ACTIVATING CULTURE AND ETHICS FROM THE BOARDROOM

The 2021 Ethics, Culture, and Compliance Forum Report

tapestry NETWORKS

LRN Inspiring Principled Performance

About this report

Corporate culture is crucial to the long-term sustainability of any company. Healthy culture drives ethical behavior and financial performance.

Toxic culture, employee misconduct, or ethical lapses can destroy enterprise value. Boards of directors face a dilemma: they recognize the urgency of their oversight responsibilities for culture, but acknowledge that culture is difficult to evaluate and shape. Fulfilling those responsibilities may require them to work with management in new and potentially uncomfortable ways.

In collaboration with LRN, Tapestry Networks set out to assess the current realities of board oversight of corporate culture, ethics, and compliance, grounded in the experiences and perspectives of sitting public company directors. **Activating culture and ethics from the boardroom** reflects insights from in-depth, confidential interviews with approximately **40 directors** who occupy almost **80 public company board seats**, including some of the largest companies in the world.* *For a complete list of interviewees and their affiliated companies, please see the appendix on page 35.*

40
in-depth interviews with directors

MALE 55%
FEMALE 45%

$4.8T
market cap represented

80
public company board seats

Operations on **6** continents

Our key findings:

- Boards are responsible for ensuring that executives shape culture and compliance.
- Directors fear they are not well-positioned to "read" corporate culture, which they find to be inherently challenging to interpret.
- As oversight practices evolve, boards struggle to find a natural home for culture, ethics, and compliance.
- Trust is a key enabler of transparency and is indispensable to a board's ability to oversee culture.

* This document reflects the use of a modified version of the Chatham House Rule whereby names of participants and their company affiliations are a matter of public record, but comments are not attributed to individuals or corporations. Quotations in italics are drawn directly from interviews with participants.

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Introduction

"Values and ethics are better in the long run for the bottom line. It's a board's responsibility as representatives of shareholders and stakeholders to make sure that we're doing everything we can to make sure the company has culture that is more likely to lead to positive outcomes."

Directors are acutely aware of the urgency of ethics, compliance, and corporate culture for the success and survival of their businesses.

One director with deep professional experience in this area said, ***"These issues are as essential to the long-term success of a business as financial performance. The board, not management, must own it. Management must be held accountable for culture, even if financial performance is on target. The results of not recognizing this are scandals and the deterioration of the long-term sustainability of the business."***

As corporations are increasingly called upon to articulate a sense of purpose and a clear set of values while balancing the interests of a range of stakeholders, their ethical and compliance performance and their cultures have come under sharper scrutiny. Consumers, policymakers, and the public expect companies to deliver on their promises: treating employees fairly, being responsible environmental stewards, promoting racial justice, and working to benefit their communities. Public attention to corporate culture and corporate ethics has never been higher, and ethical lapses or revelations of toxic culture can quickly dominate the narrative, eroding trust from consumers, investors, policymakers, and regulators, as well as threatening a company's license to operate.

In response, boards are giving increased attention to oversight of culture, ethics, and compliance. One director said, ***"More and more board time is being spent on culture. It's on the agenda at every board meeting."***

However, directors acknowledge that culture is a particularly challenging area to evaluate and oversee. Culture is hard to measure and quantify, so directors often turn to intuitive assessments. Board structures and oversight processes vary, and directors lack confidence that the reporting they receive paints a true picture of a company's culture. One director said, ***"This is a difficult area to oversee because it requires judgment. There is no formula. It's difficult to make sure management is making the right decisions."***

"Culture is an 'under-overseen' area for boards."

Large, global companies face heightened challenges. Senior leaders' efforts to establish a consistent culture and an ethical standard for a global company can conflict with divergent local cultural norms and behavioral standards. A company with thousands or millions of employees is hard for directors to monitor and evaluate, and each one of those employees represents a potential ethical or compliance failure. Relationships with third parties—suppliers, vendors, distributors, agents, franchisees—open up additional avenues for ethical compromises and reputational damage. While directors acknowledge that they cannot avoid all misconduct in a massive organization—***"There is no town of 100,000 people with nobody in jail,"*** a director said—they are committed to avoiding systemic misconduct and toxic culture.

There are no simple roads to superior oversight of culture and ethics. One director said, ***"Culture is an 'under-overseen' area for boards. It's hard for boards to get their finger on."***

What is culture?

One of the first questions directors often raise is how is to define culture and its relationship to ethics and compliance.

What are boards actually doing when they oversee culture? Culture is a broad concept with a range of meanings, typically encompassing shared values, implicit and explicit norms, habits, language, and expectations. While directors recognize that part of a board's responsibility is to align culture with strategy, in this report we focus on the ethical aspects of culture. Directors offered several shorthand definitions of corporate culture:

- ***"Culture is 'how we do things around here,' not so much the rules and policies, but an informal collective understanding of how we do things."***
- ***"I always think of culture as the way things get done at a particular company. It's the rules of engagement, it's authority, it's decision-making processes. It's the way things actually get accomplished in a company."***
- ***"Culture is who you hire, who you fire, and the behaviors you tolerate."***
- ***"It's about people doing the right things for the right reasons when no one's watching."***
- ***"We expect people everywhere in the company to make the same decisions we would if we had the same information."***

Delineating the relationship between ethics and compliance and corporate culture remains a challenge. While ethics and compliance are clearly related to culture, they require differing approaches to oversight. As one director said, ***"Culture is broader than ethics and compliance."***

The distinction can affect boards' expectations for their management teams. There are no widely accepted best practices here. Boards look to many executives to lead culture: chief ethics and compliance officers, chief human resources officers, CEOs. One director said, ***"Compliance is different than ethics and culture. The chief compliance officer can oftentimes focus on programmatic elements rather than culture, which is more about people. They are connected, but I wouldn't say that a compliance person would necessarily be your culture person."***

What is culture?

Many directors suggested that, in contrast with culture, ethics and compliance is a straightforward oversight area, one in which reporting structures and information sources are relatively well-established. One director said, ***"Corporate compliance and corporate ethics is as standard an issue for boards as financial management. For ethics, it's about common business practices, laws, the rules you set up, training, and, for compliance and ethics, some ombudsman to help the organization self-police. Corporate culture is more troubling to deal with. It goes well beyond compliance and ethics."*** Another director agreed: ***"Ethics and compliance has been a relatively well-trodden path for some time, with a lot of established best practices. Culture is a much less well-trodden path. Most boards seem to be just beginning to try and get a handle on it—how to define it, how to engage with management on it, and how to try to understand what exactly is going on at the company how you monitor and provide oversight for it."***

Yet some directors acknowledged that board oversight of ethics and compliance can be uneven. ***"Some companies struggle to provide good information about ethics and behavior policies or adequate regulatory processes and reporting,"*** commented a director. Ethics and compliance executives report that they are looking for more rigorous board oversight in this area and say that most boards spend too little time on ethics and compliance, don't have adequate metrics in place, and fail to hold management accountable.[1] The persistence of corporate compliance failures and ethical lapses suggests that even a well-established ethics and compliance program can be undone by an unhealthy culture.

[1] LRN, *What's the tone at the very top: the role of boards in overseeing corporate ethics & compliance* (LRN Corporation, 2018).

01 | Accountability and delegation

Responsibility and accountability for culture, ethics, and compliance flow from the board through top and middle management to front-line employees.

Accountability is non-negotiable.

While boards will be held accountable in law, regulation, and public opinion for lapses in compliance or ethics, they largely rely on management—starting with the CEO—to establish and reinforce ethical behavior, compliance, and healthy company cultures. ***"Management has to drive culture but the board can help set the tone with hiring, compensation, and in interactions with management,"*** said one director. Accountability is non-negotiable, but boards vary in their approach to holding senior managers accountable for their own conduct and the culture of the organization, especially with respect to the link between compensation and culture.

The right CEO

Directors recognize that boards have limited ability to influence culture directly and must rely on senior management to translate values into day-to-day actions. That process starts with the CEO. Directors agree that a CEO's commitment to ethics and culture is indispensable and that the responsibility cannot be delegated. ***"I think the right tone has to come from the CEO. If you have the right CEO, that person gets the management team aligned. The board shouldn't really have to be driving that internally,"*** a director said.

