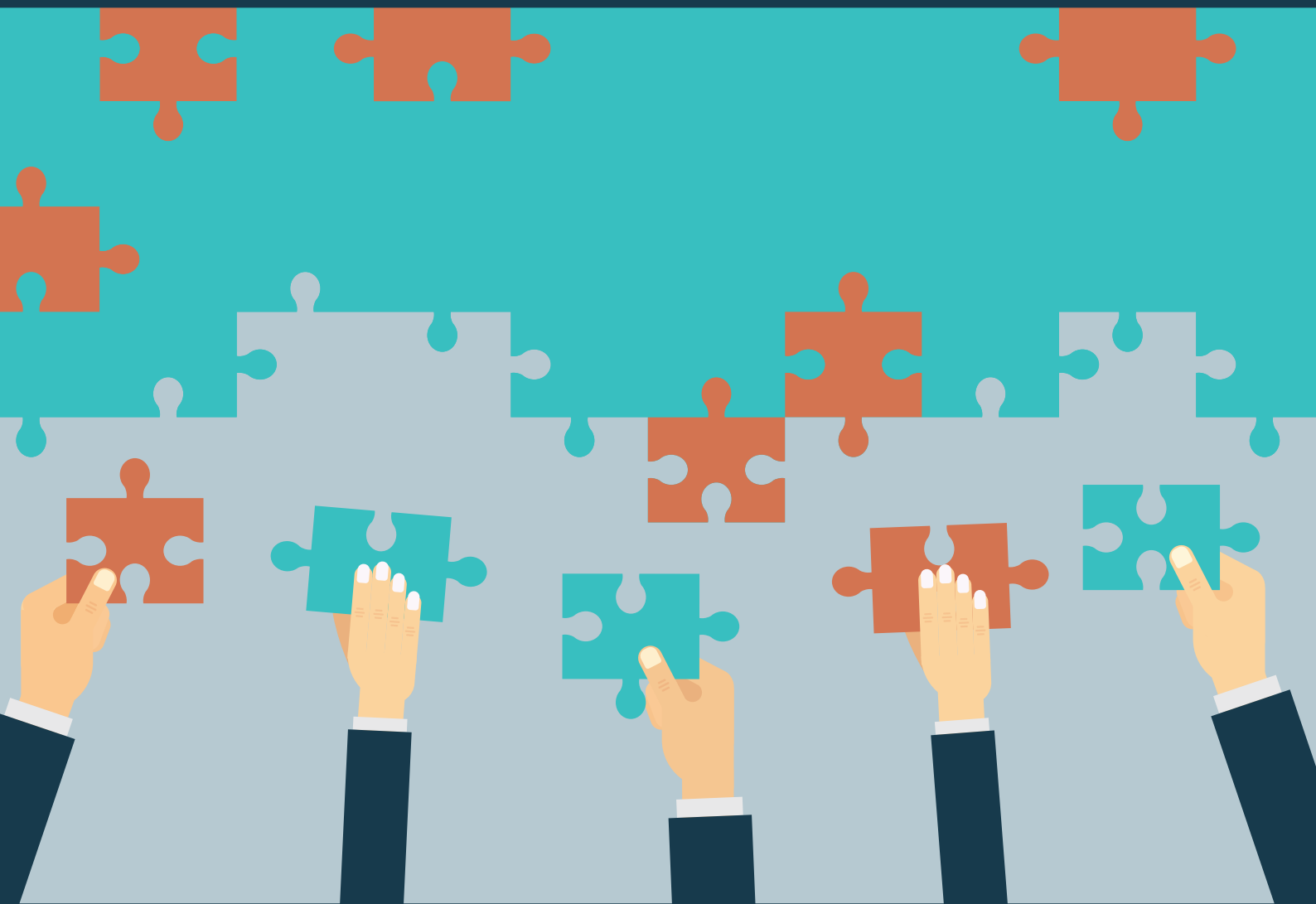


Board Leadership in Corporate Culture: European Report 2017

Research Report by Board Agenda & Mazars
in association with INSEAD



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Executive summary

AT A TIME of increasing scrutiny of corporate culture, a worryingly large gap is appearing between the good intentions of individual board directors and the broader corporate discussion and implementation of policies aimed at influencing good corporate behaviour. At the same time, a picture of misaligned culture and strategy is emerging that could seriously hamper attempts to ensure that business “does the right thing”.

While believing that the culture of business can be influenced from the top, particularly through the role of the chief executive officer, only one in five board directors believe they are spending the right amount of time addressing cultural issues. In fact, almost two-thirds of directors say that their boards either do not consider culture as part of their formal risk assessment or fail to routinely consider the risk associated with their corporate culture.

Half of these board directors say they are “reasonably clear” on the desired culture of their business, but only a fifth say that their boards fully consider the desired culture of the business. Almost one-third are not very clear or say there is no discussion at board level about the desired culture of the business.

Key findings of the Board Agenda survey include:

- Setting the right tone from the top is overwhelmingly seen as the main way that the board can influence business culture.
- Culture is ranked third by boards in terms of importance, behind strategy and financial performance.
- 40% of board members believe they either do not devote enough time to cultural issues or that culture is not valued as a discussion topic. Only one in five say they spend the right amount of time on culture.
- When they do discuss culture, the number-one focus is on understanding the actual culture of a business, closely followed by the link between strategy and culture.
- Half say their board is “reasonably clear” on the desired culture, while a third are “not very clear” or say there is no discussion. Only one-fifth “fully consider” their culture.
- A third are not confident they have the right information, and are unclear on alignment between the desired culture and that which actually exists in the business. Only 5% are very confident that there is clear alignment.
- Half say there are either significant gaps between strategy and culture, or they have not spent much time considering alignment between the two. However, the other half believe they are very clear on alignment between strategy and culture, or that their strategy is broadly consistent with their culture.
- Nearly half (43%) say the culture of the board is seldom discussed at board meetings, though a third say the board’s culture is always assessed during board evaluation.
- There is a three-way split on opinion over managing the risks associated with culture: 36% say such risks are fully embedded in their risk-management systems; 32% say that, while not part of formal management, it is discussed at board level; and 31% do not routinely consider risks associated with culture.
- Directors are inward-looking when considering their culture: two-thirds rely on employee feedback to assess existing culture. While half also consider customer feedback, an equal number look to “risk events”, such as rule breaches, for measurement; and 17% say culture is not measured at all.
- Employees are seen as major targets for cultural change programmes: enhancing employee motivation and productivity was cited as the number-one reason for a change programme.

