LRN Inspiring Principled Performance

Measuring the Impact of E&C Program, Culture, and Leadership on Employee Behavior

EMILY MINER

LRN CORPORATION

Why do catastrophic compliance failures continue despite investment in ethics & compliance programs?

1MDB
1Malaysia Development Berhad
INVESTIGATIONS

408 Bank accounts frozen

Including those owned by :

81 individuals **&** **55** companies

Funds amounting to **RM1.1 billion**

Believed to be linked to the alleged embezzlement & misappropriation of 1MDB funds

Involving **900** transactions between March 2011 & September 2015

Source : 1MDB Special Task Force

Bernama Infographics

"Compliance is a culture, not just a policy."

US Department of Justice, Deputy Criminal Director of the Antitrust Division, 2017

A focus on culture is now table stakes – Regulators agree

US Federal Sentencing Guidelines
*"… undertake an appropriate assessment of corporate efforts to **create an organizational culture** that encourages a commitment to compliance with the law and ethical conduct.*

The Department of Justice
*"… A corporation is directed by its management and **management is responsible for a corporate culture** in which criminal conduct is either discouraged or tacitly encouraged."*

UK Serious Fraud Office
*"**Culture needs to be set from the top**. Members of the corporation need to know that the corporation is committed to ethical standards of business and that executives at the most senior levels are **role models for ethical business conduct**"*

The Securities and Exchange Commission
*"Keep up your vigilance, avoid complacency, and remain steadfast in your efforts to **maintain strong compliance programs, built on the foundation of a culture** in which investor interests are placed first. Let your business and compliance decisions always be guided by that principle."*
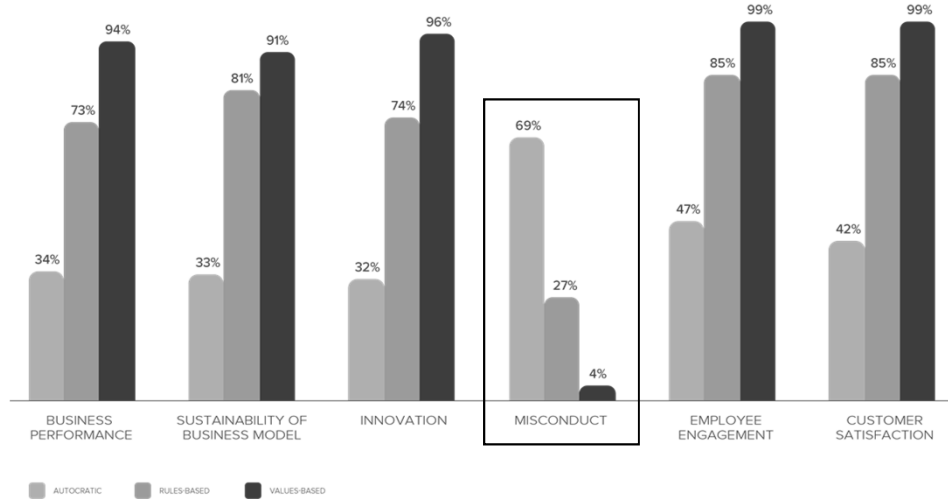
Australian Compliance Standard
*"The **development of a compliance culture** requires the active, visible and consistent commitment of the chief executive and management to a **common, published standard of behaviour** that is required throughout every area of the organization."*

International Monetary Fund
*"Ultimately, we need more individual accountability. Good corporate governance is forged by the ethics of its individuals. That involves **moving beyond corporate 'rules-based' behavior to 'values-based' behavior**. We need a greater focus on promoting individual integrity."*

LRN *Inspiring Principled Performance*

6

Organizations with strong, values-based cultures outperform

	AUTOCRATIC	RULES-BASED	VALUES-BASED
BUSINESS PERFORMANCE	34%	73%	94%
SUSTAINABILITY OF BUSINESS MODEL	33%	81%	91%
INNOVATION	32%	74%	96%
MISCONDUCT	69%	27%	4%
EMPLOYEE ENGAGEMENT	47%	85%	99%
CUSTOMER SATISFACTION	42%	85%	99%

LRN Inspiring Principled Performance

Source: LRN 2016 *The HOW Report*

7

The trend is growing

Over the past five years, my organization's ethics & compliance program and efforts have increasingly focused on values, not just rules.

