Building a better working world

EY Center for Board Matters

Four ways boards can govern culture to reduce risk

New EY research reveals that some boards may be overlooking a vital ingredient of business success: culture. Just 22% expect that a misaligned culture will more than moderately impact their business in the next 12 months. In other words, culture is the risk category boards are least concerned about.

And boards are not alone. Even fewer (11%) CROs expect misaligned culture to more than moderately impact their business in the next 12 months. And according to the EY CEO Imperative study, CEOs rank culture and purpose as their lowest priority area for change in the next three years.

Complacency in this regard can introduce undesirable risks. When aligned with the organization's purpose and supported by leadership, culture serves to protect and create value. When it isn't aligned, risks increase, and potential value is left on the table. Companies that lead in risk management understand this.

Our global board risk survey found that 80% of companies leading on risk management often or always talk about the culture needed to support the organization's strategy at board meetings. In comparison, 63% of organizations that are classified as "developing" in their risk management approach do the same.

How can your organization join the leading group, if it isn't there already? As part of our Board Imperative Series, we offer four ways that boards can govern culture and enhance risk management:

1. Align corporate culture to strategy, and recognize when your culture should evolve
2. Consider how your culture is communicated and reinforced
3. Ask your management team to measure and monitor progress on culture
4. Carve out enough time to discuss culture at board level

1 Align corporate culture to strategy, and recognize when culture should evolve

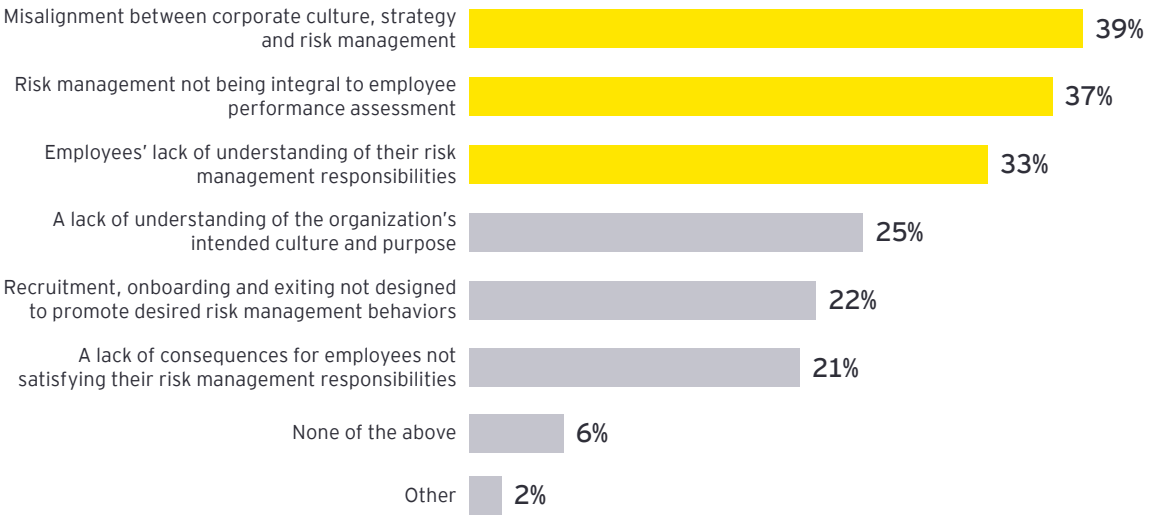
Misalignment between culture and strategy is the greatest culture and workforce-related challenge when it comes to risk management. A corporate culture that is inspired by the company's purpose and aligned to its strategy enables and accelerates that strategy. Culture also is a critical component of enterprise risk management: it influences how an organization identifies risk, what types of risks it accepts, and how it manages risk. A misaligned culture can introduce additional risks.

As organizations transform, they must also evolve their culture. Often this evolution comes in response to shifts in strategy and the changing business landscape. For example, recent social justice movements inspired many companies to focus more on diversity and inclusivity. Additionally, the pandemic forced many companies to adopt new ways of working, which led some to adopt a more flexible culture and introduce new ways of collaborating virtually. Our survey shows that boards of companies with the most effective risk management spend time discussing how to foster the required organizational culture in a remote working environment.

According to the data, leading boards spend more time discussing how management teams define corporate culture in the context of the organization's strategy. They recognize that management's role is to articulate the organization's desired culture, and identify and work to close gaps that may exist between the current and desired culture. As a board member, you play an important role in overseeing how management defines and continuously harmonizes culture, strategy and risk management.

What are the greatest culture and workforce-related challenges in your organization in regards to risk management?