Overall, the findings indicate that, although awareness of the importance of corporate culture to business success is recognised, boards have yet to find a way to discuss corporate culture in a meaningful way.

Forewords



David Herbinet, global head of audit, and
Anthony Carey, head of board practice in the UK, Mazars

UNDERSTANDING BOTH THE desired corporate culture and that which exists in practice is vital if a board is to provide effective leadership and direction to the business.

This is recognised by survey respondents: understanding the actual culture in the business was rated as a principal area of focus by 42% of respondents, along with monitoring the upholding of aspects of culture related to ethics—also, of course, related to the actual culture—and considering the desired culture.

Worryingly, whilst boards are aware of the need to focus on the desired and actual cultures, addressing these issues in the boardroom is still very much a work in progress.

Only a fifth of respondents felt that their boards fully consider the issue with widespread consultations in the business on it, and a further half felt that they were reasonably clear on the desired culture, having had some discussions on the matter.

This leaves just under one in three boards as not very clear on their desired culture. Similarly, a third believe that they do not have much information on the culture that actually exists.

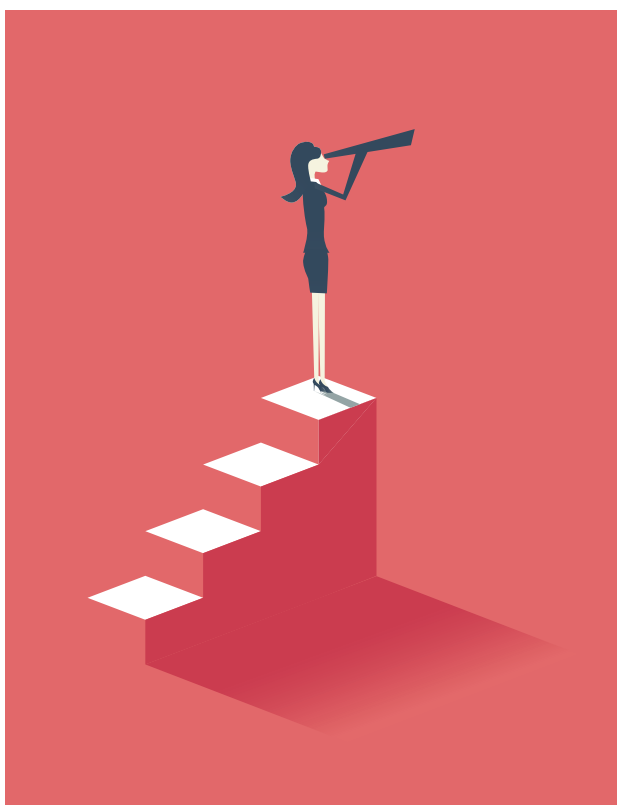
Three sources seem to predominate when assessing actual culture: far in front is feedback from employees, for example from surveys and staff dialogue, followed by customer complaints and satisfaction surveys, and risk events such as rule breaches, HR issues and compliance-monitoring.

Interestingly, far less attention seems to be paid to information emerging externally, such as social media and newspaper comment or from investor engagement; and only a quarter undertakes an internal or external audit of their culture. We would expect these are areas to be of far greater importance to boards in future.

Around 85% of the value of leading businesses take the form of intangible assets, most of which are linked to people, reputation and brand—and all of which are critically influenced by organisational culture.

Therefore, many boards need to assess whether their information on cultural issues is sufficiently comprehensive, structured and subject to independent scrutiny to meet their current and future needs.

High-quality data is essential if businesses are to achieve their full potential and enjoy sustainable success.



Erik van de Loo, professor of organisational behaviour, and
Jaap Winter, visiting professor of corporate governance, INSEAD

CULTURE IS A complex and broad phenomenon that needs to be better defined, understood and researched in the board context.

One needs to differentiate between culture in visible and invisible phenomena (artefacts, norms and values, assumptions and behaviours) and all the factors shaping and explaining culture (incentive schemes, rules and regulatory context, group dynamics, cognitive biases, individual characteristics, etc.).

Common traps when confronting culture issues are to do so either superficially (reducing its complexity) or too technically (changing culture via rules, regulations, policies). It is an illusion to think that a board can implement a chosen culture in a disciplined way.

Understanding and impacting culture is more than articulating corporate norms and values, conducting cultural surveys, or organising workshops or programmes—though one might need elements of those.

A misunderstood area is the impact of incentive schemes on behaviour and culture, both at board level and in the corporation at large.

Despite the increasing awareness that tone at the top matters, it is rarely translated into effective new board practices.

Board evaluations are a case in point: they do not include the required attention for culture and behaviour.

Corporate culture starts with the board and the board space: what kind of interactions, behaviours, language, and data does one observe? How packed is the agenda with technical content, or too many topics to discuss?

Many board meetings prevent, by design, engagement in meaningful conversation.

Can the role and behaviour of the CEO and chairman truly be discussed, as they are the key players driving the functioning of the board? Few boards possess explicit expertise in this domain.

Boards often assume that having some experience with corporate culture (like with leadership and change) is sufficient to navigate and supervise issues of culture. But it is not the same as expertise.