One participant said, ***"The perfect time to focus on culture is during CEO transitions."*** Hiring the right CEO, and replacing the wrong one, are among the most influential actions boards can take to promote healthy cultures. A candidate's fitness in this regard, participants said, is one of the most important considerations for boards in the succession planning process. Boards scrutinize executives' track records on culture in other organizations and look for signs that they have built loyalty and trust on previous teams. ***"I was on a recruiting committee for a CEO search. We were replacing a founder of the business, which was difficult, but it was really an opportunity to think about the strengths we wanted. A big part of each interview with the candidates was about culture, and whether promotions, hirings, and firings were consistent with a cultural outlook,"*** a participant recalled.

Beyond making the right hire, how can a board be sure that the CEO is articulating, transmitting, and reinforcing mission, values, and purpose throughout the company? Communication from the CEO is critical, and boards look for CEOs to make regular and consistent communications via policies, websites, and other means. But directors want to see compelling evidence that a CEO emphasizes compliance and ethical behavior. They examine how the CEO interacts with the senior team, the tone he or she fosters in boardroom discussions, and the level of access the CEO encourages between the board and other executives. One director suggested exploring whether the CEO is spending time with employees below the senior team, creating opportunities to reinforce cultural norms and expectations.

> ***"The right tone has to come from the CEO."***

Many participants emphasized that, in addition to communicating commitment to ethics and culture to the organization, it is important for a CEO to repeatedly model the same commitment during interactions with the board. ***"I hope that the CEO is bringing to the board, and that the board is really clear about, the organization's mission and values. Everyone in the room should be clear about those things, embrace them, and incorporate them into all communications,"*** a director said.

Driving management to see and shape culture

A culture of integrity promotes compliance and drives ethical outcomes, and does so more effectively than a rules-based approach. No code of conduct or set of policies, necessary as those are, can be detailed enough to govern every employee decision, and a company's ability to monitor employee behavior is limited. It is vital that a commitment to ethical behavior, compliance, and integrity be internalized throughout the organization, and it starts with management.

One way that boards can shape culture is by urging executives to articulate a clear vision for the culture they want to achieve and to develop a detailed strategy for getting there. This usually implies a need for change, and one challenge, a director said, is that ***"management typically doesn't think that it has a problem to begin with."*** Even when executives have a vision for the culture they want to achieve, ***"they often fail to articulate an ethics, compliance, and culture strategy for getting there that is relevant to the board."*** Boards can help management probe for blind spots by pushing executives to learn from issues or crises faced by other companies. A participant recalled an example: ***"When a widely reported scandal happened at another company in a different industry, the board challenged management to think, We are in a very different industry, but if it could happen at that company what makes us think it can't happen here? How can we monitor things internally and know what to be concerned about?"***

Participants also stressed the importance of integrating culture strategy with business strategy. One director insisted, ***"Obviously, culture should be a key part of the company's business strategy."*** Another identified the need for companies to ***"align culture with strategy and ensure that everything is consistent."*** But this can be difficult to accomplish. For companies in highly regulated industries or those with strong safety cultures, viewing culture and business strategy through the same lens may be routine. For other companies, a perceived dichotomy remains. When culture and ethics are viewed as an "added ingredient" rather than a core element in strategy, there is heightened risk of good behavior becoming optional. Some cultural aspirations—entrepreneurialism, creativity, tenacity—are widely considered as positive and even essential to a company's strategy. Yet participants emphasized that "cautionary" aspirations—adherence to safety policies and codes of conduct, reporting malfeasance, sensitivity to social issues—are essential to risk minimization, corporate reputation, and financial performance, and need to be considered just as strategically important.

The chief ethics and compliance officer and the board

Several participants lamented the fact that chief ethics and compliance officers (CECOs) or equivalents sometimes lack the stature to ensure that ethics issues get the necessary time, attention, and resources from the board. While few directors insisted that all CECOs should report directly to the CEO, many participants hoped to see CECOs obtain elevated status to more fully expose directors to ethics and compliance matters and examples of employee behaviors that reveal culture. Even more important than the position of the CECO in the organizational chart is the quality of his or her relationship with key board members. Some directors drew an analogy: the CECO should have a relationship to the relevant committee chair akin to that between the head of internal audit and the audit committee chair. ***"You need to establish that same sort of relationship between the CECO and the chair of the compliance committee,"*** one director said. This can help the board hear about issues in a timely way: ***"The board should want to know about issues early to understand the problems. As a director, you need to make that expectation clear with your CECO."***

When culture and ethics are viewed as an "added ingredient" rather than a core element in strategy, there is heightened risk of good behavior becoming optional.

It takes time and effort to establish such a relationship. Executive sessions with CECOs and one-on-one calls between committee chairs and CECOs—and other interactions outside of formal meetings—are common ways of doing so. These settings foster the candor that boards and CECOs need to raise touchy issues. ***"It's helpful when a CECO can tell you something in a private session knowing that it won't blow up in their face. We seem to get to the right answers better that way,"*** a participant said. Another director said that committee chairs can shape board reporting and internal communication through these interactions: ***"As audit chair, I have private sessions with my CECO, who has dotted-line reporting to me. I speak informally and formally with that person about expectations and lines of communication."***

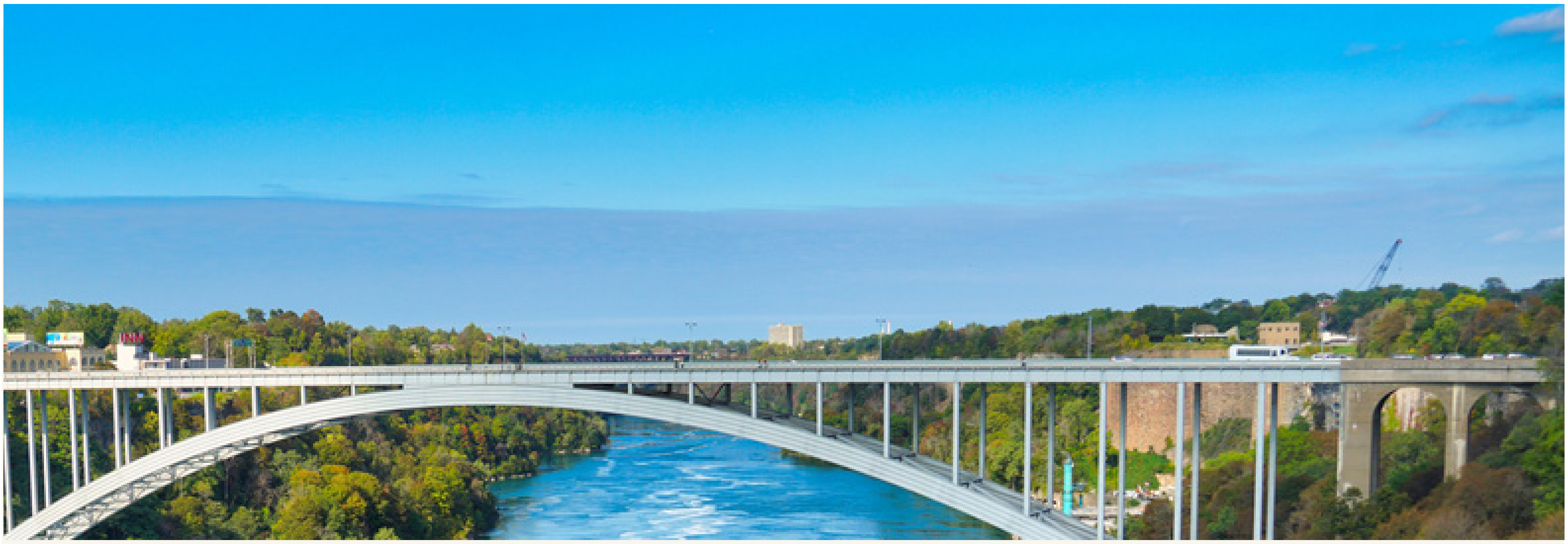
Demanding management accountability

Many participants indicated that boards need to engage more directly with management on culture, ethics, and compliance than they might on other topics. ***"For most issues, most directors look at their role as 'nose in but fingers out.' With culture, it's more fingers in,"*** one participant said. Some directors challenge executives simply by asking how values are being translated into actions. ***"We ask questions in the context of the articulated values. We ask whether people are being held accountable for them,"*** a director said. For companies where safety is a paramount concern, one way to keep executives and directors aligned and consistently mindful of these compliance priorities is to reinforce safety in board meetings, just as is done in meetings throughout those companies.