Respondents selected up to two options



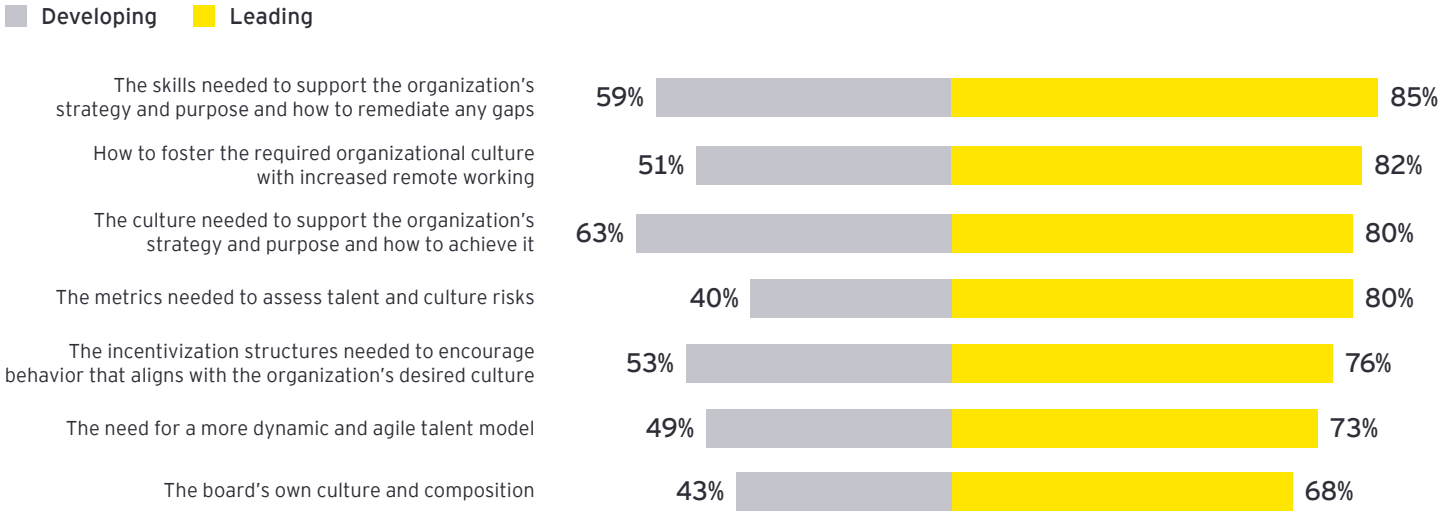
2 Consider how culture is communicated and reinforced

Shifting your organization's culture and sustaining related behavior changes takes deliberate design, practice and measurement. A critical component of shifting culture is instilling accountability for how it is communicated and lived throughout the organization – and internal communications can be key to reinforcing desired behaviors. For example, the board should evaluate how culture is communicated to new employees during onboarding and how leadership reacts to breaches of the company's stated values. Boards should seek to validate that management frequently communicates and demonstrates the desired culture and associated key behaviors across the entire business.

According to the survey, boards of organizations that lead in risk management spend more time discussing how to incentivize behavior that aligns to the organization's desired culture. As a board member, consider how to align executive compensation to the desired behaviors and culture of the company, and confirm that there are clear and straightforward linkages between rewards and the right behaviors.

With investors, regulators and other stakeholders paying close attention to culture, it is important to understand and consider how the organization communicates about its culture and related incentives externally.

How frequently are the following topics, related to talent and culture, discussed at board meetings?



> I would put culture as one of our most important risks alongside cybersecurity, operations risk and regulatory risk. We discuss culture at every board meeting because of its importance.
>
> Brendan McDonagh, Deputy Chair, AIB

3 Measure and monitor progress on culture

Just half of board members are confident in the reporting they receive from management on culture and conduct-related risks. Leading boards take a more proactive approach.

