UNDERSTANDING & ASSESSING CORPORATE CULTURE

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  – IIA’s Superconference CAE Panel Discussion
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  – Women’s Energy Network
  – Energy CAE Shareforum
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Certifications:
- CPA – Since 2000
- CIA – Since 2008
- CISA – Since 2008
- CGEIT - Since 2009
- CRISC - Since 2011
- CRMA – Since 2011
- CCSA – Since 2007
- CGMA – Since 2012
Professional Development:
- **Nationally-Recognized Leader** in Audit and People-Centric Skill Training
- Over 100 Full-Day Courses on Audit, Accounting, Finance and People-Centric Skills
- Registered with NASBA to offer CPE’s for all courses in course catalog
- Competitive Pricing
- Interactive and Educational Courses for all levels

Executive Recruiting:
- Unique approach to filling positions, including personality assessment for candidate and organization
- Expansive network of qualified candidates actively looking

Staff Augmentation:
- Market leader in locating cost-effective, recognized resources in accounting, finance, audit and IT
- All requests filled within 72 hours
AGENDA

• What is Corporate Culture
• Pulse of Internal Audit
• Dimensions of Corporate Culture
• Key Areas:
  – Organizational Structure
  – Organizational Mission / Values / Strategy / Objectives
  – Compensation / Incentives / Performance Management
  – Enterprise Risk Management
  – Company Policies

• Case Studies:
  – Enron
  – Wells Fargo

• Perspectives from the BoD
  – Healthy Culture
  – Red Flags

– Interviews:
  • Tone at the Top
  • Mood at the Middle
  • Buzz at the Bottom

– Board Agenda and Reporting

– External Sources of Feedback: Ex-employees / External Auditors / Regulatory Audit Report
CULTURE QUOTES

“Culture eats strategy for breakfast.” - Peter Drucker

“The only competitive advantage we have is the culture and values of the company. Anyone can open up a coffee store.”
—HOWARD SCHULTZ, EXECUTIVE CHAIR, STARBUCKS

In looking for people to hire, you look for three qualities: integrity, intelligence, and energy. And if they don’t have the first, the other two will kill you.
—WARREN BUFFETT, CHAIR, BERKSHIRE HATHAWAY
What is Corporate Culture?
What Is Corporate Culture

• Generally shared beliefs that determine how a company's employees interact with each other.

• Blend of the common values, ethics, expectations, assumptions, goals, work environment, behaviors, and prohibitions that organizations develop over time

• The ‘personality’ or ‘DNA’ of the organization

• Usually unconsciously understood, not written.

SOURCE: Understanding and Assessing Corporate Culture, Manny Rosenfeld, April 2, 2015.
SUBCULTURES OF A CORPORATE CULTURE

• In large organizations, it is very likely that the various divisions, departments, and operating units have their own version of the corporate culture (i.e., subcultures).

• For the leaders of the overall organization, a major challenge is to properly align these subcultures so that they reflect the values and goals of the overall Corporate Culture.

SOURCE: Understanding and Assessing Corporate Culture, Manny Rosenfeld, April 2, 2015.
How do Corporate Cultures Form?

- Culture is usually started by the founders of the organization, and is in line with their beliefs, leadership styles, and values.
- Grows over time from the behaviors of the people the company fires, hires, trains, develops, and promotes (especially “key” players)
- ‘Proper’ cultural behaviors are encouraged and rewarded by the organization (reinforcement)
- Employees who chronically do not work within the culture of the corporation usually fail, and will likely end up leaving the organization

SOURCE: Understanding and Assessing Corporate Culture, Manny Rosenfeld, April 2, 2015.
2016 Pulse of Internal Audit Report
2016 IIA Pulse of Internal Audit Report

• 58% of respondents said they do not audit organizational culture

• Barriers to Addressing Corporate Culture:
  – 24% Do not believe internal audit has freedom to assess the entire organization and staff
  – 35% Do not believe internal audit has full support of executive management to assess all levels of the organization
  – 23% Do not believe internal audit has full support of the board or audit committee to assess all levels of the organization
## 2016 IIA Pulse of Internal Audit Report