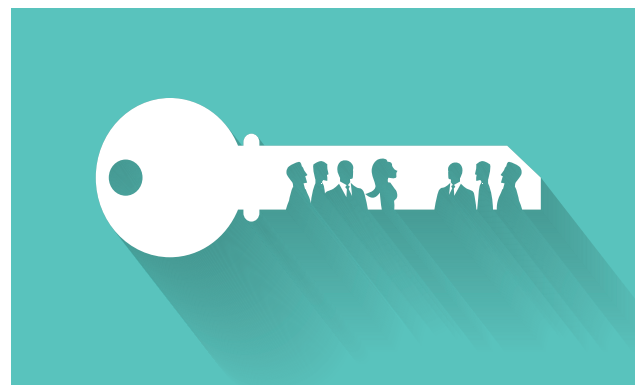
That assumption is a naïve self-serving illusion. Appointing a single board expert will not work if the other board members do not understand the language and distinctions that seek to address issues of culture.

Executives and non-executives need to up their game in corporate culture and be open to learn and develop.

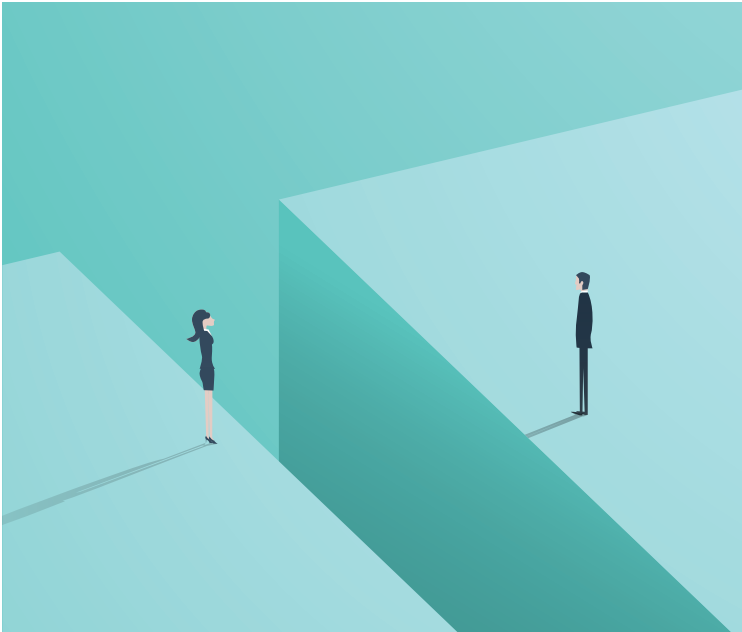
That is a challenge; the ability to truly learn is not easily triggered in boards.

Board members feel pressure to be seen as knowledgeable—and the assumption that everyone is on the board because of previous achievements and expertise often creates an environment that is hostile to true learning.

Acknowledging limited understanding is the first step for boards to open up to developing their knowledge of corporate culture.



Introduction



SETTING THE RIGHT corporate tone from the top is seen, by far and away, as the most effective way to influence the culture in today's businesses. Lead by example, and others will follow that lead. But research among European company board directors reveals that this belief is not being reinforced by action on how their business behaves.

There appears to be a significant discrepancy between what these board directors believe and what happens in practice. It is a gulf that needs to be bridged if they are to maintain, or restore, public trust in their businesses.

How can customers believe the business is doing the right thing if

corporate culture is not given the appropriate weight at boardroom level? Boards not only need to say what they believe, but also build it in to everything they do, particularly when developing their corporate strategy. Too often, there is a disconnection between desired behaviour and reality.

So just how seriously is this issue being taken in boardrooms? Not as seriously as one would expect, it appears. That is not to say that board members aren't thinking about it. It is just that they do not appear to be very effective in putting their thoughts into practice. And when they are, it is being done in an inconsistent way. The research, carried out by Board Agenda and Mazars, in association with INSEAD, confirms the view that, quite simply, more must be done.

Pressure will be brought to bear from regulators. As Sir Win Bischoff, chairman of the Financial Reporting Council, said recently: "Culture in business is a key ingredient in delivering long-term sustainable performance. When there is a healthy culture, the systems, the procedures, and the overall functioning and mutual support of an organisation exist in harmony. This brings enhanced integrity, confidence, long-term success and, ultimately, trust. A poor culture is, in my view, a significant business risk in itself."

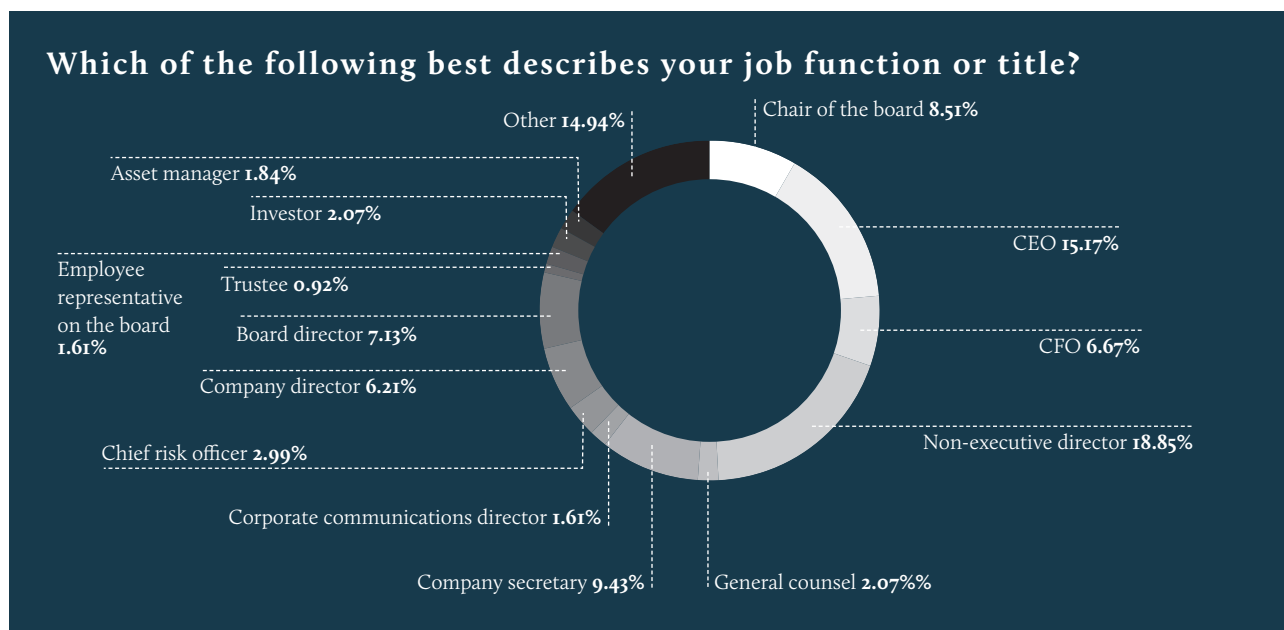
If boards are to avoid this pressure, then they will need to grasp the cultural nettle. They will need to plan, implement and measure the success of their efforts. And report on them in a transparent way to ensure that, not only are they tackling cultural issues, but that they are being seen to do so.