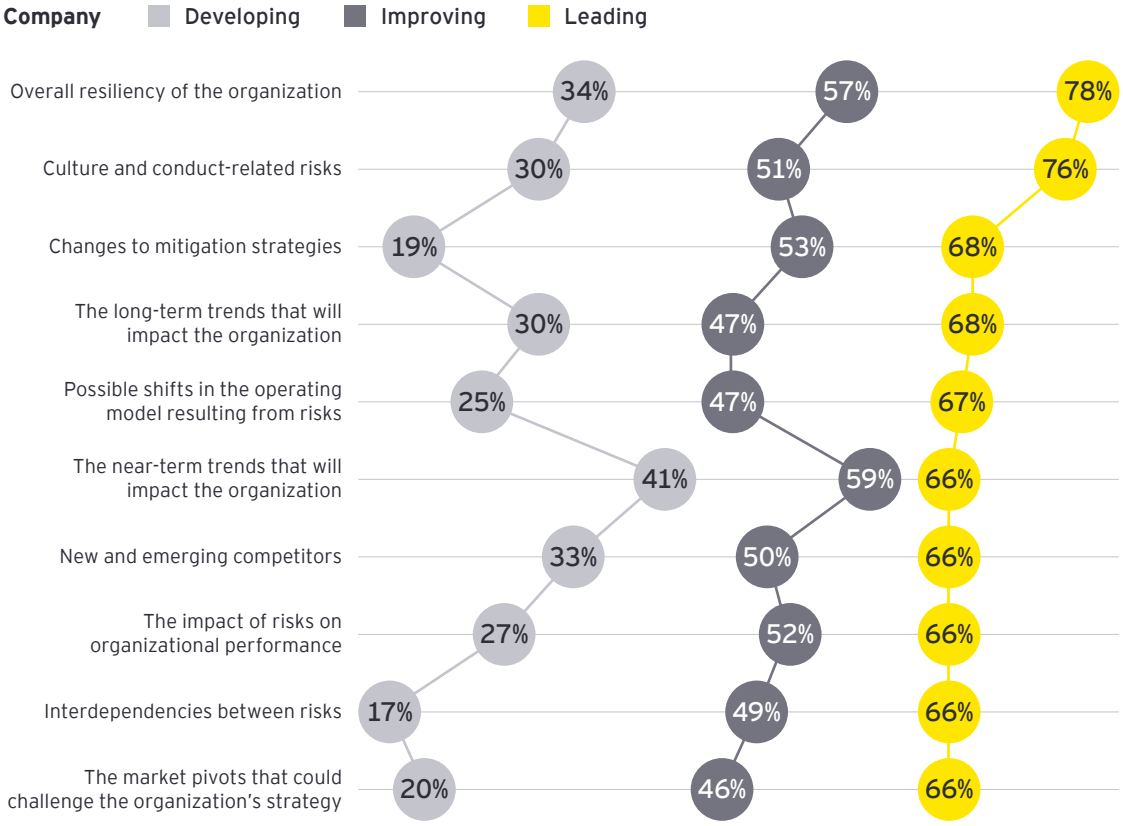
Our survey indicates that 80% of boards of organizations that lead on risk management (as opposed to 40% of those considered laggards) discuss the metrics needed to assess talent and culture risks.

For enhanced reporting on culture, effective and leading boards look for analytics of cultural trends, benchmarking to other entities or standards, reviews of behavioral trends and surveys of risk attitudes and risk awareness. If it isn't already, your board should consider regularly reviewing direct and indirect culture metrics such as employee pulse surveys, employee onboarding and exit interviews, and other customer surveys.

Don't forget that discussions with management can help you gain context about the data and give you valuable insights into how the data relates to the company's strategy and culture evolution efforts. The Chief Human Resources Officer can be a strategic resource on these matters as they assume a greater role in overseeing the company's culture and talent goals and assessing the company's overall return on talent investment.

Leading companies are significantly more confident in their risk reporting to the board

Percent of respondents that are confident



4 Carve out enough time to discuss culture at board level

The past 12 months have served to emphasize the importance of culture, as remote working put physical distance between office-based employees, and essential workers were asked to shoulder the burden of the pandemic. Increasingly, regulators are focusing on culture as well. In recent years, changes to corporate governance codes in the UK, the EU and Japan emphasize the importance of the role that boards must play in defining, instilling and measuring culture. Major global institutional investors also are paying attention.

