

It is seldom easy to assess the health of a company's culture, but that does not mean it should be relegated or ignored. Directors do well to have corporate culture as a board agenda item for regular review to assess if the culture is changing (for better or worse); whether it is consistent with the company's stated values and strategy; whether it creates risk or encourages sub-optimal performance; and, generally, whether it is adding long-term value to the company. ■