Alexandra Schaapveld, independent director, and chairwoman of the Audit & Internal Control Committee, Société Générale, said: "It is clear from this interesting report that culture and leadership need to be addressed by boards. Culture must be removed from an HR remit and made visible to all, into the front office. The board must be highly responsible for the tone at the top and make a clear interlinkage with culture to strategy."

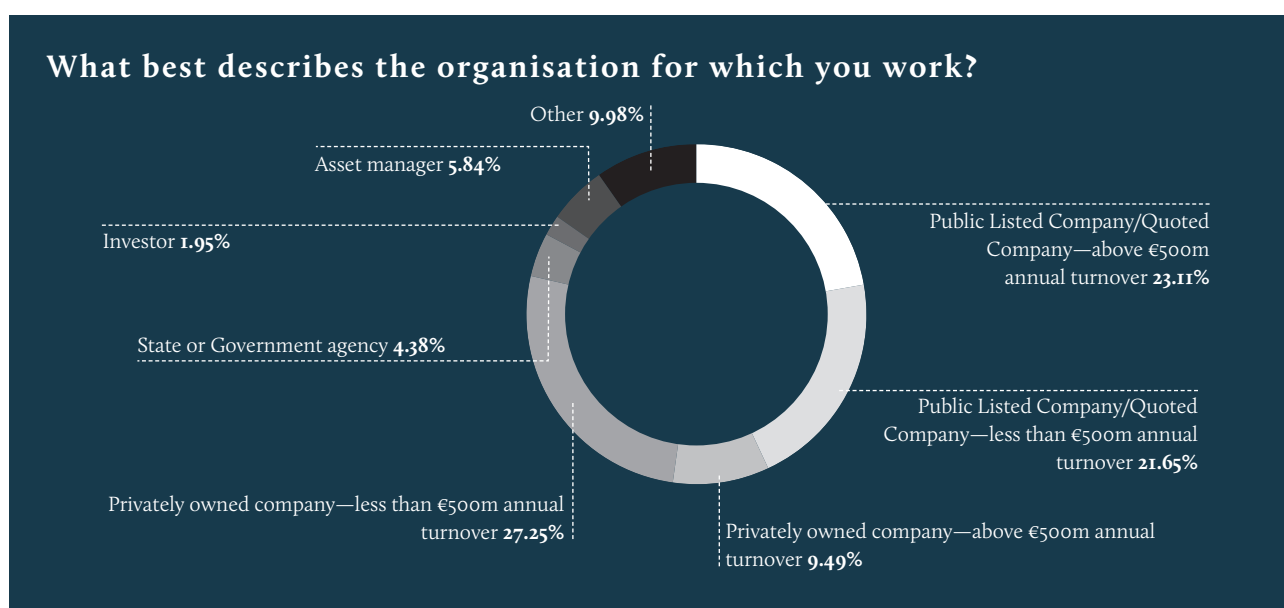
This research shines a light on the mismatch between words and deeds—it is to be hoped that the emphasis placed on the tone from the top, especially in the role of chief executive officer, will rapidly spread around the boardroom table and into the business.

Methodology

The Board Agenda survey was conducted during the summer of 2017, with 450 responses from chief executive officers, chief finance officers, board chairs, executive and non-executive directors, company secretaries, risk officers and investment managers. The survey was carried out online, via SurveyMonkey.



The respondents represented both private and publicly listed companies and were drawn from the UK & mainland Europe. Nearly a quarter came from quoted companies with an annual turnover greater than €500m, while a similar number were from quoted companies with an annual turnover of less than €500m. Ten percent represented private companies whose turnover exceeded €500m, whilst 27% were from private companies with a lower turnover than this amount.



The findings

1. How important is corporate culture to the board of directors?

As a starting point, this research sought to find out just how important the issue of culture is to board directors. Respondents were asked to rank in order of priority six specific aspects that a typical board would be expected to focus on. These include risk management, sustainability and productivity. As one might expect, strategy is the number-one issue in the boardroom, followed closely by financial performance. Culture was then placed third, above the other remaining issues.

This suggests that business culture is of significant importance to boards, and as a consequence, one might expect to see the subject appearing regularly on board agendas. This view is given additional weight when considered against the follow-up question on whether board directors believe the view of management guru Peter Drucker, that “culture eats strategy for breakfast” in terms of its impact on business performance. Nearly four out of ten respondents agree with this assertion, while only a tenth disagreed, saying that strategy is more important. But perhaps more telling is the fact that more than half believe that strategy and culture are interrelated.

This alone suggests that board directors are fully aware of the impact that corporate culture can have on business performance, and that it should be working hand-in-hand with strategy to develop this performance. However, such a finding, while seemingly attractive, will ultimately prove to be superficial, as the views expressed in answers to further questions will begin to show.

Where would you place culture relative to other issues as a topic of importance to your board? (Rank in order of priority)



2. How can the board influence business culture?

But first, the research sought to establish how board directors believe that their actions and decisions can have a wider impact on their businesses. When asked what are considered to be the main ways in which the board can influence the culture of the business, respondents placed “setting the right tone from the top” as the most important method. In fact, 62% place it at the top of their rankings. Again, on the face of it, a very encouraging result.