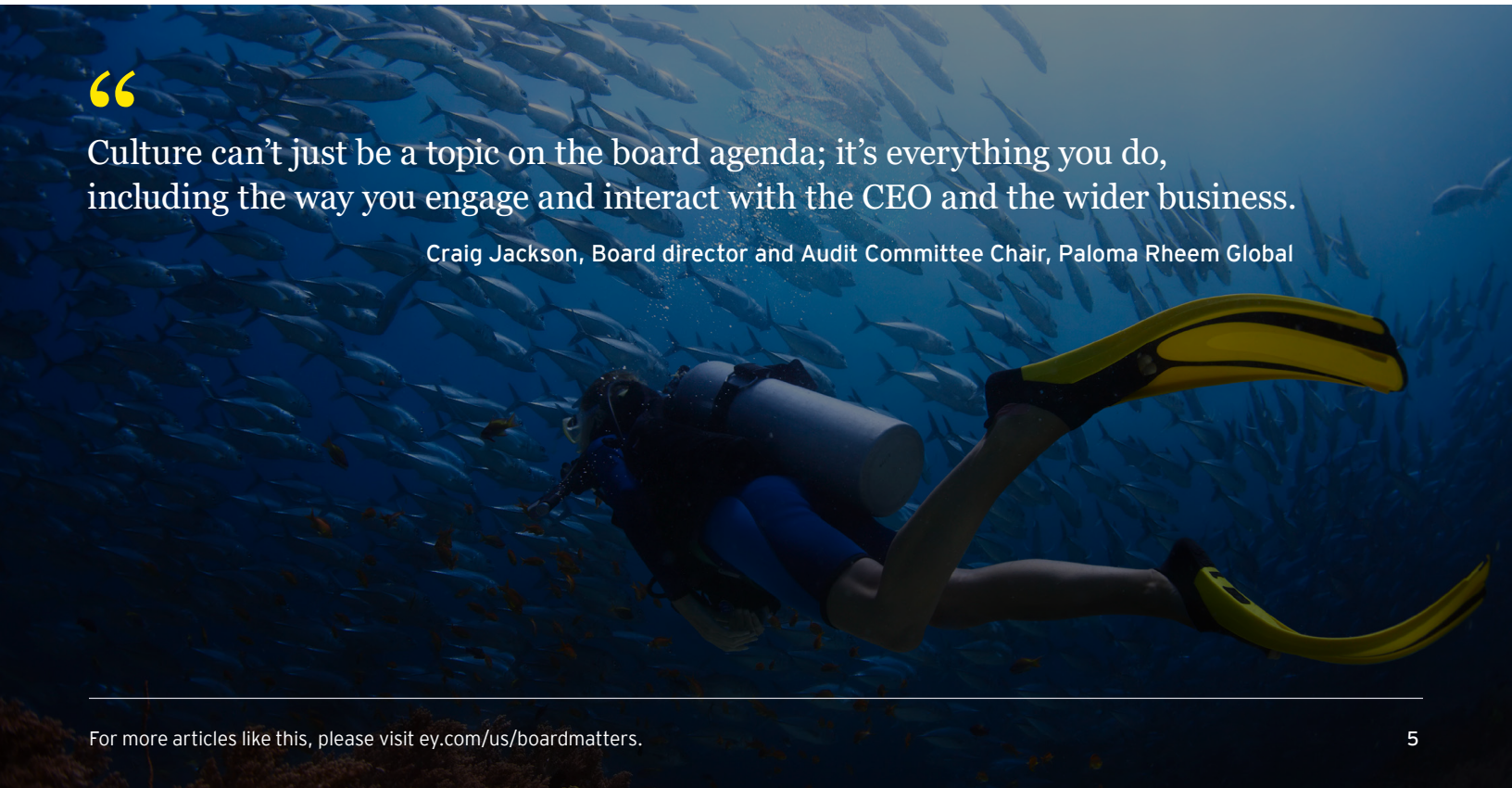
That's not to say every board ignores this topic. We spoke to many board members who spend a considerable amount of time thinking about culture. But the survey data indicates most boards are prioritizing other issues.

Is your board dedicating enough time and attention to culture matters? We found that 27% of boards never or rarely discuss the culture needed to support their organization's strategy. Further, 38% of survey respondents say the board never or rarely discusses its own culture and composition.

Boards should regularly consider how culture supports and aligns to the company's purpose and strategy. The board should evaluate every board decision to determine whether it reinforces or undermines the desired culture. Furthermore, the board plays an important role in setting the tone at the top and can demonstrate a commitment to the importance of culture by regularly evaluating its own composition and dynamics.

Given the importance of corporate culture and the move to a more distributed workforce, organizations and boards should assess the current state of their culture and deliberately evolve it to achieve desired business and stakeholder objectives. You can help management realize culture as a strategic asset by enhancing your oversight of culture in relation to strategy and risk management and by holding both the board and management to higher levels of accountability.

Methodology
The EY Global Board Risk Survey 2021 is a survey of 510 global board directors from organizations with greater than $1bn revenue and across industry to uncover their perception of enterprise risk management (ERM) within their organizations.



"Culture can't just be a topic on the board agenda; it's everything you do, including the way you engage and interact with the CEO and the wider business.

Craig Jackson, Board director and Audit Committee Chair, Paloma Rheem Global

Questions for the board to consider

- Do we set the right tone at the top and give enough attention to culture at our board meetings as a key enabler of strategy?
- How thoroughly have we, as a full board or committee, discussed the impact of culture on risk, risk management and the internal control environment?
- How is the organization's culture shifting to align with a change in strategy? Can the company achieve new things with old ways of working?
- Have we discussed metrics that could be gathered and monitored as a barometer for cultural fitness? Does management's reporting need to be adjusted to capture better data for the board's consideration related to culture matters?
- Do our board's composition and dynamics support the company's commitment to fostering an environment and culture of diversity and inclusion as well as its broader purpose?

Looking for more?
Access additional information and thought leadership from the EY Center for Board Matters at ey.com/us/boardmatters.

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Effective corporate governance is an important element in building a better working world. The EY Center for Board Matters supports boards, committees and directors in their oversight role by providing content, insights and education to help them address complex boardroom issues. Using our professional competencies, relationships and proprietary corporate governance database, we are able to identify trends and emerging governance issues. This allows us to deliver timely and balanced insights, data-rich content, and practical tools and analysis for directors, institutional investors and other governance stakeholders.

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