Of course, while reinforcement in the boardroom is important to directors, the primary test is whether the rest of the company hears and embraces the message. ***"It isn't so much the statement on the boardroom wall that shows your values and purpose; it's whether those things are being translated into action throughout the company,"*** one participant said. ***"The further you get from the head office, the truer the test of whether values and purpose really are permeating the organization. If you can transmit them effectively from a company office in New York City to a company location in Prague, that's a pretty darn good measure."***

Directors' responses when ethical or compliance issues emerge send an important signal about how seriously the board takes these issues. One audit committee chair recalled an occasion when ***"there was sloppy compliance behavior in a business unit. So, we called the business head to come to the audit committee to discuss it. I said, 'You've got five directors here, so it's a big deal.' Everyone got the message."***

Several directors emphasized that equal organizational justice—holding all employees accountable regardless of their rank or financial performance—is essential. Indeed, senior executives, because of their visibility and influence, are held to higher standards on some matters than rank-and-file employees. Disciplinary action against senior leaders and "superstars" sends a clear message to the rest of the organization that regardless of who commits malfeasance, there are consequences. Directors say that some of the most challenging episodes of their board careers have come when they needed to discipline



or terminate a high-performing CEO or other senior leader. ***"We had to terminate a senior leader who had circumvented a capital allocation rule,"*** a participant recalled. ***"This person had been at the company for a long time, and was about a month from retirement, so it felt very cruel, but we had to be clear that that you can't do that at this company."***

Participants emphasized that accountability for compliance and ethics belongs to business line leaders as much as to the compliance function, and that business-led accountability must begin in, and be reinforced from, the C-suite. ***"The executive team has to take the lead, not the CECO or general counsel,"*** a director said. When executives demonstrate compliance leadership and communicate that compliance is a priority, it makes the compliance function an ally, rather than an unwelcome internal police force. This can counteract the unfortunate reality that, as one director said, ***"the compliance function is often viewed as the skunk at a garden party."***

> *"There are some things that are just your job, and you should be doing it. Either you're safe, or you're not."*

Tying compliance metrics to performance and compensation

While directors agree that holding management accountable is essential, they differ on the extent to which ethics, compliance, and culture can be integrated into executive performance goals and compensation plans. Some aspects are relatively easy to incorporate in compensation, and many compensation plans have begun to do so. ***"The compensation committee and its compensation consultants consider safety in executive compensation,"*** one director reported. Others noted that progress on diversity and inclusion goals are increasingly being integrated into executive compensation. Another participant explained how compensation programs can be tailored for employees below the C-suite in order to reinforce compliance cultures: ***"We have compliance ambassadors around the world. Some come from the compliance function, while others simply have interest in compliance. The company rewards them with stock options because those people are conduits for good behavior in the field."*** Adding penalties for failures in compliance, safety, or related areas to pay plans signals to executives that the board is committed. ***"Clawback provisions in executive compensation prevent 'getting there' the wrong way,"*** a director said.

Some directors expressed reservations about ethics and compliance metrics entering the compensation calculus. The complex current state of executive compensation plans is one deterrent. ***"Executive compensation is already too complicated. They're starting to slice the pie too thin. Nobody knows what's really important. You need accountability, but maybe it shouldn't be driven by your bonus,"*** one director said. Some directors expressed discomfort with the idea of incentivizing executives to promote doing the right thing, holding that the obligation is non-negotiable. One participant said, ***"I'd never tie compensation to safety. If an additional person gets hurt, you'll be docked 2% of your executive compensation? I don't promote that arrangement. There are some things that are just your job, and you should be doing it. Either you're safe, or you're not."***

Beyond ethics and compliance, measuring culture performance and incorporating culture metrics into compensation is a less precise process, one about which participants had varying opinions. However, they acknowledged that it is coming. ***"Culture-related compensation is getting traction. It's going to be more and more common, like it or not. Investors are going to demand it. It's already built into compensation programs to some degree, but the trend will continue,"*** a director said.

> ***"If you want a compliance culture but don't work with middle management, you won't get anywhere."***

Empowering the middle

Many participants said that, while accountability originates with senior leadership, it must permeate the organization. ***"If you want a compliance culture but don't work with middle management, you won't get anywhere. You need buy-in there,"*** a director insisted. Directors noted that specialized ethics and compliance training is critical to ensure that managers grasp their responsibilities for ethics, that they understand the financial benefits of an ethical culture, and that they know how to properly handle employee concerns and avoid any type of retaliation or perceptions of retaliation for raising concerns.

It is perhaps inevitable that business imperatives and customary practices might lead to isolated incidents of bad behavior, but a consistent lack of accountability lets those behaviors multiply and persist. If senior leaders promote a company's values and principles but do little to bring them to life and enforce them, the desired culture will not emerge. Directors emphasized the importance of not only punishing misconduct, but also calling out and rewarding, in formal or informal ways, employee examples of positive conduct or prioritizing safety or ethics. ***"We've started to celebrate the occasions on which someone at the operating-line level stopped work because something didn't look right. Word gets around that somebody was praised and rewarded for stopping work instead of getting the 'What the hell are you doing!' speech. That kind of validation and verification is irreplaceable,"*** a director said.

Participants said that companies need to clearly communicate the outcomes of disciplinary processes and responses to hotline calls throughout the organization for them to achieve their full impact. Many directors expect reporting on the entirety of these processes, from report to resolution and internal communication. ***"A compliance issue has a lifecycle with a beginning, an end, and many steps between. I want to see that lifecycle,"*** a participant said.

02 | Oversight of culture

Oversight is a critical, never-ending task for every board. Some companies have more than a million employees and fewer than a dozen directors.

> Success can foster complacency.

Overseeing culture, ethics, and compliance requires significant board time and effort, but directors struggle to find room in already crowded agendas. Directors are eager to refine their oversight practices to address this challenge. Board composition and board culture are important considerations. An important step is to identify the right committee(s) to focus on culture.

Creating time and space for culture

There is increasing pressure on boards to devote more attention to corporate culture. In recent years, high-profile crises related to poor company cultures and the resulting ethics and compliance failures have contributed to this. ***"The role of the board in culture has grown. Each director has to take on additional responsibility,"*** a participant noted. Another said, ***"It's now part of the director's job to ask questions about culture. Most boards are in early stages of managing this responsibility."*** And one director noted that ***"many boards didn't focus on culture even 10 years ago. Now, we talk about it at every board meeting. But we're still a long way away from being perfect in this regard."***

Despite heightened commitment and attention, oversight of culture remains difficult. Boards continue to explore the best ways of handling the nebulous characteristics of corporate culture. A director noted that culture used to be more closely tied to a company's philanthropic efforts than to its core purpose and performance. Today, boards are finding ways to tackle this culture as a strategic priority. One director said, ***"Culture oversight is less about positioning the board for culture than positioning culture for the board. Culture is soft and loose. Directors gravitate to hard, measurable things with clear metrics. Even having the culture conversation on the board can be difficult; language around culture gets in the way."*** The director went on to explain that ***"pulling in the intangible cues about culture together into a comprehensive view of what culture really is would help boards with the absolute mandate of overseeing this critical part of the organization and understanding its impact on the bottom line."***

Participants emphasized that regular board attention to culture and related compliance issues is critical to understanding a company's health. One director said, ***"If you are not looking at these things a couple***

times a year, you may miss the clues." Many directors view culture as a full-board issue that should be discussed at every meeting. For some boards, culture is a distinct agenda item; more often, it is woven into other discussions. ***"Everybody owns culture on the board. There should be a little bit of culture in every board presentation,"*** a participant said. Another director noted that ***"there are benefits to having multiple avenues at every meeting to be informed about anything that caught somebody's attention or has awoken somebody's 'spidey sense.'"***