The second most important aspect was ensuring the CEO was supportive of the desired culture, though only 16% placed it at number one in their rankings. The third most popular choice was to ensure the recruitment of board members and senior management who supported the desired business culture.

This focus on getting the right people at the top of the organisation, and acknowledgement that these people can have a direct influence on culture, outweigh other methods on influencing behaviour such as effective communications and training programmes, as well as linking bonuses and incentives to desired cultural outcomes. In fact, training programmes hardly register at all, while only 3% place executive bonuses at the top of their list of preferred influencing methods. The results would seem to suggest that directors believe that positive culture cannot be bought or taught. Instead, it is something that is inherent in those at the top.

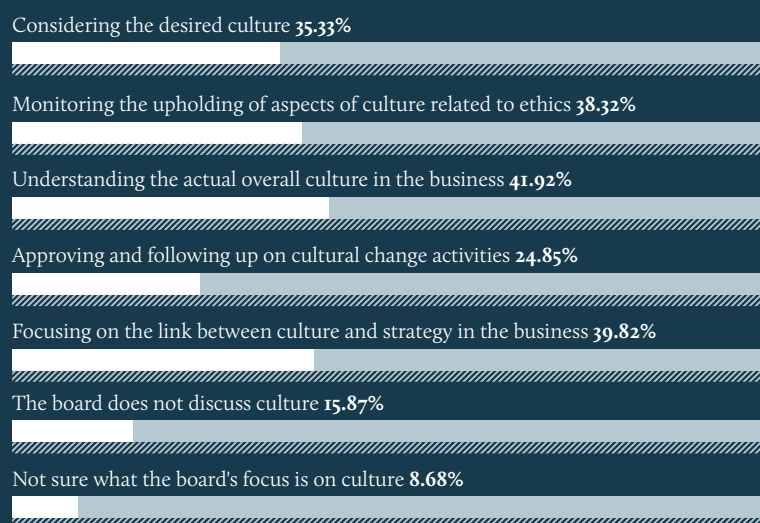
What do you consider are the main ways in which the board can influence the culture in the business? (Rank in order of priority)



3. What are the main areas of focus for discussion of business culture?

When directors come together to discuss culture, what is it that they really discuss? Top of the list is the desire to understand the actual overall culture within the business. This is the most popular area of focus, but is closely followed by the link between culture and business strategy, and a specific desire to monitor the upholding of aspects of culture related to ethics.

What are the principal areas of focus in the board's discussion of culture?



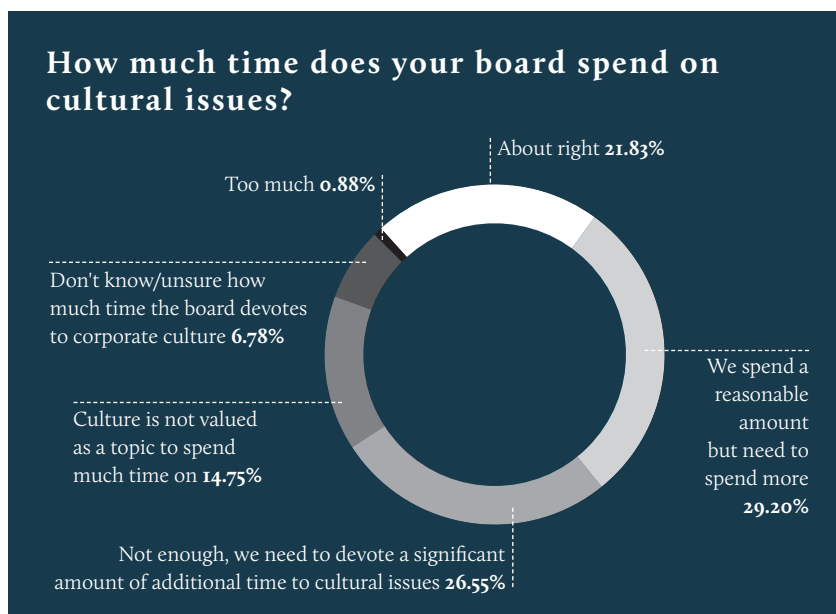
A third of respondents agree that consideration of the desired culture is an important area of attention, while a quarter focus on approving and following up on cultural change activities. Only 15% say that the board does not discuss culture, while a further 9% are not sure or don't know about the board's focus.

Such focus would suggest that the board dedicates a certain amount of time to understanding and influencing corporate culture. But this is where the research begins to expose a disconnection between what board members might think is right, and what actually happens.

4. How much time does your board spend on cultural issues?

Given the results to the previous two questions, it would be logical to conclude that corporate culture is a regular topic of conversation around boardroom tables. But this is where reality and board director beliefs begin to part company. When asked how much time the board spends on cultural issues, only one in five say the time spent is about right. A further 29% reckon they spend a “reasonable” amount of time, but need to spend more. Less than 1% say there is too much talk of culture in the boardroom.

More than a quarter say they do not spend enough time and that they need to devote a “significant amount of additional time” to cultural issues. Furthermore, 15% that say culture is not valued as a topic to spend much time on, and almost 7% either do not know or are unsure how much time is devoted to a subject that ranks as the third most important boardroom topic, behind strategy and financial performance. Thus, it becomes apparent that there is a disconnection emerging between the hopes and reality of boardroom cultural conversations.

