

Corporate
Governance



A robust dialogue
with members of
the executive
board



Mastering culture and conduct



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Introduction



Debby Jannink
*Partner Change &
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Renewed focus on culture and conduct

In recent years the relevance of culture and conduct for members of the supervisory board and regulators has increased dramatically. The financial crisis and recent events in the business world and semi-public sector have prompted a review of ethical standards, shared values, integrity and sensitivity in the wider context. Organisations must fulfil the expectations of stakeholders. The latter will scrutinise the former's strategic ambitions, standards and values, requiring a social attitude and a wide-ranging protection of interests, which goes beyond merely ensuring financial returns. Stakeholders are also increasingly addressing members of the executive board and supervisory boards publicly on the organisation's conduct, aided by the transparency and accessibility of social media.

Tone at the top, in the middle and at the bottom

Increased attention towards culture and conduct helps to prevent internal problems of integrity, such as bribery or corruption, or to highlight this early on. A poorly developed sense of ethical standards at the top will also influence the ethical stance of staff throughout the rest of the organisation. Consequently, members of the supervisory board must be aware of not only the tone at the top, but also the tone throughout the middle and bottom layers.

High on the agenda of members of the supervisory board

Insufficient attention to culture and (undesirable) conduct within an organisation entails significant risks, vis-à-vis the internal control, reputation, competitive position and continuity of the organisation. After all, culture affects the speed and flexibility within which organisations can capitalise on developments.

Monitoring continuity constitutes one of the most important tasks of members of the supervisory board. Hence monitoring culture and conduct is now an indispensable item on members of the supervisory board's agenda.



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This trend is also reflected in the regulations for governance and standards for risk committee members of the executive board. The most recent revision to the Dutch Corporate Governance Code asks members of the supervisory board to do their bit towards implementing a culture geared towards long-term value creation. The most recent version of COSO ERM¹ cites culture as an essential factor in successful risk committee members of the executive board.

Re-opening debate in the Dutch boardroom

Despite these developments, members of the supervisory board often still struggle in practice when it comes to monitoring culture and conduct. They are not keen to put themselves in the shoes of the members of the executive board, regarding culture as a slippery topic; and find it hard to discuss undesirable conduct, as was evident from a previous study carried out by PwC². Furthermore, members of the supervisory board frequently do not appear to know how to: drive solid information about culture and conduct into the open; understand what hidden signals they need to pay attention to; and how to make contact with internal and external stakeholders, so as to ascertain what is going on inside and outside of the organisation.

Six sample dialogues

This booklet offers practical guidelines to help members of the supervisory board create culture and present a topic for discussion, across all aspects of business. The booklet consists of six sample dialogues by members of a supervisory board. By asking the right questions and by having the courage to keep asking questions, even when presented with sensitive issues or unsatisfactory answers, are key to fostering a solid debate about culture and conduct within Dutch boardrooms. This will give members of the supervisory board a handle on this present-day, yet delicate, supervision topic.

We hope that this booklet will inspire members of the supervisory board to engage in a relevant and robust dialogue on this subject with members of the executive board and other stakeholders.

¹ COSO Enterprise Risk
Members of the executive
board – aligning risk with
strategy and performance
(June 2016)

² Reappraisal (2012).

Culture and conduct do what you'll say you'll do

Walk the talk

Culture in an organisation means answering the following questions: 'Who are we as an organisation? What do we stand for? and How do we do things?'

Culture is formed by the messages staff receive from the organisation's leaders with regard to the type of behaviour that is desired. This is as much about action as it is about walking the talk. Talking without walking is counterproductive. Such conduct is soon challenged by internal and external stakeholders.

Having a strong foundation internally, builds confidence externally

Internally, culture provides members of the executive board and staff with a basis, when it comes to day-to-day conduct and dealing with dilemmas; externally, a solid culture has the capacity to contribute towards fostering trust amongst stakeholders.

Culture is not like the latest diet or fitness fad. Neither is there a one-size-fits-all culture. A strength in one company's culture (e.g. security and controls in a risky technical environment) could be a weakness in another company's culture (e.g. in a service provider, where flexibility and customer focus are the be-all and end-all).

'Culture is not like the latest diet or fitness fad'



How deep is the gap between the desired culture and the actual culture?

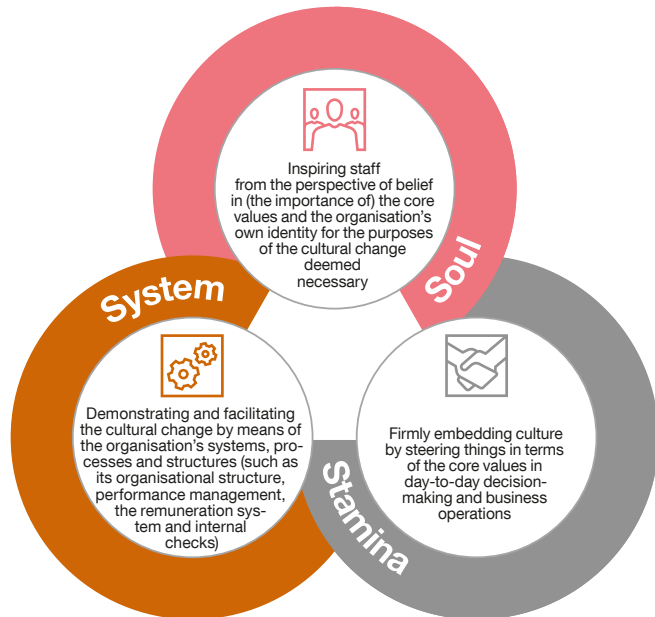
Monitoring culture starts with asking what one wants the culture to be like and the accompanying conduct. The answer can be compared to the situation as it actually is: how deep is the gap between the defined standards and values and their implementation in practice? Three leadership dimensions characterise the steering and monitoring of the change process for the desired robust culture³ (see Figure 1):

