

Assessing Corporate Culture – Part I

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Over the last two years, few topics in the field of compliance and ethics have generated more interest, and provoked more questions and concerns, than the topic of corporate culture - and rightly so. Compliance and ethics officers have every reason to be concerned about the new emphasis on culture.

To many, the term itself is like air; it's there, it's vitally important, but it's hard to describe and harder still to do much about. While it is true that corporate culture has long been recognized as having a critical impact on the effectiveness of compliance - the maxim that bad culture trumps compliance is, for example, well known – until recently few were held accountable for developing and maintaining an ethical corporate culture. That is beginning to change. But do compliance and ethics officers have the clout, resources or allies to do what must be done? What exactly are you supposed to do? What is the objective? What specific actions are required?

We will examine specific steps that compliance and ethics officers can take to assess and improve their corporate culture. In this article we present suggestions for the initial phase of assessment: creating a process to identify your current corporate culture. In Part II, we provide a step by step process for evaluating the impact your culture has on the effectiveness of your compliance and ethics initiatives.

Paul Fiorelli, in a recent article in the *Wake Forest Law Review* summarized the increasing number of regulations and guidelines that refer to ethics and corporate culture and that are now being used to hold corporations and individuals accountable. The SEC, Congress, regulators, the Sentencing Commission, the NYSE, the Department of Justice, rating agencies and others have all weighed in on the topic. For examples, consider just three recent business news headlines:

February 8, 2005 - During the sentencing phase of the government trial against Qwest executives, the U.S. Attorney, in arguing for the imposition of the legal maximum, referred to the perpetuation of a corporate culture that urged employees to do whatever was necessary to hit or exceed revenue targets.

February 11, 2005 - S&P's Rating Service downgraded Bally Total Fitness Holding Corporation's credit rating in part due to Bally's Audit Committee's finding that the former CEO and CFO created a culture of aggressive accounting.

February 17, 2005 – Charles Prince, CEO of Citigroup Inc., announced a “five-point plan” to better align ethics and reputational concerns with the existing corporate culture.

Every organization has an existing culture. For most, the good news is that their existing culture, while containing a few bad elements, is largely in good shape.. The task, therefore, is not to create or invent a new culture, but to identify what exists, assess where

improvements are needed, develop an action plan and implement. This may seem obvious and yet the temptation may be strong to skip the preliminaries and jump right into action plans and implementation. Too many organizations assume they know what their culture is and that it can be summed up in a slogan like: “we have a culture of innovation” or “we’re an action-based culture.” Others assume their values statement adequately represents their unique culture. Ideally, your values statement should be an expression of your “shared values” and as such a concise description of your corporate culture, but don’t assume that it is. Nor should you assume that your views or the views of senior management accurately describe the existing corporate culture.

Step One - Describing Your Existing Culture

It may be best to begin by setting aside your values statement and your preconceptions. You need to hear directly from employees throughout your organization. There are a variety of means to gather this input including surveys, focus groups, and formal and informal interviews. Use a variety of methods, but remember, your goal is to determine what people really think about the organization, what motivates them, what behaviors do they believe are rewarded and punished, what are the “unspoken rules” that everyone knows? For this reason, interviews and focus groups are by far the preferred method.

Your existing corporate culture is largely conveyed from one generation of employees to the next through corporate stories and the informal systems that convey values over time. You need to explore these stories and informal systems. When examining corporate stories, don’t focus exclusively on the official corporate history and folklore, though it

may be of some interest. Instead, examine the stories that currently travel on the corporate grapevine. Is there a pattern to the type of stories that survive the longest and travel the furthest? Do employees seem only too willing to believe a story about excessive executive perks, even if it's not true? Or are stories of corporate good works, generosity and social responsibility foremost on everyone's mind? Most importantly, you need to determine what lessons are drawn from these stories. If a senior executive has been fired and the speculation is that there was an ethics violation, is this interpreted as a reinforcement of "the way we do business here," or are people surprised and skeptical about what "it really means."