Several directors reported that the COVID-19 pandemic has heightened board awareness of culture. Remote working environments, virtual interactions, and quick adoption of technologies to facilitate ongoing business have all disrupted company cultures and raised concerns over compliance risk. ***"Over the last year, the board has been digging deeper and feeling more personally responsible than ever. The pandemic was probably the best thing that happened to our employee base. The company is held to a code of conduct that is far stricter than it used to be,"*** a participant said. Although commitment to culture, ethics, and compliance among directors is universal, several participants warned that success can foster complacency and urged boards to remain vigilant, even when company culture and compliance efforts appear to be working well. A director said, ***"It's human nature to pull back the microscope when things are going well, but that's actually a time you need to ask the hard questions."***

> ***"Culture oversight is less about positioning the board for culture than positioning culture for the board."***

However the board chooses to approach culture, creating time and space to address it is fundamental. As with many pressing oversight topics, managing agendas and limited meeting time is a challenge. Recurring agenda items like financial condition and performance, and emerging issues like cyberattacks or the COVID-19 pandemic already occupy limited board and committee time. Creating space for additional oversight priorities could invite deprioritizing other important issues—something directors are reluctant to do. Tightening meeting agendas and meeting materials is one way to handle the additional burden. One director said, ***"We all could do a better job of running meetings."*** Although mounting director workloads and crowded, overlapping committee agendas can make time feel short, participants saw no excuse for the board to deprioritize compliance and culture. ***"I do not buy all this crowded agenda stuff,"*** a director said. That sort of mentality, the director continued, can arise from an understandable impulse to ***"check all the boxes that the regulators make us cover."*** Those things are necessary, but ***"there is nothing more important than what we're talking about. You've got to find a way for the board to engage with management on strategy and on culture."*** Allowing ample time for follow-up questions and additional discussions with management or among directors without management present is critical. One director said, ***"We just need to spend more time in the boardroom in Q&A and discussion, and less time in presentation. My biggest complaint, as a board member, is the proportion of presentation material to the proportion of discussion time."***

Clarifying committee responsibility

Traditional committee structures may not be suitable for handling increasing demands for board oversight of culture, ethics, and compliance. Participants emphasized that, whatever the committee structure, there needs to be a "home" for ethics and compliance issues so they get the priority and focus they need. Audit committees, which have been called the "kitchen drawer" of the board because they take on a wide range of risk and oversight tasks, are often the first destination for management's ethics and compliance reporting. Given the hefty demands that boards already place on audit committees, this practice may not sufficiently cover the topic. A director said, ***"I'm skeptical that, in heavily regulated industries, compliance issues can be handled on the audit committee."*** Another participant noted that ***"it's hard to make up for a bad culture on the audit committee. If you have a cultural issue, it affects every committee."***

"I'm skeptical that, in heavily regulated industries, compliance issues can be handled on the audit committee."

Management reports on culture, ethics, and compliance can reach the board in different committees or on the full board, leaving oversight balkanized. Risk, nomination and governance, and human resources committees contribute to culture oversight in many companies. Human resources and compensation committees look at "people issues" from employee surveys, exit interviews, and employee wellness data. One participant's human resources committee charter listed culture oversight as one of its responsibilities. Nomination and governance committees often play an umbrella function when culture and compliance issues land on more than one committee agenda. A participant described how one board structures committee coverage of compliance and works with management on issues that emerge: ***"The nomination and governance committee covers standards of business conduct and policies, but the audit committee oversees the compliance function and examines compliance with policies. If there is something notable, it gets escalated to senior management and maybe even to the full board."*** While careful coordination

across committees can be an effective way to ensure coverage, fragmented oversight can make it difficult for the board and for individual directors to get an overall sense of how the company's ethics and compliance functions are performing.

One way to promote coverage and thoroughness is to create a compliance committee or equivalent, but directors have differing views on the wisdom of such an approach. A dedicated compliance committee can empower the CECO to raise issues with the board: ***"It does make a huge difference in terms of the Chief Compliance Officer's role. She knows that if she's got an issue, she's got a place to land and she's going to get the time she needs to get the issue addressed."*** Boards of companies in financial services, biotechnology, energy, and other highly regulated industries often have compliance committees in order to provide due attention to regulatory burdens. Companies with significant employee safety concerns often have compliance committees as well.

For boards without compliance committees, organizing committee oversight of ethics and compliance is a challenge because subtopics can be difficult to separate neatly. But some participants were reluctant to endorse compliance committees because, as one said, ***"there's a logistical problem to adding committees."*** Directors are wary of adding complexity and disrupting stable inter-committee collaborations. Creating a new committee often means redefining other committee roles and disrupting how the full board approaches issues. Adding a committee frequently also adds more meetings, preparatory work, and follow-up tasks.

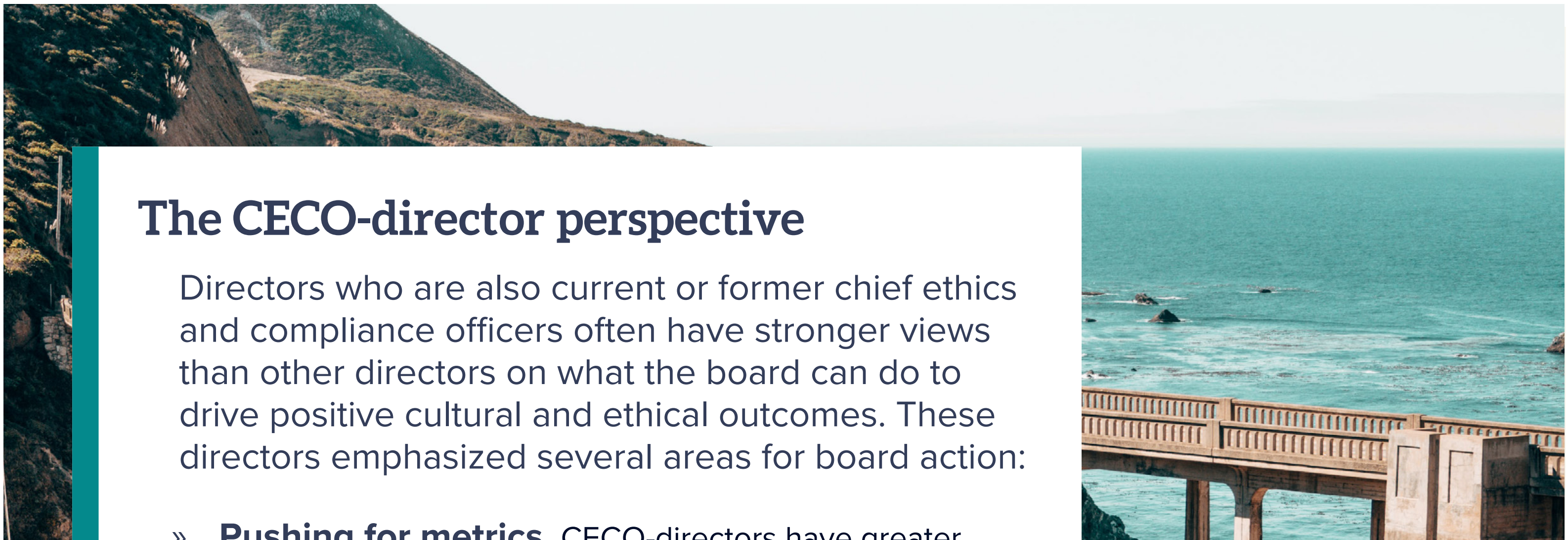
Capitalizing on compliance expertise

Many participants noted the contributions that directors who themselves are or were CECOs have made to compliance oversight. These directors pointed out ways they were able to bring their experience to bear in their board service. ***"You bring current credibility on the subject to the board, which helps make clear to the CEO that ethics and compliance are priorities,"*** a participant said. Another director said, ***"The board should have some compliance expertise to help senior management ensure that they're looking at the right things and managing them properly."*** Several participants with experience in highly regulated industries agreed. ***"In companies where compliance burdens are especially high, compliance experience and perspective on a compliance-related committee is important,"*** a participant said.