### Factors Influencing Corporate Culture:

<table>
<thead>
<tr>
<th>Factor</th>
<th>% Respondents that ranked factor as 1st or 2nd Most Effective</th>
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<tbody>
<tr>
<td>Behavior Modeled by Executive Management</td>
<td>75%</td>
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<tr>
<td>Direct Communication by Other Employees</td>
<td>54%</td>
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<tr>
<td>Establishment of Code of Conduct</td>
<td>34%</td>
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<td>Behavior Modeled by Other Employees</td>
<td>16%</td>
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<tr>
<td>Formal Training on Code of Conduct</td>
<td>10%</td>
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<td>Enforcement of Code of Conduct through Disciplinary Measures</td>
<td>6%</td>
</tr>
<tr>
<td>Other</td>
<td>3%</td>
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</table>
DIMENSIONS OF CORPORATE CULTURE

SECTION SOURCE: Understanding and Assessing Corporate Culture, Manny Rosenfeld, April 2, 2015.
**Dimensions of Corporate Culture**

- Empowerment vs. Command-and-Control
- Ethical Orientation
- Teaming/Collaboration
- Improvement/Quality Orientation
- Communication Style
- Silos vs. Cross-functional Cooperation
- Management Style
- Fear/Risk Avoidance
- Cost-Cutting Focused
EmPOWERMENT vs. Command & Control

• Are employees micromanaged (minutely directed) or broadly empowered?
• What is the level of delegation?
• What are employees allowed to do without getting approval from their boss?
• Are most work instructions top-down, or is there room for employees at different levels to provide input?
• Is the organization managed in a hierarchical (military) style or is participative in nature?
ETHICAL ORIENTATION

• Do the executive actions match what they say about values?
• Are ethical lapses of certain employees treated differently depending on their perceived value to the company?
• Is there a history of regulatory problems?
• Are there executive discussions as to the odds that the regulators will find an issue and the ‘affordability’ of any fines?
**TEAMING & COLLABORATION**

- Do employees work mostly independently, or is teamwork and collaboration more the style?
- What are the interactions between employees? Friendly and supportive, or tense, cut-throat, and competitive?
- Are employees pitted against each other in a ‘dog-eat-dog’ fashion?
- Are employees more appreciated for being a very successful individual contributor (‘hero’), or for contributing to a very successful team?
IMPROVEMENT/QUALITY ORIENTATION

• Is there an expectation of being excellent and a desire to be ‘best-class’?
• Are all employees expected to generate ideas for improving their areas and processes?
• Are process failures carefully analyzed to understand the root causes? Or are failures just fixed and then people move on to the next crisis?
• Is continuous and relentless improvement emphasized? rewarded?
COMMUNICATION STYLE

• What is the tone and nature of communications to employees? Formal or informal?
• Do employees get news of corporate happenings via the ‘rumor mill’?
• Do employees have broad knowledge of the business or do they mostly know about their immediate area.
• Is it dangerous for employees to communicate bad news upwards? Are messengers of bad news “shot?” How are whistleblowers treated?
ORGANIZATIONAL SILOS VS. CROSS-FUNCTIONAL COOPERATION

• What is the interaction among departments? Is there a spirit of collaboration or are there ‘turf wars’?
• Do employees often blame their difficulties on other departments?
• Do broad business processes break down at the organizational boundaries of processes? (Implies limited collaboration between organizations)
**Management Style**

- How are employees valued, recognized, rewarded, and promoted?
- Is the accepted management style confrontational and aggressive, or collegiate and easy-going?
- Is there undue resistance to change?
- Are the company practices inflexibly rooted in the past?
- Do executives prefer employees who usually agree with them or do they prefer employees who tell the ugly truth?
FEAR/RISK AVOIDANCE