You may want to go beyond your current employee base. In order to gain a broader perspective consider including former employees, former compliance and ethics officers, suppliers, consumers, competitors and third parties who have been in a position to observe your organization over time. They all have stories to tell and can help you fill out the complete picture. If you choose to include third parties in your review, concentrate on the specific, first-hand stories that they tell not on their opinion of your corporate reputation. Your reputation may not accurately reflect your current culture. Instead, your reputation may be sustained by public relations and marketing or by academic case studies that no longer relate. The latter is particularly common if the case studies pertain to corporate social responsibility. Such cases have a long academic shelf life.

Another way to assess your current corporate culture is to determine what employees and others believe are the motivations behind your ethics initiatives, including this one. Do

they believe they are just attempts to “cover” the corporation, and meet compliance requirements? Or do they see them as tools that help them to achieve business objectives in an ethical way?

Surveys can be helpful. One company asked employees to respond to the claim: “I would receive more criticism for violating an ethical principle than not meeting a deadline or target”. Another asks: “It is safe to voice my opinion...true or false?” These and similar questions can provide valuable data to supplement the interviews and focus groups.

Whether you employ interviews, focus groups, surveys or all three, specific questions such as the following should be included in order to help gain insight into employee’s beliefs:

- Is the pressure to perform unreasonable?
- Is it sometimes difficult to ask questions or raise concerns?
- Is compliance, ethics or even legal issues ever denigrated or marginalized?
- Is bad conduct rewarded or tolerated?
- Is there a close tie between performance and rewards?
- Does short term thinking dominate?
- Do employees identify sufficiently with the interests of shareholders?
- Do employees understand and sufficiently care about the needs of the customers?
- Is the quality of products and/or services a high priority? Are employees proud of the products and/or services? Are they proud of the organization?

Through questions and discussion a picture will begin to emerge. But as you try to bring your corporate culture into focus, don't assume that there is just one culture. It's often not that simple. Complex organizations may have a number of subcultures. The open, innovative culture in R&D will not be the same as your more rule-bound culture in Accounting. A successful organization needs both. Also, be on the lookout for subcultures that create obstacles to effective compliance as well as those that are underutilized but may be useful for promoting and improving your efforts. As an example of the latter, you may find that some groups of employees, - in marketing and sales or in various regional locations, - are especially social. They like to gather for discussions and have a strong collegial bond. For them, this characteristic is a defining attribute of their subculture. If you ignore this and insist that this group participate individually in web-based compliance and ethics training, you may find that they reject it as "ineffective." The only training that is likely to work for this group is discussion-based, which you may be able to deliver at the same or even less cost.

The existence of subcultures creates interesting challenges for corporations. As you identify more and more subcultures you gain the ability to improve effectiveness by fine tuning the delivery of your compliance and ethics program. Not only can you improve the effectiveness of training, but you might also be able to tailor your communications or even the methods by which you allow for internal reporting. One U.S.-based, diversified holding company acknowledged at the outset that their organization encompassed a variety of cultures. Their approach was to set broad parameters and establish general goals, but then they turned to local managers and gave them the authority, resources and

incentives to create values statements, training programs and other systems that best suited their unique businesses. But at some point increased costs will outweigh the return on the investment in subculture customization. Eventually you run the risk of fragmenting the organization and losing corporate identity. Today, most err towards ignoring subcultures and rolling out “one size fits all” programs. The right balance will be unique to each organization.

When identifying your corporate cultures remember that important cues are often conveyed by customs and routines including acceptable dress, rituals and celebrations, meeting protocol – who attends and where people sit. Even the layout and furnishings of your facilities can be significant. Are executives secluded in plush offices on a separate floor with executive dining rooms and reserved parking? Is there interaction between work groups and corporate functions or do they operate in “silos”? Most importantly you must examine how these matters are interpreted by employees. Don’t ignore the little things. Even the dynamics of lunch can be illustrative. In one corporation, for example, the fact that the CEO frequently joined employees for lunch in the cafeteria was taken as evidence that he “walked the talk” when it came to the company’s espoused values of openness, respect, and fairness. In terms of impact, his lunch habits far outweighed the content of his “global web casts”.