56%

78% of high performing organizations agree, compared to **36%** of low performing organizations

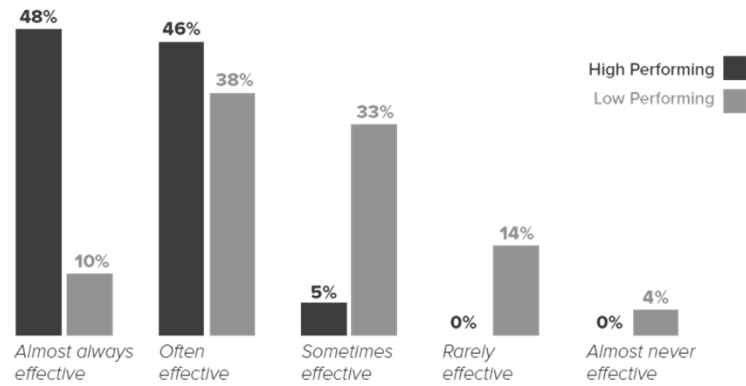| To a great degree	Somewhat	Very little	Not at all
56%	30%	11%	3%
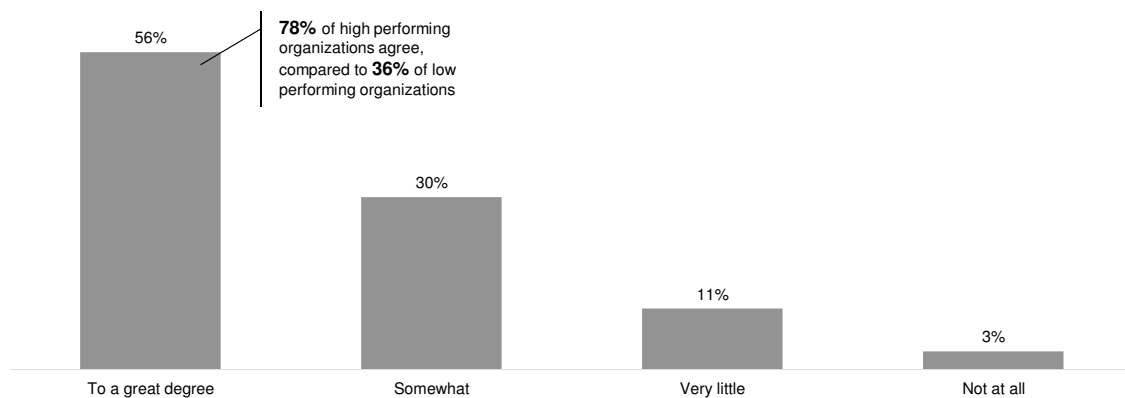
LRN Inspiring Principled Performance
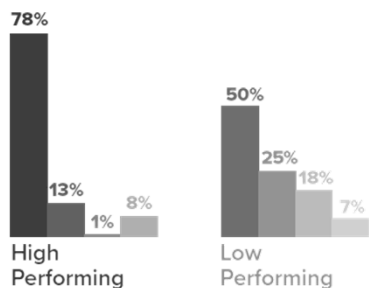
Source: LRN 2018 *E&C Program Effectiveness Report*

8

4

Indicate how you would characterize the effectiveness of your organization's E&C program as a business enabler (e.g., provides advice/counsel, enables better decision-making):
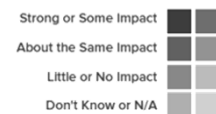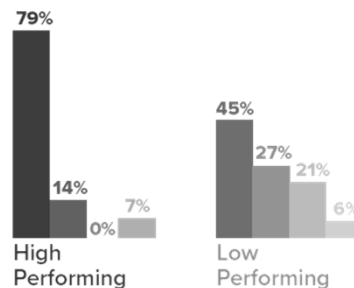
High Performing
Low Performing

	Almost always effective	Often effective	Sometimes effective	Rarely effective	Almost never effective
High Performing	48%	46%	5%	0%	0%
Low Performing	10%	38%	33%	14%	4%

Source: LRN 2018 *E&C Program Effectiveness Report*

9

Compared to last year, rate the impact your organization's E&C program has had on each of the following:

Employees recognizing and reporting misconduct

High Performing: 78%, 13%, 1%, 8%
Low Performing: 50%, 25%, 18%, 7%

Levels of speaking up/out

High Performing: 79%, 14%, 0%, 7%
Low Performing: 45%, 27%, 21%, 6%

Strong or Some Impact
About the Same Impact
Little or No Impact
Don't Know or N/A

Source: LRN 2018 *E&C Program Effectiveness Report*

10

You manage what you measure….

What CECOs say….