• Are risks well understood? Carefully considered and managed?
• Are the Risk/Reward aspect of actions considered?
• Are people afraid to change or innovate because the organization would punish them if an initiative failed?
• Is thoughtful risk-taking encouraged or discouraged?
COST CUTTING FOCUSED

• Budgeting Process expects cost cutting as a standard each year
• How many reductions in force have there been?
• Where are the cuts typically made?
OVERVIEW: AREAS TO ASSESS
ASSESSMENT AREAS

• Organizational Structure
• Organizational Mission / Values / Strategy / Objectives
• Compensation / Incentives / Performance Management
• Enterprise Risk Management
• Company Policies
• Interviews: Tone at the Top / Mood at the Middle / Buzz at the Bottom
• Board Agenda and Reporting
• External Sources of Feedback: Ex-employees / External Auditors / Regulatory Audit Reports
Organization’s Structure
What’s Wrong With This Picture?
POTENTIAL RED FLAGS

• Compliance related functions are not in place, including:
  – Compliance function
  – IT Security function
  – Quality function
  – Internal Audit function

• Reporting lines of compliance related functions

• Title and/or authority of heads of compliance functions

• They do not have regular reporting requirements to BoD

• Turnover in these compliance related functions
  – Are these leaders leaving for the reasons that would be a red flag?
POTENTIAL RED FLAGS

• There is no documented / written strategy, mission, values
• The strategy does not address “how” to achieve goals
• The strategy is not communicated company wide
• The performance measurement process does not align individual goals/objectives with company strategy
• Compensation is not tied to “how” the company achieves its goals (ethically, compliant w/regulations)
• The “how” does not apply to everyone consistently
PERFORMANCE EVALUATIONS

How are employees being graded?

- Volume of sales?
- Quality of sales?
- Is there a section on adherence to company code of conduct/policies/ethics?

Remember: People will behave the way to incent them to behave....
POTENTIAL RED FLAGS

• Compensation is based only on volume, speed or top line revenue
• Compensation is not impacted by “how” the goals are achieved or tied to “soft” metrics
• Sales goals are very aggressive or unrealistic
• Top sellers are given “passes” for compliance related breaches
POTENTIAL RED FLAGS

- There is no ERA or ERM process in place or not updated
- There is no risk mitigation plan for each risk
- There is not a process to receive status updates on risk mitigation plan progress / hold owners accountable
- There are no target vs actual metrics to measure progress
- Corruption / fraud risk is not on ERA (but is a risk for peers within industry)
- Internal Audit is not involved in process (at a minimum to assess / validate that mitigation plans are in place and operating effectively)
COMPANY POLICIES
Policies & Procedures

- What types of policies exist?
- To whom is policy distributed?
- Is written confirmation obtained that policy has been received and understood?
- Is it reviewed / updated on an annual basis?
- Is there training?
- What type of training is provided?
- Who is trained?
- How frequent is the training?
Policies & Procedures

• Policies should address the following:
  – Code of conduct
  – Anti-corruption
  – Travel & Entertainment
  – Charitable Contributions
  – Gifts
  – Per Diems
  – Facilitating / Extraordinary payments
OTHER RELATED POLICIES

• Whistleblower
• Procurement / Bidding
• Delegation of Authority
• Contract
• Accounts Payable
• Petty Cash
**POTENTIAL RED FLAGS**

- Policy is not reviewed / updated on an annual basis
- Training metrics are not defined (i.e. timeliness, participation, etc.)
- New employees / vendors are not trained within required timelines
- Employees / vendors have not received policy or have not been trained within required timelines
- Exceptions are made (e.g. for executives)
- Management overrides become the “rule” rather than the “exceptions”
Tone at the Top (Middle and Bottom)
WHO SHOULD YOU INTERVIEW?

• To understand the “Desired” culture:
  – CEO
  – COO
  – BU Presidents
  – CFO
  – CIO
  – CLO
  – HR Executive
WHO SHOULD YOU INTERVIEW?