Finally, a key element in determining your current corporate culture is to examine how decisions are made. Who carries weight? Where is the power? The centers of power will likely also play a dominant role in determining the culture.

Step Two - Assessment of Corporate Culture

Once you have a picture of your current corporate culture you will want to assess it and determine an action plan for improvements. Of course culture is very difficult to assess. How do you evaluate it? What do you measure your culture against? Benchmarking with peer organizations has some, limited value but unfortunately most organizations are in the early stages of assessing and building ethical corporate cultures. There are studies, particularly in management literature, that identify common elements of long-term, successful organizations and these can be helpful. Specific benchmarks however are not yet in place. This will undoubtedly change in the years to come as the theme of corporate culture is discussed more often at best practice conferences and in peer-to-peer exchanges.

Since measuring your culture against peer organizations may prove difficult, a better approach is to conduct a step by step diagnostic test of your culture following the elements of the “effective compliance and ethics program” contained in the U.S. Sentencing Guidelines for Organizations. As is well known, the amended guidelines now state that “to have an effective compliance and ethics program...an organization shall...promote an organizational culture that encourages ethical conduct and a commitment to compliance with the law.” The Guidelines further state that to meet this provision, an organization must, at a minimum implement the “seven steps” plus the critical requirement of on-going risk assessment.

You should precede step by step through the elements of the guidelines and at each step ask if your current culture enhances the effectiveness of your compliance efforts or does it detract from effective implementation. Some specific suggestions along these lines have been made in the preceding paragraphs. In Part II, we will provide a more detailed plan for conducting this step by step review. For now, however, consider the following additional suggestions.

When assessing the impact on culture of senior leadership including the Board and CEO, begin with the view from below. Tone at the top is of course important, but more important is how that tone resonates throughout the organization. Some CEOs believe that all that is necessary is for them to say the right thing. You need to ask “what is really being heard?” For example, a sincere, strong endorsement of compliance and ethics by the CEO may unfortunately be second guessed and over-analyzed by employees. They may try to “read between the lines” and conclude that “given the current environment he has to say those things.” In this case, instead of improving compliance the speech may only serve to further marginalize your efforts. This is especially likely if employees are receiving mixed messages: ethics is given lip service but the pay and incentive systems – including executive compensation and perks, - recent promotions, and the pressure to meet quarterly targets, all underscore the “win at any cost” culture. In short, you need to assess how the message from senior leadership is actually being received and interpreted.

Second, you also need to think of your senior management team as your organization’s most critical subculture. Is your senior leadership surrounded by subordinates who want

to please them? Are they isolated? When problems do arise, is the first response to blame others? How is bad news received? Is there a culture of fear that further stifles frank feedbacks? Is compliance and ethics respected and understood as a business asset, or is it disparaged as a necessary evil?

Under the Guidelines, hiring practices, incentives and other human resource functions must also be reviewed. These matters can have a critical impact on corporate culture. Have you developed recruiting and selection methods to screen people to ensure that new hires share your values and will help promote the type of culture you are trying to sustain? Does everyone in the recruiting process know what attributes they should be looking for? Step three of the guidelines requires that past conduct “inconsistent with an effective compliance and ethics program” be considered when hiring or promoting individuals into positions with “substantial authority”. Have you identified criteria for making this assessment? Do your performance review systems and incentive plans reinforce the desired values and culture or do they undermine them?

A step by step assessment of culture following the Sentencing Guidelines is a very useful approach but ultimately it may not be sufficient. You may wish to consider a more ambitious project. Ultimately the goal of your culture assessment should be to create and maintain a corporate culture that accomplishes far more than merely enhancing the effectiveness of your compliance and ethics program. In addition, you should work toward building a corporate culture that is understood to be all to be a strategic, business asset. It should align with your business priorities in such a way that it enhances success

while at the same time ensuring that business objectives are reached in a manner that is true to your values. Your culture should be a source of passion, pride and inspiration for your employees, investors and consumers. It should encourage moral imagination and creative decision-making. It should help build commitment and loyalty, be a positive stimulus for the growth and development of individuals and not just a means to keep them in check.

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