"There are few ways businesses can get away with reporting on activity because business is about outcomes, but we haven't translated that to ethics and compliance."

"We absolutely need to have [culture metrics]. Culture is 90% of the work."

"We don't do culture diagnosis… Management and the board think they know the company culture but then are … surprised when something goes wrong."

Source: LRN *The Role of Boards in Overseeing Corporate Ethics & Compliance*

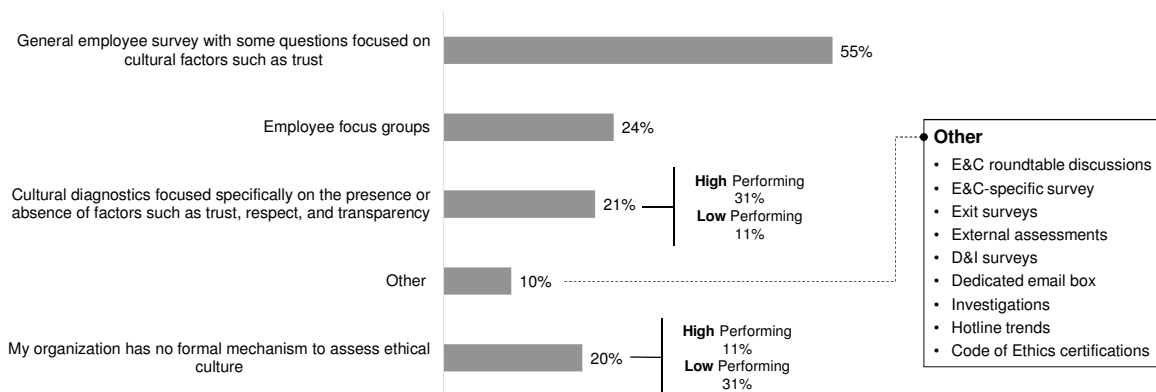# How do you measure culture?

The strongest E&C programs feature regular evaluation

Which of the following methods does your organization use to assess its ethical culture? (check all that apply)

General employee survey with some questions focused on cultural factors such as trust — 55%

Employee focus groups — 24%

Cultural diagnostics focused specifically on the presence or absence of factors such as trust, respect, and transparency — 21%
High Performing 31%
Low Performing 11%

Other — 10%

My organization has no formal mechanism to assess ethical culture — 20%
High Performing 11%
Low Performing 31%

Other
- E&C roundtable discussions
- E&C-specific survey
- Exit surveys
- External assessments
- D&I surveys
- Dedicated email box
- Investigations
- Hotline trends
- Code of Ethics certifications

LRN *Inspiring Principled Performance*

Source: LRN 2018 *E&C Program Effectiveness Report*

14

What you measure matters

Traditional Program Assessments

- Evaluate program design and implementation
- Track lagging indicators
- Do not gauge underlying causes
- Try to assess risk as a function of observed misconduct

Engagement Surveys

- Focus on work enablers and barriers
- Assess satisfaction with the employee experience

Ethical Culture Assessments

- Consider how behaviors and decisions are shaped and enabled by values, culture and leadership
- Surface the behavioral antecedents of misconduct
- Identify sub-cultures, exemplars, and pockets of risk with precision
- Communicate to employees the organizational commitment to ethical behavior

---

So what should you measure?

To protect reputation and propel growth, organizations must go beyond program design to encompass interdependent forces operating at different levels of an organization.
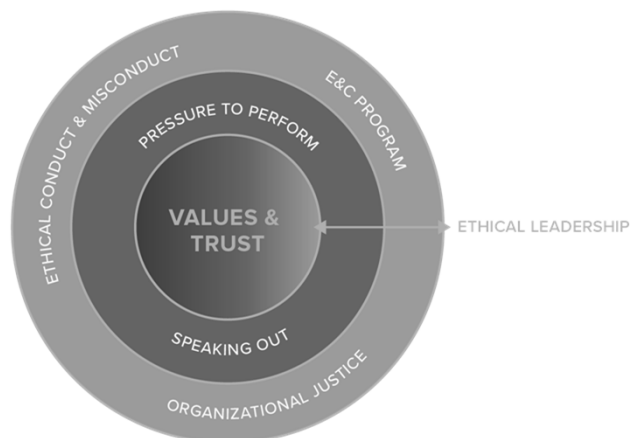
Suggested metrics

PROGRAM ACTIVITY
Does the E&C program resonate with employees? Is it useful and relevant to their roles?

VALUES-ORIENTATION
Do values guide behavior and decisions, and to what extent?