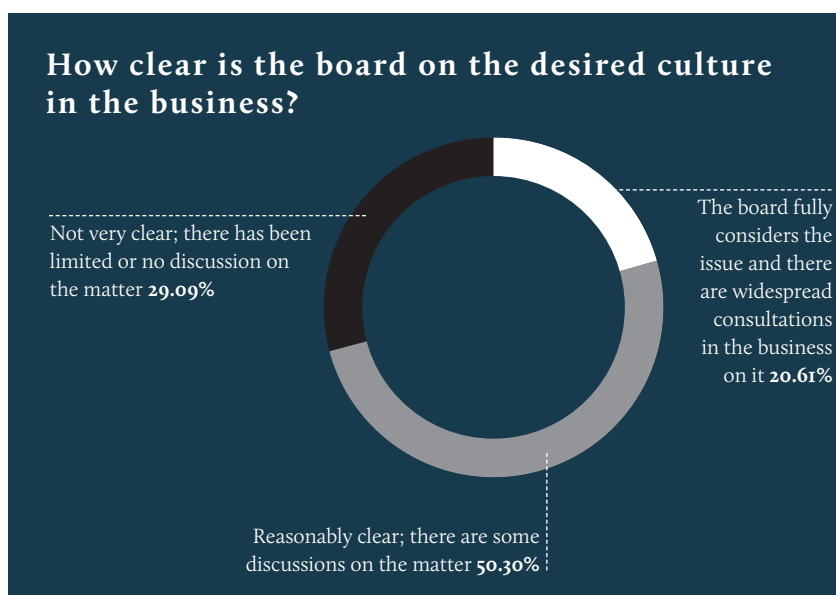


What is it that prevents such an apparently important subject from being placed firmly on the board agenda? Is it because there is a lack of clarity about what the board collectively desires?

5. How clear is the board about the desired business culture?

This is a straightforward question, but the picture is not as clear as the certainty expressed in earlier answers. Half those that responded to the question say they are “reasonably clear” and that there are some discussions on the matter. Nearly one-third (29%) admit that they are not very clear, and that there has either been limited or no discussion of the matter. Only 20% say the board fully considers the issue and that there are widespread consultations in the business on it.

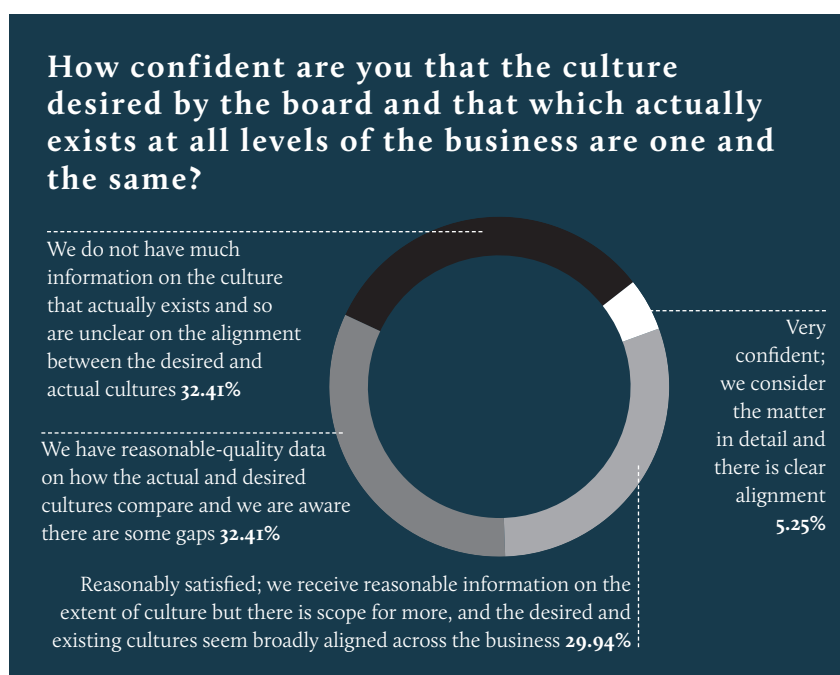
So, the reasons behind the apparent gap between the importance that individuals might place on culture and the collective reality of what happens in the boardroom could be the result of a lack of clarity. It could be that boards are failing to understand their existing culture, let alone have collective agreement on what a desired culture should look like.



The gap in understanding culture could be the result of a gap in information available to the board. Without this knowledge, it could be argued that it becomes very difficult to understand how culture aligns with other business objectives. This makes it very difficult for the board to discuss culture in any meaningful way. And without this clarity, it becomes difficult to have confidence that what is desired and what actually exists is the same.

6. How confident are you that the desired culture and the actual culture are one and the same?

Confidence that desired culture aligns with reality is evenly split three ways, between “reasonably satisfied” to an awareness that there are gaps, through to a lack of information that means it is unclear whether there is alignment between desired and actual culture.



Only 5% are able to say they are “very confident” that there is “clear alignment”.

Thirty percent say they receive reasonable information on the business’s culture but accept there is scope for more, though from the information available they are able to claim that the desired and existing cultures “seem broadly aligned” across the business.

These current levels of confidence could be linked to the nature and source of information that is being collected, but the overall results suggest that even these levels of confidence could be misplaced.

7. What are the main sources of information on culture?

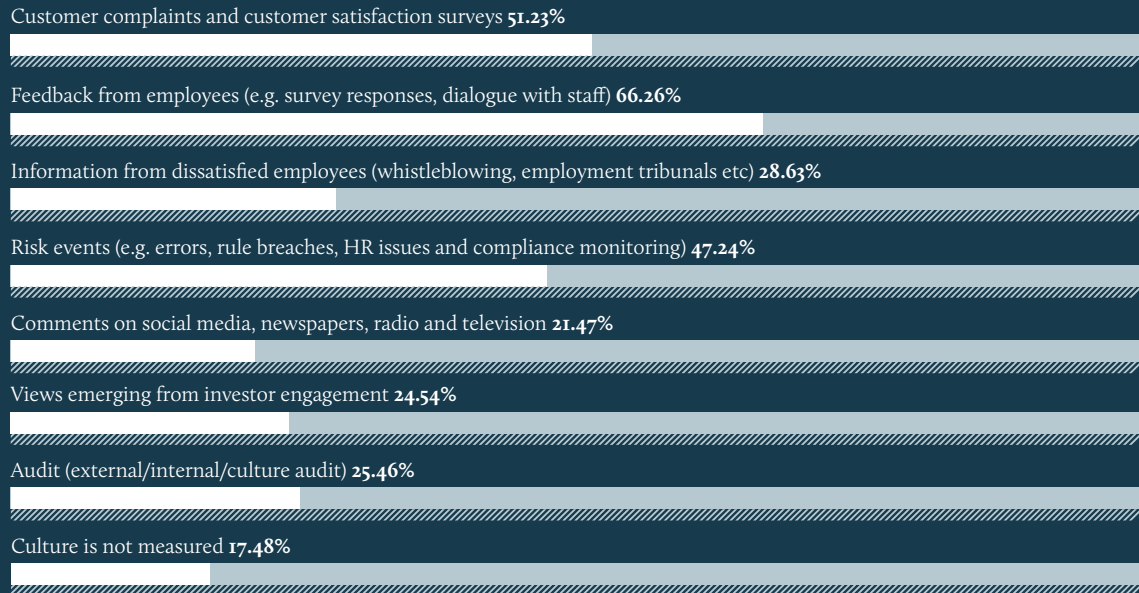
There are a wide range of sources available to companies as they consider and evaluate their business culture. These can be split into internal and external sources and it appears that the board is able to tap in to both in equal measure.