- the exemplary conduct of the leaders in the organisation, derived from the central value system (*Soul*);
- the symbols and decisions used when it comes to decisionmaking (*System*);
- the processes, structures and systems of the organisation, such as remuneration and appointments policies (*Stamina*).

The result is a coherent context in which people are encouraged to exhibit good conduct and ostensible conflicts of interest are a topic for discussion.

³ A 'strong' culture does not necessarily have positive connotations. An unhealthy, undesirable culture can also be exceptionally strong, in the sense of intractability. Nevertheless, the term 'strong culture' is used in a positive sense in this publication.

Figure 1 The three dimensions of leadership in cultural change.



Unity in diversity

The majority of organisations encompass a variety of subcultures. Straightforward examples include the specific cultures of those who sit in 'line', 'middle' and 'leadership' levels. These subcultures are necessary to give people sense of belonging within the organisation and to improve their performance. Furthermore, as is often the case within international organisations, the local organisation sets up subcultures, due to the geographical distance from the headquarters, as well as the local culture of the different territories in which the organisation operates. Despite these differences, it is important for all these subcultures to feel connected by the same core values.

Culture as a unifying factor

Explicit focus on culture and conduct results in increased cohesion within the organisation. It is clear what the organisation stands for. All staff in the organisation know how they are contributing towards accomplishing the higher goals, fulfilling the expectations of the most important stakeholders and creating the desired outcome. There is clarity regarding structure, roles and responsibilities and there are unequivocal agreements in place as to what constitutes constructive conduct and what does not. Moreover, the organisation is capable of capitalising on change.

Six fundamental principles for a strong culture

- 1 Culture and conduct are **regarded as being of strategic importance** at the level of the executive board.
- 2 There is a **core value system**, which has been translated into exemplary conduct, symbols and decision-making and processes, systems and procedures.
- 3 People at all levels within the organisation know how they have to act and feel **responsible for their conduct**.
- 4 **Essential conduct at 'moments of truth'** (critical decisions and interaction with stakeholders of decisive importance for external perception and reputation) has been set out in lucid terms and fine-tuned to goal, vision and value system.
- 5 Successful organisation realize that leadership driven by values permeates all levels: **'tone at the top, in the middle and from the tail'**.
- 6 All staff are reading from the same page and there is **no difference between desired and actual conduct**. The conduct is measurable and a topic for discussion.

How robust is the culture in your company?

Use this checklist as a quick test

Exemplary conduct	Symbols and decisions
<ul style="list-style-type: none"> • Are the purpose and values of the organisation clear? 	<ul style="list-style-type: none"> • How does the organisation ensure that leaders act in accordance with the purpose and values?
<ul style="list-style-type: none"> • Is it clear to everyone who the external stakeholders are and what is important to them? 	<ul style="list-style-type: none"> • Which values have genuine value?
<ul style="list-style-type: none"> • Who are the role models within the organisation? How do people deal with one another formally and informally? 	<ul style="list-style-type: none"> • How is this evidenced by the leadership? What is being given priority? What point is always getting dropped from the agenda?
<ul style="list-style-type: none"> • Are the leaders living examples of the organisation's purpose and values? 	<ul style="list-style-type: none"> • Is diversity monitored (mixed-sex and multicultural aspects)?
<ul style="list-style-type: none"> • Is there inspiration? Is there unity? Is there transparency? From what is this evident? 	<ul style="list-style-type: none"> • How do performance reviews work? How are people assessed? How are people rewarded or punished for contributing or failing to contribute towards the purpose and values? How far does the organisation go in this regard?
<ul style="list-style-type: none"> • Do decisions that are made also get implemented? Are agreements adhered to? 	<ul style="list-style-type: none"> • How do you make difficult decisions? How do you cope with dilemmas? Are you transparent about these with all stakeholders?
<ul style="list-style-type: none"> • How do you ensure cohesion and a shared sense of values throughout the organisation? Are the subcultures within the organisation reinforcing or undermining the transition to the desired culture? 	<ul style="list-style-type: none"> • And to get down to basics: Who parks where? Who occupies what office?
<ul style="list-style-type: none"> • Do any non-standard rules or special privileges apply to leaders and their inner circles: do they feel that they are 'above the law'? 	
<ul style="list-style-type: none"> • Are the leaders open to criticism and questions? 	
<ul style="list-style-type: none"> • What happens if mistakes are made? How does the organisation learn? 	