The structure and state of the company's compliance function can influence the emphasis that boards place on directors' compliance expertise. One participant said that a director's compliance experience can be helpful when a company is building a centralized compliance function. But leveraging that expertise to manage compliance from the board is not the goal. ***"I don't think that it's an appropriate board role to get a compliance expert on the board and expect that person to run the compliance function or be deeply involved in it,"*** a director said. ***"You want the board to be conversant in that area,"*** the director added. ***"There is a balance to be struck."***

A need for balance applies to compliance committee makeup. Few participants insist that all compliance committee members have executive compliance experience. ***"I wouldn't want a compliance committee filled with compliance framework people,"*** one participant said. The decision about who should sit on the compliance committee is case by case, however. ***"Having a legal background gives you something interesting to add, but I would say that having experience running a business can give you more of an instinct to see trends,"*** a participant said. Other directors agreed, preferring to have well-rounded directors, particularly those with general management experience, on the board. One said, ***"Directors who haven't been in the C-suite don't always know the practicalities of management's issues."*** Another said, ***"We want somebody who can contribute broadly to all areas. Focusing on a small amount of specific experience in a candidate is a wasted board slot."***

Whether or not a compliance expert is on the board, there can be value in having a board or committee member champion ethics and compliance and put significant time into its oversight. A director in this role can relieve some of the pressure on committee chairs for compliance oversight, especially where the audit committee has primary responsibility. An audit committee chair recalled delegating compliance oversight items to a director with a "first-rate legal background" who had much more experience in compliance issues. ***"It was just more logical to delegate to that person,"*** the director said. Another reported occupying such a role, if unexpectedly: ***"They brought me to the board for my financial expertise, but my value-add is in the area of culture."*** Participants emphasized, however, that all directors on the board—individually and collectively—need to focus on culture, ethics, and compliance; the responsibility cannot be given to a single individual.



The CECO-director perspective

Directors who are also current or former chief ethics and compliance officers often have stronger views than other directors on what the board can do to drive positive cultural and ethical outcomes. These directors emphasized several areas for board action:

- **Pushing for metrics.** CECO-directors have greater confidence in the measurability of culture; they encourage their fellow directors to push management teams for more and better data. ***"The board can and should have deliberate discussions about culture, grounded in data. The data frames the discussions about things like speak-up culture and safety."***
- **Linking culture to compensation.** Boards can incentivize positive cultural and ethical outcomes by incorporating them into concrete performance objectives linked to compensation. ***"I absolutely believe that the top of the house should have some portion of their compensation tied to ethics and compliance. Senior leaders should set annual compliance objectives. You have to measure people, hold them accountable, and integrate that into the human resources process."***
- **Defining the culture strategy.** Boards should expect management to be very explicit about the culture they are aiming for, and the implementation path. ***"Well-run companies do have a culture strategy. The external world expects it. Responsible directors recognize that."***
- **Creating board focus.** For CECO-directors, ethics, compliance, and culture should be given a home at the board, generally by creating a distinct committee. ***"Having a committee that is compliance or compliance 'and something else' is a good practice because it forces the creation of a committee charter where the legal and compliance team says what should bubble up to the committee and the board."***

> ***"Well-run companies do have a culture strategy. Responsible directors recognize that."***

A healthy culture starts in the boardroom

Healthy board culture is important in providing compliance and culture oversight. The sensitivity and complexity of culture and compliance issues, and the novel challenges they present, call for good working relationships among directors as they examine complex issues. Directors who connect informally, often one-on-one, are able to develop these connections with their peers over time: ***"Relationships among directors are a big part of what makes boards effective. You develop those relationships by having meals together and having informal conversations—these basic things help directors to bond,"*** a participant said. These bonds help directors engage with each other freely and openly: ***"A good test of your relationship on the board—and often it comes from a long-term relationship—is that others open up to you about ideas and concerns because they know that you care,"*** a director said.

Many participants emphasized that a mix of views and backgrounds on the board is essential to oversight of ethics and culture. A director said, ***"Diversity of perspectives and experiences helps thought processes and stimulates directors to ask the right questions."*** Diverse perspectives also prevent boards from becoming too comfortable with their own approaches. One participant said, ***"Certain crises or difficult situations could have been circumvented or identified sooner without 'groupthink.'"*** Many participants said that their executive experiences, and the varying experiences of their fellow directors, provide their boards with useful insights about what good culture reporting to the board looks like and how board oversight can be improved. For similar reasons, experiences on one board can be useful on another.

Refreshing a board is a common way to obtain diversity of perspectives, but doing so can erode valuable institutional knowledge and break bonds among directors. Participants noted that long tenure helps a director develop a "nose" or a "feel" for issues that come before the board; that acute alertness can be critical to a director's ability to challenge management. Echoing other participants, a director said, ***"You have to be nosy and ask the right questions."*** Several participants indicated that refreshment at the expense of board culture is not always worthwhile. ***"You lose the important connections among directors when boards refresh too frequently. You only really start building those bonds in years three, four, and five,"*** a director said. Changing directors' committee assignments offers a compromise: ***"Moving directors around within the board prevents directors from 'homesteading' and getting locked into habits."***

03 | The challenge of "reading" a culture

Cultural problems are often the result of long-running trends, gradual changes, or the interaction of complex factors, making them difficult to identify. Even when directors have access to ample data about culture, ethics, and compliance, it can be difficult to identify emerging problems and find narratives to guide action.

"It is very easy to know only what you are told."

A major task in exercising oversight of corporate culture is to incorporate information from a wide array of sources into decision making. Culture and ethics represents a particularly acute manifestation of what one director called ***"the classic problem of asymmetrical communication between boards and management."*** Boards are insulated from the organizations they oversee and depend on management for information. Many directors emphasize that culture is inherently resistant to measurement and that quantitative data, while essential, is of limited usefulness in assessing it. As a result, directors commonly turn to qualitative, informal means of seeking information in an effort to gain a more direct feel for the culture.

The management filter

Boards necessarily stand apart from the companies they oversee. Many directors fear that the pictures they are receiving from management reporting are filtered, incomplete, or inaccurate. One said, ***"The biggest challenge is, how do you get a handle on culture? Clearly you rely on management to do that."*** Another director noted, ***"It is very easy to know only what you are told. You are relying on the transparency and integrity of the organization to get you data that's accurate."*** Senior leaders can be reluctant to be candid with directors. ***"Very few people are direct with the board, either because of our lofty position or because they're scared that it might reflect badly on them,"*** a director said. ***"As a result, the messages that you're sent are often subtle and nuanced. It's in the way they answer questions, as much as the answer itself***."

Large organizations make this especially difficult, given that the board's view is refracted through senior management, who themselves might have limited visibility into the broader culture of the organization. ***"Oftentimes what people at the senior level say about culture isn't the way people in the field feel about it, particularly in an organization like ours where we have stores all over the country and people who are fairly far removed from the corporate culture that exists in the corporate offices,"*** one participant noted.

In exercising their oversight responsibilities, directors adopt a degree of healthy skepticism toward management reporting. ***"Part of board responsibility is to make sure mechanisms are in place to measure things like ethics and culture. Management will jealously guard that; they put their best foot forward for the board. That is not to suggest management is trying to hide the true culture, but the board needs to strike a balance between not sticking its nose in and taking care of its responsibilities,"*** one director said. Another director agreed: ***"There are better or worse ways around a board's dependence on management, but the majority of the information you get is going to be packaged and given to you through management. You can either take that at face value, or you can take it with some degree of cynicism and suspicion to try to dig deeper for the things that they're not telling you. I've seen boards do both, and I think a board is always better off doing the latter rather than the former."***

Directors agree on the need to ask questions, probe, and dig into the information management presents to them. ***"It's not about just identifying issues; it's about finding root causes. That's never-ending. It has to be continuous."*** Directors emphasized the need to push management to go beyond their core presentations and dig deep into the issues. Boards must build into their agendas the necessary time to do this, and they must create board structures that allow it.

Finding the culture narrative

There is no lack of quantitative data that directors receive to get a handle on ethics compliance and culture. The following sources are widely utilized:

» **Direct measures of employee sentiment.** Boards regularly receive and review employee engagement surveys, including annual surveys, pulse surveys, employee net promoter scores, results of exit interviews, and surveys from third-party sources such as Glassdoor.