The most popular source is the business’s employees, who are after all the ones required to demonstrate and live the board’s desired culture. Feedback from employees through survey responses and dialogue, at 66%, is the most prevalent, followed by a more outward-looking use of customer complaints and satisfaction surveys. Risk events, such as rule breaches and compliance monitoring are popular with half of the respondents.

Information from dissatisfied employees, through exit interviews to whistleblowing and employment tribunals, is used as culture-related data among 28% of respondents, while audit and investor engagement have a broadly similar level of popularity.

Comments on social media, whether based on fact or posted maliciously, were only considered by 21.47%.

What are the main sources of information that the board receives on the nature of the culture as it exists in practice? (Choose up to three)



But most worryingly, 17% say that culture is not measured. There is a saying that if something isn't measured, it doesn't get done. And if this is the case, then it becomes difficult to establish whether business culture is aligned with strategy and purpose.

This lack of measurement also extends into risk assessment.

8. Does the board actively consider the risks associated with its particular culture?

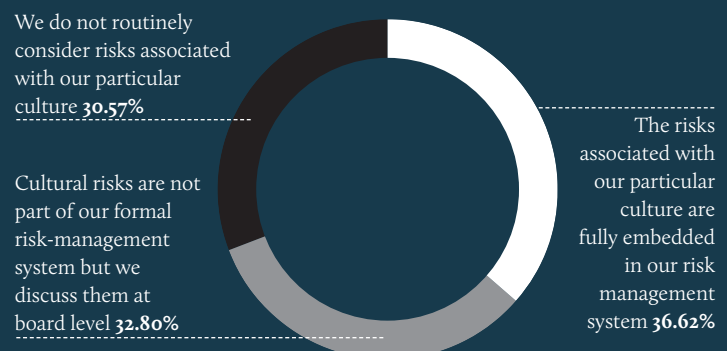
Board Agenda asked how deeply embedded culture was within corporate risk management. For instance, what would be the risk of unethical behaviour where there were significant incentives associated with performance, such as sales targets?

The results reveal a three-way even split. One-third claim the risks associated with their particular culture are fully embedded in their risk management systems, while a similar number say that, although cultural risks are not part of their formal risk management system, they are discussed at board level.

However, 30% admit that they do not routinely consider risks associated with their particular culture.

This risk assessment, or rather a lack of it, would appear to extend to how well the board aligns its business culture with its strategy.

Does the board actively consider the risks associated with its particular culture (e.g. the risk of unethical behaviour where there are significant incentives associated with performance, such as sales targets)?



9. Does the board consider how well aligned its culture is with its purpose and strategy?

Only one in ten are able to say their board is very clear on its purpose, culture and strategy and that they have actively checked that all are well aligned. Compare this with the answers given to Druckman’s breakfast proposition.

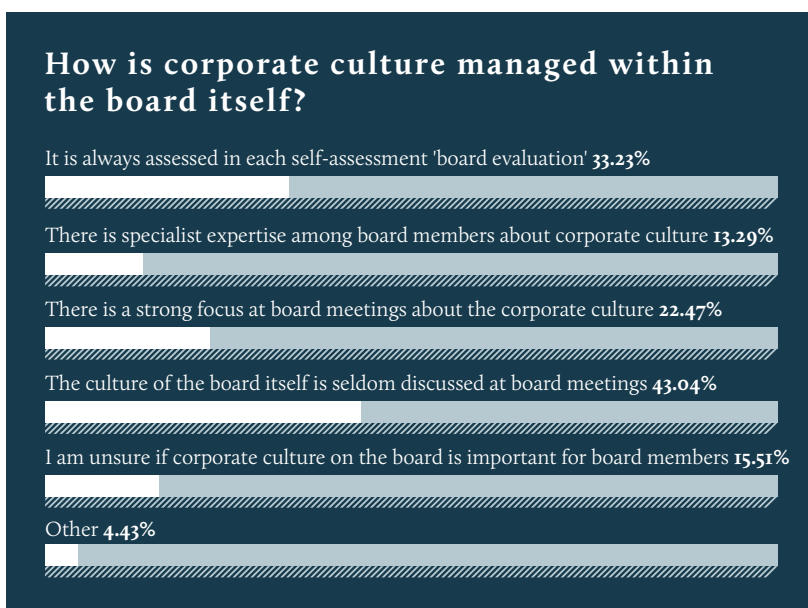


Forty percent of respondents say they are clear on purpose and strategy, and that these “seem broadly consistent with our culture”. This is not overwhelming confidence, but given the disparate ways companies evaluate their culture, as noted in the previous question, this is perhaps to be expected.

However, the bigger concern is that half of respondents are either aware of “some significant gaps” between their strategy and culture (25%), or have not spent much time considering this alignment (25%). This lack of alignment appears to continue into the boardroom, as the answers to the next question reveal.

10. What processes are in place to ensure that the culture and behaviour of the board is aligned to the needs and culture of the company?

