The Effective Board

INDEPENDENT AUDIT LIMITED

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Getting comfort over corporate culture and behaviour

Boards all know that having the right culture is a core aspect of managing risk. They know that ethical and behavioural failures can result not only in financial costs but can cause a significant and lasting hit to value. But how many boards (either directly or through their committees) actually take steps to assure themselves that the standards of corporate and individual behaviour are what they think – or hope they are? It's a squishy sort of issue, but nonetheless regulators are increasingly focusing on it. An effective board will have got there first. So what should be done?

Good practices to consider...	Things to avoid...
The Board explicitly considers what the organisation is committing to publicly about its standards of ethics and behaviour. It assesses how far the business is meeting and capable of meeting these professed standards in a rigorous and honest way.	The Board doesn't fully register the nature of the statements or commitments it makes in the Annual Report or elsewhere. Or, even if it does, it doesn't think through what this means for the approaches and systems needed to underpin this behaviour and reduce the risk of very public embarrassment.
The Board emphasises the importance to risk management of embedding the ethical and behavioural standards. It understands how this is implemented and monitored as part of the risk management framework.	Assessment of the risk management framework is concentrated on standard processes and systems and fails to cover the cultural context. The Board doesn't focus on this and so fails to give a clear signal to management on its importance.
The sources of assurance over behaviour are clearly identified – whether this comes from Internal Audit, External Audit, Risk Management, Compliance… And the Board sets out what sort of (co-ordinated) reports it expects to see to give it comfort – or at least to get comfort that problems are being exposed.	Assurance reports are focused on standard processes and controls and fail to take into account the behavioural aspects when considering root causes. And they are submitted as separate reports, failing to present a behaviour-specific picture in a joined up way.
Existing indicators of behavioural issues are used effectively to provide the Board with a picture of the "state of health" of ethics and behaviour. KPIs such as staff surveys, customer and supplier feedback, training data, internal audit findings, exit interview findings, "whistleblower line" activity… are seen as a set of indicators in a combined report. Site visits by the Board are used to add to the picture.	Even if these indicators reach the Board, they're considered separately and not in an "ethics and behaviour" context. Often it does not take too much effort to pull this picture together (it doesn't have to be complete) and so an opportunity is missed. And site visits aren't used effectively to talk to operating management and staff to gauge attitudes.

From time to time the Board commissions a staff survey, specifically around their attitudes to ethics and behavioural standards, how these affect their work and how they see them in practice. This is undertaken and reported by an independent source such as internal audit.

The staff survey doesn't cover the ground around ethics and behaviour or the questions are process-based (eg did you read the Code of Conduct?) and give little insight. Even if these problems are avoided, the Board doesn't get to discuss the results (or even see them). And the degree of objective, unadulterated analysis is unclear.

The Board undertakes ethics training. It has a specific discussion around the way the "Code of Ethics/Conduct" and standards are rolled out and the training used to support them becoming embedded. It sets an example in taking the training seriously.

The Board feels that "ethics training" is only for management and staff on the basis that non-executives don't get involved in operational matters. It fails to recognise that the Board's direct commitment to underpinning standards is an important part of creating the right culture.

Where there are significant or systemic problems – significant compliance failures, legal issues or disciplinary activity – this information reaches the Board in a timely way.

Dealing with problems is seen as a management issue. But part of the Board's risk-related responsibilities is to make sure the system is effective, so the fundamental problems need to be considered for the lessons they hold…

In significant individual cases, the root cause of the problem – and the lessons learnt – are specifically discussed at the full Board. It makes sure it understands what penalties have been applied and how the rest of the organisation understands the nature of the failure and the consequences. It is particularly alert to the example that is set by the disciplinary treatment of errant senior managers.

Such cases are seen as operational issues and not reported upwards. So even when it is right that the Board should not be directly involved, it is not getting an important piece of the "behaviour jigsaw". Nor is it getting an opportunity to press management to make sure appropriate action is being taken and the right sort of example set for the organisation.

In a JV or merger/acquisition situation, the due diligence specifically looks at the approach of the partner/target to securing sound ethics and behaviour and, as far as possible, any indicators of actual standards including its compliance record. And this is explicitly considered by management and the Board. …

Looking at ethics as part of due diligence is seen as too tricky or not possible given the timelines. It's considered as something that can be sorted out later. To a degree this is true, but at least it should be on the list, and on the Board's radar, so that it's not lost sight of as part of the integration planning.

Read past issues…

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- Are we doing enough around risk?
- Succession planning: breadth, depth and transparency
- Governance reporting – getting the message over
- Better to give than to receive? Individual directors' performance review