• To understand the “Actual” culture:
  – Middle Management
  – Employees in all functions / depts.
  – Employees at all levels
  – Compliance / Chief Compliance & Ethics Officer
  – HSES / Quality functions
  – IT / CISO
What Questions Should You Be Asking?

The Institute of Internal Auditors
2016

The Standard in Staffing, Recruiting and Professional Development
Interview Questions

• Interview questions to assess Corporate Culture:
  – How would you describe the company culture in 3-5 words?
  – Do you (and others) have broad knowledge of the business or mostly know about your immediate area/job function?
  – Do you feel “safe” to report bad news without fear of retaliation?
  – If/when you have the need to report bad news, do you believe it will be handled/resolved timely and appropriately?
  – Do you feel empowered to perform your jobs?
  – Do you feel that employees are held accountable for their actions (or lack of action)?
  – Do you feel management “walks the talk”/their actions and behavior is consistent with the company’s stated values?
• Interview questions to assess Corporate Culture:
  – Do you have a clear line of sight between your work and the company’s strategic objectives?
  – Do you believe the company has clearly established values / ethics / principles to guide behaviors?
  – Do you believe that everyone in your group collaborates with each other and with other stakeholders in other groups to achieve common goals / objectives?
  – Do you believe that you are well informed about the risks and are comfortable with the way the company is managing them?
BOARD REPORTING

The Institute of Internal Auditors
2016

GOLD SRD
Staffing, Recruiting and Development

THE STANDARD IN STAFFING, RECRUITING AND PROFESSIONAL DEVELOPMENT
BOARD REPORTING

• What is reported to Audit Committee and by whom?
  – CAE
  – Chief Ethics & Compliance Officer
  – CISO
  – Quality Assurance

• Hotline Trend Reporting
  – Types of hotline activities (financial misstatement, fraud, theft, etc.)
  – Management actions to resolve (termination, training, etc.)
  – Time to resolve
  – Activity higher in specific region, office, department, manager
  – Repeat offenders
EXTERNAL SOURCES
EXTERNAL SOURCES

- Glass Door / Indeed (ratings and nature of comments)
- Former employees, especially those in compliance related roles/responsibilities (Exit Interviews, farewell lunch)
- External Auditors
- External Consultants
- Regulatory Auditors
- Industry Peers
- Benchmarking data
- Candidates (who declined offers)
- External Recruiters
THE SMARTEST GUYS IN THE ROOM

• No one at Enron used such terms as “build consensus”, it was “come to shore” (e.g. “Everyone needs to come to shore on this”)
• Skilling’s mantra was “Volume! Volume! Volume! (of deals)
• Enron’s socialization process was referred to “Enronizing” with people who didn’t fit in called “losers” or “shipwrecks”

• CEO Jeffrey Skilling was well know for his accusation that those who didn’t understand Enron or a particular financial structure were not “smart enough to get it”
• Smart people stopped asking questions for fear of looking like they didn’t “get it”
RED FLAGS

• Transparency (lack thereof):
  – Earnings call April 17, 2001:
  – When asked by analyst why Enron is the only financial
    institution that cannot produce a balance sheet or cash flow
    statement with their quarterly earnings.
  – CFO Jeff Skilling responds by calling the analyst an “A@$hole”

• Tone at the Top:
  – Ken Lay forced all Enron employees to book corporate travel
    through his sister’s travel agency even though it was more
    expensive than more competent agencies
  – “The slightest erosion in values at the CEO level is magnified in
    the trenches.” – Sherron Watkins, ex-VP at Enron and
    Whistleblower
Case Studies: Wells Fargo
“EIGHT RHYMES WITH GREAT”

- In 1997, CEO Dick Kovacevich, launched an initiative called “Going for Gr-Eight”
- This sales initiative required each employee to get the customers to buy eight products from the bank
- Why eight products? Because it rhymes with GREAT.
- For branches in small towns, it wasn’t easy – the town population was small and there could be seven other banks.
- Lesson learned: Employees will behave the way the organization incentivizes them to behave.
RED FLAGS

• Hotline trends:
  – In 2002 (15 years before the scandal), the company’s internal investigations unit noticed an uptick in “sales integrity” cases.
  – Employees were gaming the system to make sales goals.
  – Report recommended that company reduce or eliminate sales goals.
  – There was no follow-up.