Encouragingly, a third claim that management of corporate culture within the board itself is assessed during every board evaluation, with nearly a quarter (22%) stating that there is a strong focus at board meetings about the corporate culture of the board, while 13% claim that there is specialist corporate culture expertise among board members.



But conversely, 43% say that the culture of the board itself is seldom discussed at board meetings, and a further 15% claim that they either do not know or are not sure if corporate culture is important for board members.

This itself does not align very well with the previously stated desire to set the right tone from the top.

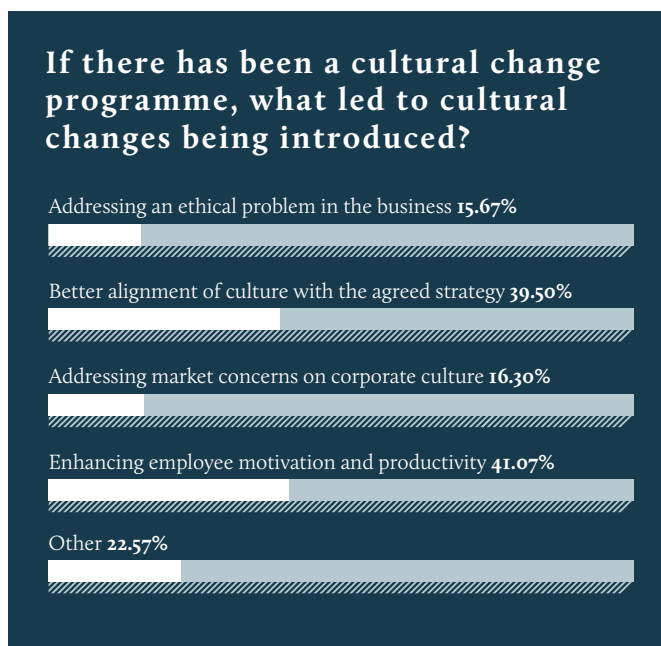
So why is there a lack of alignment among so many of the respondents? Perhaps the answer lies in what businesses are trying to change when they embark on a cultural change programme.

11. What has led to cultural changes being introduced?

The Board Agenda research asks directors if there had been a cultural change programme within their business, and if so, what led to cultural changes being introduced.

Some 40% say that this was to better align culture with the agreed strategy, but an equal number (41%) say it was to enhance employee motivation and productivity. Only 16% say it was to address an ethical problem in the business while a similar number say it was to address market concerns on corporate culture.

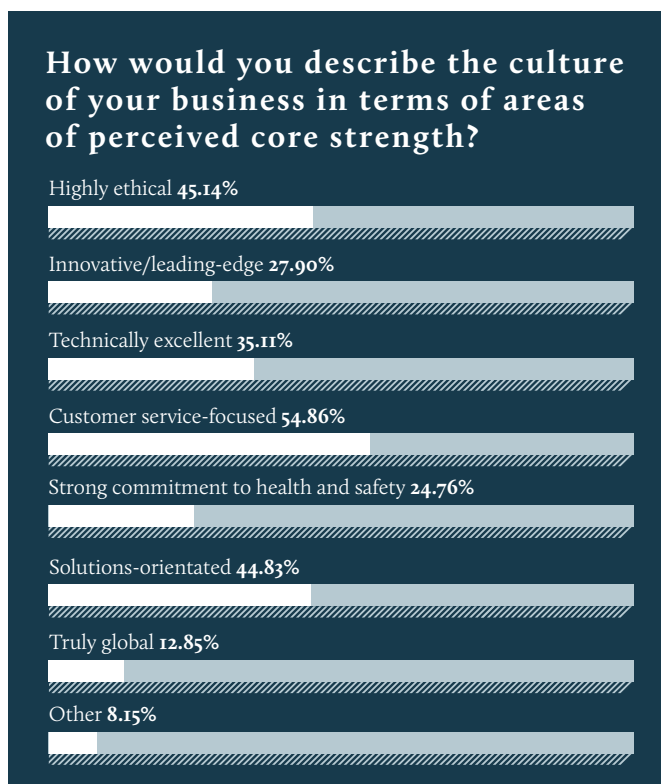
It could seem, therefore, that for many companies, culture is a siloed issue that relates to the management of staff. But it equally could be argued that change programmes are not required, as shown in the answers given when respondents were asked to list their culture in terms of core strengths.



12. How would you describe the culture of your business in terms of perceived core strength?

More than half of respondents (54%) say that one of their core strengths lies in their focus on customer service, and a surprisingly low proportion (27%) see their core strength as either being innovative or leading-edge. Some 35% believe their strength lies in being technically excellent.

But close to half (45%) also say that they are perceived to be highly ethical, which would have to rank highly in most boards' list of desirable cultural traits. If half see their business strength in this commitment to ethical behaviour, then perhaps they feel they are well on the way to creating the culture they desire in their business. This could either indicate that there is a mismatch between perception and reality, or that they are beginning their cultural journey. If it is the latter, then there is cause for optimism—the bridge is under construction.



Conclusion

How to bridge the cultural divide

1. Move culture from HR to the boardroom
2. Focus on divergence between aspiration and reality
3. Gather information and measurable data
4. Identify the challenges
5. Align with strategy
6. Build into risk assessment
7. Improve expertise in the boardroom
8. Look outside the business as well as internally for evidence of culture
9. Evaluate impact of social media
10. Engage with investors



This research into corporate culture confirms what had only previously been seen as anecdotal: while board directors acknowledge the importance of culture, and are thinking about how it can impact on the business, these thoughts have not been translated into actions. There is a worrying lack of time dedicated to culture in boardroom discussions, and even when it is discussed, it is done so in internal terms rather than fully incorporating external views.

However, there are grounds for optimism. The direction of travel is positive, but in reality the journey has only just begun. Without measurement and evaluation, that journey could easily come to a standstill, but analysing just part of the available data could create a false map to follow, leaving the board and their businesses progressing along the banks rather than building bridges to take them across the cultural divide.

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