» **Human resources data.** Participants identified a range of useful human capital metrics, including talent strategies; hiring and promotion (particularly data on diversity, equity, and inclusion); employee turnover, retention, and termination; and absenteeism and productivity. Some directors also noted the value of examining compensation programs to assess whether they might be unintentionally fostering unethical behavior.

» **Ethics and compliance data.** Boards look to a standard range of ethics and compliance data sources, including hotlines, helplines, and other anonymous reporting tools. One director described "exhaustive confidential reporting mechanisms on harassment, policy violations, and how training is preventing bad behavior" as particularly useful. Directors noted that both the number of reports or calls and the content of those reports are important measures of the ethical culture of the company.

» **Measures of customer sentiment.** For businesses with more client or customer-facing businesses, measures of customer satisfaction, positive customer experiences, and customer net promotor scores provide boards with indications of the health of the culture.

Separating signal from noise

The availability of data is one thing; deriving meaningful insights from data is another. Many directors cited the challenge of identifying patterns or trends that might indicate widespread ethical or compliance issues or a simmering culture crisis. One participant said, ***"We have data, but how do you get the intelligence out of the data? How do you look at the trends that might indicate that there's an issue?"*** Another director agreed: ***"Boards do not lack for data. We lack narrative and interpretation of what the data may be showing. We need more opportunities to discuss and explore with management what they see in the data."***

> ***"Boards do not lack for data. We lack narrative and interpretation of what the data may be showing."***

While there is a great deal of commonality in the types of data boards receive, its quality and presentation can vary, and some boards and management teams make better use of it than others. One director said, ***"Hotline information is critical, but how you use it, parse it, and dissect it makes a lot of difference."*** Interviewees noted attributes that make data more or less valuable. One director said, ***"In my view, trends are important. Point-in-time data is useful, but how it's changing over time is more helpful."*** Similarly, data that is broken down by geography or business unit is more useful that highly aggregated data. One director said, ***"Comparisons between locations are more helpful. If hotline calls are remaining constant overall and you don't go further you may not know there was a spike in one place and a drop in another and that's why the data appears to be constant."***

While employee surveys are commonplace, not all surveys provide the same quality of information. One director said, ***"Some surveys give you information about moral and ethical issues, such as having trust in management to do the right thing, or trust in supervisors to do the right thing."*** Another participant noted approvingly that one company's employee survey asks whether employees feel respected and valued, if they feel safe raising concerns, if expectations about ethical behavior are clear, and whether leaders model the values and priorities of the organization. Frequency is also important: ***"Annual surveys aren't enough. Monthly pulse checks give a continuous feedback loop."***

Mapping the connections between hotline or survey data and other developments in the organization can generate additional insights. ***"I don't think a survey in a vacuum can tell you much, but over time it can show trend lines. They might show a dip in morale when the business is under pressure. On the other hand, when things are going well, there's a kind of 'grade inflation' going on, so it's important to assess survey data in the context of what is happening in the business,"*** one director said. Combining different sources of employee data around speaking up can show otherwise hidden signals: ***"Hotline trends correlated to ethics survey data and exit surveys can be good indicators,"*** a participant said.

"There are barometers you can read and statistics you can see, but I'm not sure you can measure culture without feeling it."

The limits of data

Almost all interviewees emphasized that even the best data is inherently limited in its ability to inform boards on ethics and compliance—and especially on culture. One director asked, ***"What ARE the measures of good culture? Are there objective metrics? What are the targets?"***

Most directors, even those who cited the strength of the reporting they receive, simply lack confidence in the ability of data alone to deliver an accurate picture of corporate culture. One said, ***"I don't think you can measure culture mathematically. There are barometers you can read and statistics you can see, but I'm not sure you can measure culture without feeling it."*** Another director said, ***"Data has value but there's only so much insight it can give you; it can be manipulated, and it's often rear-view-mirror data."***

Surveys and hotlines provide limited insights. One director noted that ***"often what you get in terms of an employee survey readout is categories and comparisons—say one group versus another within the company, or you may get a comparison of this year versus last year, or you may get a comparison to other companies. But that's not a lot of information and it doesn't have much in the way of subtleties. So, it's a tool, but it's a blunt tool."*** Data without context can also be ambiguous in its interpretation. One director pointed to ***"the relationship between other information and hotline data. Suppose you have a spike in hotline calls where you have a new manager but the board doesn't know that. You're just looking at the data, and an important piece of context is missing. The hotline is a baseline, but how it's supplemented and analyzed is also critical."***

Experiencing culture

In response to concerns about filtered information and the limits of quantitative data, most directors we interviewed cited the need for direct, unmediated contact with wide swaths of the organization. ***"Culture is harder—you know it when you see it,"*** said one director. ***"You can use surveys but they're not as helpful as actually knowing people."***

Achieving direct insight into the organization's culture requires getting managers across the organization—down to the level of plant supervisors or store managers in some cases—in front of the board and getting board members out to see and experience the organization and its culture firsthand. This allows them to develop a more intuitive "feel" for the culture. As one director said, ***"Directors can feel isolated, circumscribed by the senior figures they engage with. Directors need to step outside and talk to people. I encourage boards to institutionalize that to understand the culture. Getting out into the field is so important because boards can be walled off, and that's not healthy."***

Assessing tone at the top

Directors' search for qualitative indicators of the state of a company's culture begins with their interactions with the CEO and other senior leaders. Participants emphasized the importance of tone at the top as a key indicator and driver of corporate culture. ***"There is nothing more important than the tone at the top, and you can see that really well in the position that the CEO, the CFO, and the senior executives take during boardroom discussions, especially how they are willing to make tradeoffs on difficult issues,"*** one director said.

Even the culture at the very top of the organization can be opaque to directors, despite their best efforts. One director said, ***"Problems can be part of the senior team. You may not see it because people are on their best behavior for the board."*** Another director recalled a situation where the board had to replace the CEO due to an ethical crisis. The process of choosing a successor ***"revealed a terrible working relationship between the CEO and the senior team. They disliked each other immensely. And no one on the board picked up on it. With all of our tentacles into the company, with all of those conversations, it was completely non-transparent to us, and we were shocked at the situation we found out. How could that be unknown to 12 people on the board?"***

Developing a culture barometer

In describing their oversight of corporate culture, directors often use metaphors of sensing—having a nose for the culture or keeping an ear to the ground. Some even alluded to a kind of sixth sense:

"Things that make the hairs on the back of your neck stand up shouldn't be dismissed." Interviewees repeatedly cited the need to get a feel for corporate culture through personal observations and interactions with individuals throughout the organization. ***"We need a more direct pipeline to the workforce and decision makers in the field. As a director, you need to have your ear to the ground. It's not just being a director for a long time or having the right network. You need to have a barometer."***

Another director stressed the need to ***"interact with broader levels of the company, to create opportunities for less formal encounters with people within the organization. The ability of the board to interact is crucial—I am a big fan of boards visiting sites. Over time, as boards have trips to different sites and see interactions, you can develop a reasonably accurate sense of what is going on. Absent that, you're looking at the front of the curtain."***

A participant explained an approach to site visits: ***"I spend a day at company locations, including the ones abroad. I get a tour, interact with a couple people, and have dinner with the CFO or president of that location."*** Another said, ***"Wherever I would go, I made it a point to stop in our stores. They didn't know I was I'm coming. I walked in as a customer. That was the best barometer that I think I had."***

Balancing data and experience

A few directors, primarily those with significant professional experience leading ethics and compliance, expressed a different view. They insisted that quantitative data can provide more meaningful insights than many directors recognize. ***"Data-driven ethics programs work,"*** said one such director. Another said, ***"The type and value of the data available to measure culture is increasing every day."***

It rests with the board to press management for better data on culture. One director said, ***"I think it's incumbent upon the board to set its expectations for the kind of information it gets. They need to ask, for example, 'Can I see the data on diversity, equity, inclusion? Can I see the data on promotions over the last three years, broken out by gender and ethnicity?'"*** Boards should stay abreast of evolving practices to understand what new insights data can deliver. A participant put it this way: ***"Board members have a responsibility to keep up with best practices in culture oversight and emerging trends in programs that drive ethical culture and effective ways to measure the culture. Boards need to push for the right data."***

"The type and value of the data available to measure culture is increasing every day."