• Shoot the Messengers:
  – Employees reporting gaming were ignored, fired or “retired”.
  – HR said they were aware that these practices were occurring throughout the company but “there was nothing they could do.”
SINS OF THE PAST

- Restated three years of financial statements (2011-2013)
- Five Material Weaknesses in Internal Controls
- 4 different CFOs within 1 year period
- Paid over $42 million in fines/penalties to SEC
- Four executives also paid penalties to SEC
- A separate SEC order found FCPA violations
- Company agreed to retain an SEC compliance consultant (“monitor lite”) to review and test its FCPA compliance
CORPORATE CULTURE: PERSPECTIVES FROM THE BOARD

Source for this section:
NACD Blue Ribbon Commission Report on Culture as a Corporate Asset
NACD: Blue Ribbon Commission

- “Oversight of corporate culture should be among the top governance imperatives for every board, regardless of its size or sector”

- Contains three parts:
  - Part 1: Definition and Key Attributes
  - Part 2: Outlines specific actions for Directors
  - Part 3: Summarizes recommendations and provide resources to help implement recommendations
DEFINITION OF CULTURE

- Explicit and implicit rules
- Norms of behavior and interaction
- Compliance and ethics policies
- Incentives
- Recruiting and training activities
- Processes for decision making and prioritization
- Communication and information flows
  leadership styles
Culture by the Numbers

- 87% of organizations cited culture and engagement as a top challenge
- 28% of executives reported that they understood their organization’s culture
- 12% of executives believed their company is driving the “right culture”
- 53% of directors believe some members of their boards are reluctant to express their point of view in front of management
HEALTHY CULTURE

• Directors should look for the following “signifiers”:
  – Alignment
  – Accountability
  – Transparency
  – Resilience
ALIGNMENT

• Clear linkage between company's:
  – Stated purpose
  – Expressed core values
  – Desired culture
  – Actual culture

• “Boards need to ask for evidence as to the consistency between the company’s statements about its culture and values, and actual behaviors”
ACCOUNTABILITY

• ‘Culture of accountability is one where “mistakes are identified, remedied, and regarded as a source of learning rather than of blame.”’

• “Fear of criticism can leave employees unwilling to take ownership and preferring to pass on responsibility to others.”
TRANSPARENCY

• Robust cultures have well-developed processes for communicating internally – up, down, across and externally

• Employees at all levels of seniority are encouraged to report problems, errors, or risks without fear of disciplinary action

• “Bad news takes the elevator and good news takes the stairs”
Resilience

• The foundational elements of a company’s culture and values must be able to withstand stressors from outside and inside sources

• Discussion about culture should be forward-leaning – encompassing where the company is going, not just where it’s been
Culture Red Flags

• Focus on revenue/income versus how results were achieved

• High performers allowed to operate outside policies

• Frequent “near misses” of adherence to code of conduct

• Go along to get along attitudes

• Relationships outweigh skills and/or performance

• Sharing bad news is discouraged (‘’shoot the messenger’’)

The Standard in Staffing, Recruiting and Professional Development
EXERCISE – LET’S ASSESS YOUR COMPANY CULTURE
YOUR COMPANY CULTURE

• Take a minute to think about what your organization’s “stated” or “desired” culture is (what are 3-5 words that are often used)?

• Based on your own observations and experiences of others who have shared them with you, how well do you think the “actual” culture aligns with the “desired” culture?

• How many culture red flags have you observed at your organization?
QUESTIONS?