TRUST
Are relationships marked by trust in all directions?

ETHICAL LEADERSHIP
Do leaders model values and reinforce the importance of ethical behavior?

ORGANIZATIONAL JUSTICE
Are standards of conduct applied appropriately and consistently?

SPEAKING OUT
Do employees voice their opinions or report improper behavior? If not, why not?

PRINCIPLED PERFORMANCE
How do people behave when they are under pressure?

RETALIATION
Do people experience retaliation when they report misconduct?

ROI (return on insights)

Develop a deliberate E&C strategy and roadmap

Prioritize training

Hone leadership communication

Proactively address risks

Demonstrate effectiveness to business leaders, regulators, and audit committees / boards

Engage employees and create a wave

Breakout

Let's hear from you

1. How does your organization gain insight into your ethical culture?
2. What have you learned?
3. What has your organization done differently as a result?
4. In what ways has your E&C function been involved?
5. What has been the impact (or what do you expect the impact to be)?

Case studies

Example #1

Company profile
Industrial manufacturing company with 6,000 employees in the U.S. and Mexico

Organizational context
Rapid growth and diversification through acquisition

Assessment objectives
Baseline ethical culture and program effectiveness to inform E&C strategy

Say "our education and training has prepared me"

Think the Code of Conduct is relevant and useful

Are confident mgmt. handles reports appropriately

65% Know how to access the hotline

Only **46%** of those with less than one year of tenure

ACTION
- ✓ "Speak Out" campaign
- ✓ New hire training and onboarding

One business unit **stood out**

consistently scoring **10% lower** than the next and up to **30% lower** than the highest-performing business unit

ACTION
- ✓ Targeted training
- ✓ Incorporate culture into M&A due diligence

LRN Inspiring Principled Performance

22

11

Example #2

Company profile
Private health and wellness company with about 10,000 employees in the U.S.

Organizational context
Founder-led with strong values, experiencing rapid geographic expansion

Assessment objectives
Inform the strategy of the newly-formed ethics and compliance function

Employees are inspired by the **mission and purpose**

Values resonate and are a key driver of recruitment

Say the company pursues growth at the expense of employees

Feel pressured to achieve objectives even if in conflict with values

" I think we believe patients are first….as long as (we're) making enough money.

" We have struggled to maintain a culture of ethics, honesty, value, etc. in our growth.

ACTIONS

✓ Bottoms-up development of a behavioral framework
✓ Deliberate leadership modeling, including:
  ✓ Executive alignment
  ✓ Inspirational leader video
  ✓ New team norms
✓ Experiential, manager-led workshops with all employees to contextualize values to their day-to-day

LRN *Inspiring Principled Performance*

23

Example #3

Company profile
Manufacturing and sales organization with 3,800 employees worldwide

Organizational context
Transitioning from legacy operating model to the standardization and product focus required for scale

Assessment objectives
Understand the cultural factors contributing to a speak out problem surfaced by internal employee surveys

Employees are inspired by the **mission and purpose**

Most people **do the right thing**, even under pressure

Employees are **highly engaged** in helping the company be its best

Key drivers of low speak out culture:
• Lack of leadership **transparency** and accountability
• Mistakes **not accepted**

55% Experience a high level of **trust**

Leaders not **effectively modeling** ethical behavior

40% **Do not report** misconduct when they see it

ACTIONS

✓ Focus groups in high- and low-performing locations
✓ Speak out campaign and manager training on
  ✓ Executive alignment
  ✓ Inspirational leader video
  ✓ New team norms
✓ Experiential, manager-led workshops with all employees to contextualize values to their day-to-day

LRN *Inspiring Principled Performance*

24

When should you measure ethical culture?

Proactive

- To establish a baseline
- New program leadership
- Prior to program strategic planning
- Following a major E&C initiative (e.g., a new Code)
- During or after major organizational change
- To demonstrate program effectiveness to regulators, auditors or boards

Reactive

- Following serious violation of Code or standards of conduct
- To understand patterns in misconduct or reporting data
- To demonstrate program effectiveness to regulators, auditors or boards

LRN Inspiring Principled Performance

25

QUESTIONS?

Reach out and say hi
emily.miner@lrn.com

26

Want to lend your voice to E&C program effectiveness?

Participate in LRN's *2019 E&C Program Effectiveness Report*
Click <u>here</u> to take the survey or go to <u>https://bit.ly/2rjHczL</u>

THANK YOU

LRN Inspiring Principled Performance