New methods and technologies can maximize insights. One director predicted that ***"deeper insight from technology is coming. Data analytics in this area is still pretty pedestrian. Companies are using it with marketing and product quality, and it's only a matter of time before they do it with their people."*** One director suggested that day has already arrived: ***"New and improved measurement tools are being developed every day. Many companies now have data analysts and psychologists on the compliance team."***

Just as a few directors have more confidence in data than most, a minority expressed skepticism about the value of information gleaned from personal interactions, site visits, and the like. One director said, ***"You need the data to indirectly reveal things. You won't get anything from site visits anyway."*** Even some participants who advocated visiting facilities observed that announced site visits often feature polished presentations and people on their best behavior.

> ***"Boards need to push for the right data."***

Another director suggested that board members' efforts to gain direct access to the company's culture could cross the line between the board's role and management. ***"I don't encourage board meddling, to the extent of trying to assess what's going on inside the company by going out into the field or directly engaging the workforce,"*** a director said. ***"When it is possible, you need to assess whether you're making progress or not by looking at things like turnover, absenteeism, health claims, and the like."***

Views like these are clearly in the minority among directors, however. To inform themselves about the ethics and culture of their companies, most rely on a combination of quantitative data, probing management for deeper insights, and qualitative information drawn from direct interactions and observations.

04 | Cultivating trust

If organizations are to maintain the trust of investors, policymakers, and the public at a time when public confidence in institutions is low, they must behave in a transparent, ethical, and responsible manner.

> *“Trust is everything.”*

Equally, trust within an organization is the single most important means for securing a strong, ethical culture. ***“Trust is everything,”*** said one director. Trust among directors, executives, and rank-and-file employees is something that directors take pains to engender. However, it is hard to gain, easily lost, and directors are not always confident that trust goes beyond the boardroom.

Trust fosters transparency

Participants agreed that trust between the board and senior executives is crucial to fostering transparency and ensuring that the board will hear what it needs to hear, including bad news or information about emerging trouble spots. ***“Directors need to be able to rely on executives to be transparent so the board and its committees can connect all the dots,”*** a participant said. Another director said, ***“Executives should err on the side of transparency. If I were the CEO, I would never not tell my board something. I would never want them to think that I was withholding information from them.”*** Directors also want management to reveal issues promptly. One participant explained: ***“Whatever the problem, telling the board sooner is better. If you don’t have all the answers, be clear that you’re going to go find them. Present the issue, even if it’s not complete, and bring the board along on the journey. You might get some points of view from the board that could help. It takes a lot of vulnerability from management to do that.”***

While trust can be difficult to measure, directors identified several signs that it exists—for example, top executives encouraging subordinates to communicate directly with the board, even without intervening management ranks in the conversation. ***“If somebody makes a presentation to the board and the CEO makes their contact information available to directors, that shows that the CEO trusts the board to communicate with that person without the CEO being present,”*** a participant said. Close work between board committees and executives is another indication. ***“It shows great trust when the executive team partners and collaborates with the audit committee and asks questions,”*** a director said.

Challenging management to build trust

Directors insist that board members can and should take initiative in developing trust with executives, both by building strong individual relationships with them and by fostering an open conversation in the boardroom. A participant described one approach: ***"I always made a point of getting to know the CFO when I was chairing the audit committee. We had one-on-one conversations over breakfast or in between group meetings. In doing so, I made deposits into the relationship, which I could later withdraw if a hot-button issue arose."***

> *"The board needs to show transparency, honesty, and humanity. That enhances what comes from management."*

Transparency and candor in board-management interactions are hallmarks of trust. Setting a collegial, genuine tone with management helps boards show that they are willing to extend trust—and keen to receive it in return. ***"The board needs to show transparency, honesty, and humanity. That enhances what comes from management. The board needs to start the process and hope that it has the right people in management to reciprocate,"*** a director said. How directors respond when management raises problems or delivers bad news also matters. ***"Management needs to feel free to discuss problems, and boards need to think about how they react to management. Boards have to challenge—but then not overreact,"*** a participant said.

Fostering trust throughout the organization

Trust also needs to exist at multiple levels of an organization if it is to experience good compliance and culture outcomes. While directors can personally build trust with senior executives, the board depends on management to promote trust throughout the company. A director and former CEO explained that boards have only recently begun to appreciate the importance of executives who build trust within their teams: ***"As CEO, I tried to instill a culture of trust. As a board member, I am only beginning to think about how, as someone who is not in charge, to encourage executives to do the same. Most companies are not doing this really well, and I am not sure that boards know how to change that. I think that directors are only just learning about this right now. If someone tells you he is an expert in this, he is lying."***

While trust is difficult to measure, directors can ask executives questions to learn whether employees and midlevel managers have a sense of connection and trust. ***"Questions around trust and inclusion are the most important. You want answers that reveal whether people feel comfortable,"*** a participant explained. This means asking questions such as, Do people feel included in their work groups?

Some directors take an active role in advising executives on how to build trust in the organization. ***"As board chair I routinely discussed trust with the executive team and expressed what the board's expectations were and how we felt about the impact of those things on the success of the enterprise. We graded the CEO and the rest of the management team on how well they were doing,"*** a participant reported. Engaging third-party advisors in these coaching efforts can help boards avoid creating friction between the board and management.

Giving voice to values and breaches

It takes a great deal of trust within a workforce to achieve an effective speak-up culture. While all companies encourage speaking up, almost all struggle to overcome employees' fears of retribution.

> *"I hope that employees feel comfortable reporting smoke, not just fires."*

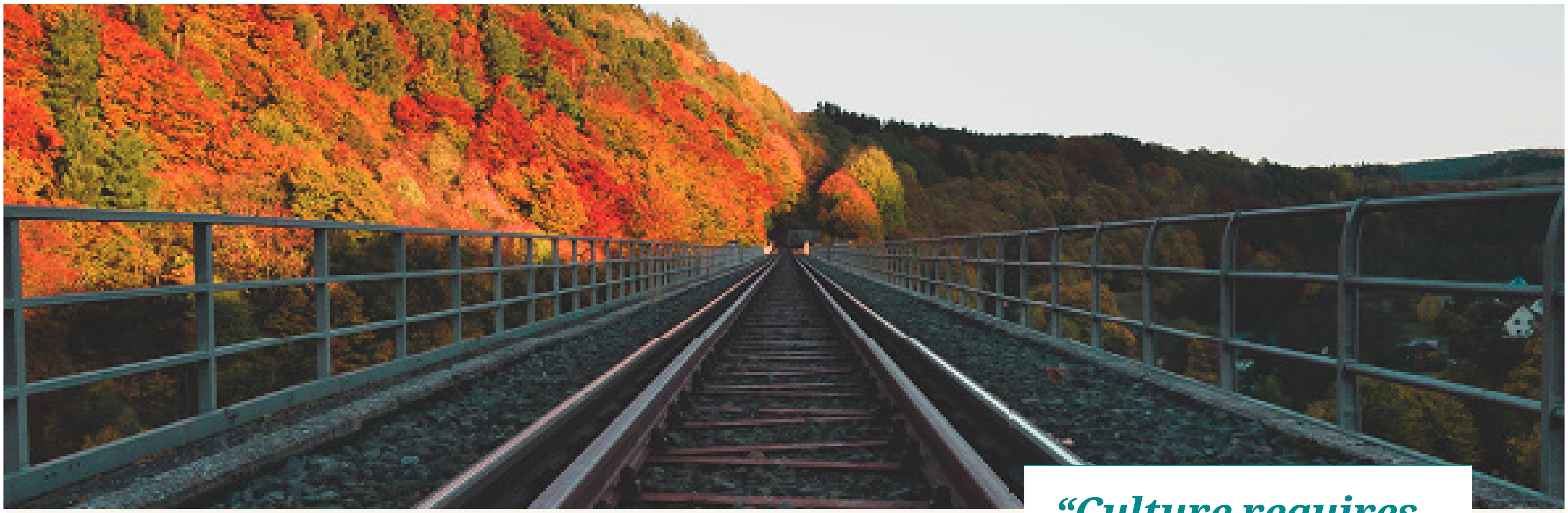
Many directors are unsure about whether their companies are achieving speak-up cultures. This is a particular concern in highly regulated and safety-oriented industries, where speaking up is both a moral imperative and a competitive necessity. The reputational and financial losses stemming from undiscovered manufacturing shortcuts can cripple a company by destroying its brand loyalty. Directors rely heavily on data from employee hotlines, surveys, and other input "from the ground" to get a sense of whether employees are readily alerting others of bad behavior. Speak-up data that goes directly to the board gives directors comfort that they are getting an unfettered view.

Many directors said that an absence of speak-up data, rather than indicating an absence of problems that merit reporting, could indicate widespread reluctance to report due to a lack of trust. ***"You might think that an uptick in speak-up calls is a problem, but it's a function of better education about the availability of channels through which to speak up, and of employees being comfortable with the anonymity and lack of retaliation. If you see a precipitous drop in speak-up calls, that indicates a problem,"*** a director said. Another director said, ***"I hope that employees feel comfortable reporting smoke, not just fires."*** A participant emphasized that employees who internally speak up prevent immediate reputational and legal harms: ***"I would rather have a lot of speak-up calls than have our employees not trust us and go outside the company to register complaints."***

When management responds quickly and powerfully to ethics and compliance issues and communicates its actions, that response reinforces speak-up culture, validates individual action, and shows employees at all levels that good behavior is expected. A participant said, ***"When individuals speak up, they want to see the organization speak up. They want to see that action is being taken and being taken consistently—not just for a particular event or for a particular person."*** Senior management needs to

take the lead in this regard. ***"I think that it starts and ends with the CEO. You need a CEO who's willing to share the bad news as well as the good,"*** a director said. One participant regretted hearing examples of ***"employees who didn't speak up because doing so was so readily dismissed by management."*** Another director said, ***"The worst thing that can happen is when an employee speaks up and we all somehow just lose it in the shuffle."***

"When individuals speak up, they want to see the organization speak up."



> ***"Culture requires intentional shaping from the board."***

THE PATH FORWARD

For corporate boards, effective oversight of corporate culture is both essential and difficult. Culture oversight, though clearly a priority for boards, is in early stages of development and board practices around it are relatively immature. Committee structures are often not fit for this purpose. Boards often sense that their companies do not have an overarching strategy to drive culture. The data directors receive, while necessary and valuable, varies in depth and quality and does not consistently deliver a satisfactory understanding of culture. As a result, boards often lack comfort that they have a genuine sense of their company's culture or that management is driving culture in a direction the board seeks.

Boards are often more hands-on in their approaches to ethics and culture than other areas of oversight and dedicate considerable time and effort to oversight. ***"Board oversight of corporate culture requires a more proactive stance from the board than we've seen in the past,"*** said one director. ***"At times it had been an area of managing by exceptions—where you hear from management only when there are problems. But it requires intentional shaping from the board."*** What directors do outside the boardroom—taking time to build relationships with senior leaders or visit facilities to observe the culture—is as important as what they do during board meetings and formal interactions with executives. Yet "intrusive oversight"—which can be a necessity in a high-risk area such as ethics and culture—may itself damage the trust between the board and the senior leadership team that is essential to create and maintain a culture of ethics and compliance.

“Culture is early in its journey on the board.”

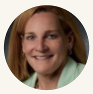
Addressing some of the following challenges can help boards chart a path forward to more effective and mature oversight.

- **Accountability and compensation.** Directors overwhelmingly want management to be accountable for culture and ethics and compliance outcomes; they do not just want to hear a report on activities. What are the best strategies in board oversight to create accountability and ensure that doing the right thing is woven into a company’s culture? As part of these strategies, to what extent can and should ethics and culture be more fully integrated into executive performance goals and compensation? What specific and concrete approaches are most effective? Is compensation an appropriate form of accountability with respect to culture?
- **Trust.** How can boards more effectively promote a culture of trust—within the board, between the board and the senior leadership team, and throughout the organization? How can boards best encourage management to measure and foster trust?
- **Assessing culture.** Companies assess their cultures in a variety of ways, and some companies measure the underlying drivers of ethical culture. Yet directors nearly universally stress the need to get a more meaningful ‘feel’ for company culture. Where are the disconnects and how can they be remedied? What are the most effective ways of measuring culture quantitatively and qualitatively and how can they be scaled? How can boards more effectively amplify weak signals in data or identify patterns that might indicate an emerging problem?
- **The role of management functions.** Directors recognize culture as a strategic imperative; yet they believe it receives insufficient attention due in part to lack of clear management ownership. To whom in management does the board look to for reporting on culture? How can human resources, compliance, and other functions best keep the board informed and provide a wholistic view? Aside from the CEO, who in management does the board expect to drive ethics and culture outcomes?
- **Board organization.** Culture, ethics, and compliance clearly need a focal point on boards to ensure they get the right priority and depth of oversight. What are effective ways to organize committee ownership of ethics, compliance, and culture to ensure these issues get necessary attention? Under what circumstances is it advisable to form a separate compliance committee?

Appendix: Contributors

The many leaders who contributed to this report spoke individually, and not as representatives of the organizations listed. Tapestry Networks wrote this report and bears final editorial responsibility for it.

This document reflects the use of a modified version of the Chatham House Rule whereby names of participants and their company affiliations are a matter of public record, but comments are not attributed to individuals or corporations. Quotations in italics are drawn directly from interviews with participants.



Virginia Addicott

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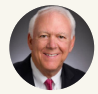

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Paulett Eberhart

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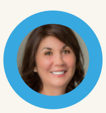

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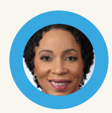

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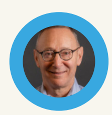
CECO

CARNIVAL CORPORATION & PLC; BankOZK



David Greenberg

CECO

International Seaways, Inc.

Ann Hackett

Capital One; Fortune Brands A home and security company

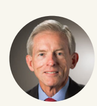
Phyllis Harris

CECO

American Red Cross

Sandra Helton

covetrus; optinose; Principal



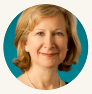
Clay Jones

JOHN DEERE; MOTOROLA SOLUTIONS

Report advisory committee member

The companies listed represent the boards the participant was sitting on at the time of their interview.

Appendix: Contributors *continued*



Julie Kane
CECO

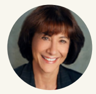
SIGA Human BioArmor

Marie Knowles

McKESSON

Mel Lagomasino

Coca-Cola
The Walt Disney Company



Cathy Lego

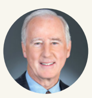
Cirrus Logic
Guidewire
IPG Photonics
Lam Research

Les Lyles

KBR

Leo Mackay
CECO

Cognizant
Ameren



John Mahoney

Bloomin' Brands
Chico's
Burlington

Mike McCarthy

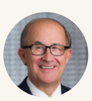
Union Pacific

Cindy Moehring
CECO

PYXUS

Henry Nasella

PVH



Chuck Noski

Wells Fargo
Booking Holdings
Hewlett Packard Enterprise

Neil Novich

Beacon
Hillenbrand
Grainger

Rick Palmore
CECO

Goodyear
Cboe

Meg Porfido

Kaiser Permanente

Report advisory committee member

The companies listed represent the boards the participant was sitting on at the time of their interview.

Appendix: Contributors *continued...*

Walt Rakowich

HOST Hotels & Resorts
Iron Mountain
Ventas

Diana Sands
CECO

PDC Energy

Gloria Santona

Aon

Vicki Sato

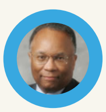
BorgWarner
Akouos
Denali Therapeutics
VIR
Bristol Myers Squibb

Melissa Stapleton Barnes
CECO

Algonquin

Kathy Sullivan

International Paper



Larry Thompson

GH Graham Holdings

David Vitale

United

Greg Weaver

verizon

Kim Williams

Scripps
Xcel Energy
Weyerhaeuser

Dona Young

Foot Locker
Aegon
USAA

Donna Zarcone

Cigna
CDW

Report advisory committee member

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About Tapestry Networks

Tapestry Networks is a privately held professional services firm dedicated to helping leaders -- directors and boards in particular – do their work more effectively

About LRN

LRN is a global firm committed to fostering principled performance and inspiring, rather than requiring, people to do the right thing.