Symbols and decisions

- Is the organisational structure and set-up in line with the purpose and values of the organisation?
- Where are the responsibilities vested?
What authorisations are where and are the limits clear?
- What does planning and budgeting look like?
What does management information look like?
- What is actually being measured?
What is being reported on?
- What does risk management look like? Is there a compliance role? How do the internal checks work?
- What is contained within the codes, rules and regulations? Is there a whistle-blower scheme?
- Do the supporting roles act as a single unit in the interests of the organisation?
- Do the supporting roles constitute a fully-fledged discussion partner for the business?



How do you make culture a topic for discussion?

Encouraging desired conduct

The supervisory board is an employer, supervising and sounding board for members of the executive board. In each of these roles the supervisory board – as well as each individual supervisory board member – should encourage the desired conduct and influence the formation of a robust culture within an organisation, including the culture within the executive and supervisory boards themselves. It is important for members of the supervisory board to be aware of this responsibility and act accordingly. The starting point for making culture and conduct a topic for discussion is a dialogue with the executive board during the supervisory board meeting.

Problems of integrity cannot be prevented by rules alone

Nevertheless, members of the supervisory board frequently fail to adequately address the executive board on culture and conduct in a fundamental way. If the topic is on the agenda, the supervisory board usually concentrates on technical and material measures, in terms of internal members of the executive board and control, to mitigate the risk of undesirable conduct in the organisation. Problems of integrity cannot be prevented by rules alone, however, nor can rules impose a sense of social relationships.

Integrity is also a point requiring attention when it comes to fundamental choices for the future. How objectively have these choices been substantiated? Are the feasibility arguments put forward plausible? Are the right questions being asked? Are the right agreements being made? Are the leaders involved sufficiently experienced to take responsibility?

Addressing them not only on the what but also on the how

Members of the supervisory board can observe culture and conduct more effectively, by focusing on monitoring the organisation's value system and making it more visible: what does the organisation stand for, and to what extent are the values and standards being lived up to in practice? This requires members of the supervisory board and regulators from all organisations (public or private, large or small) to be capable of making culture and conduct a topic for discussion, for example by discussing the way in which results have been achieved, in addition to the results themselves.



Three good practices for dialogue with board members

1 *Maintain professional distance*

Members of the supervisory board sometimes think that expertise is required for a productive dialogue about culture and conduct. In-depth knowledge of the topic is not necessary, however. This could even be a pitfall. Members of the supervisory board, keen to understand everything, could start to feel overly involved in the organisation. Rather, the members of the supervisory board should be asking specific questions targeted more towards the 'how' than the 'what': How have choices been justified? Which stakeholders and which interests have been factored in? How have things been thought through?

How are conflicts of interest dealt with in practice? Which scenarios have been discussed in that respect? Which risks have been identified? How is consistency between words (purpose and values) and actions (practice) monitored? In this way, members of the supervisory board can, with the requisite professional distance, set guidelines regarding the extent to which the organisation honours its own standards and values, whilst protecting stakeholders' interests. This ensures that the members of the supervisory board remain in their role and keep members of the executive board in their role too.

2 *Fix the roof while the sun is shining*

Engage in dialogue with members of the executive board before unhealthy culture or undesirable conduct reaches crisis point. This calls for permanent vigilance of potential integrity issues. Harvard professor Max Bazerman refers to this as the 'predictable surprise'. Perhaps (for example) it was predictable that inadequate insurance policies would lead to claims and forming cartels would result in punitive measures once these were outlawed. Members of the supervisory board can remain more alert to these kinds of predictable surprises, for example by being quicker to ask the specific question: 'do we also have an unfair policy or cartel?'⁴ Or: How do we capitalise on (social) trends such as diversity or sustainability?

3 *Be proactive, but not offensive*

Effective monitoring benefits from a mutual relationship of trust between the executive board and the members of the supervisory board. Making culture a topic for discussion and addressing members of the executive board on undesirable conduct should not be allowed to have an unnecessary detrimental effect on that trust, as the member of the executive board will perceive the supervisory board member's instigation of the debate to be offensive. The more frequently culture and conduct are discussed and dialogue therein is institutionalised, the more likely it will start to become a regular topic. Supervisory board members will subsequently be able to function as a sounding board, as well as a source of inspiration, for members of the executive board, when it comes to culture and conduct.

⁴ This passage is based on an interview with Jaap van Manen in his capacity as Chairman of the Monitoring Commission Corporate Governance Code, published in Governance Update, 11 February 2015

Practical guidelines for robust dialogue

‘Decision-making is often focused on the financial aspects and the commercial risks rather than on consistency with the core value system, the impact on culture and conduct or the external environment.’

No separate agenda item

No separate agenda item is required, let alone an additional meeting, to engage in a dialogue about culture and conduct with members of the executive board. Unless there is a crisis caused by undesirable conduct, necessitating a cultural change to restore reputation and safeguard continuity.

Added value of asking about value(s)

It is precisely to prevent this that culture and conduct must be made explicit and fully integrated into business operations: in each and every strategic choice, investment decision, takeover or product innovation.

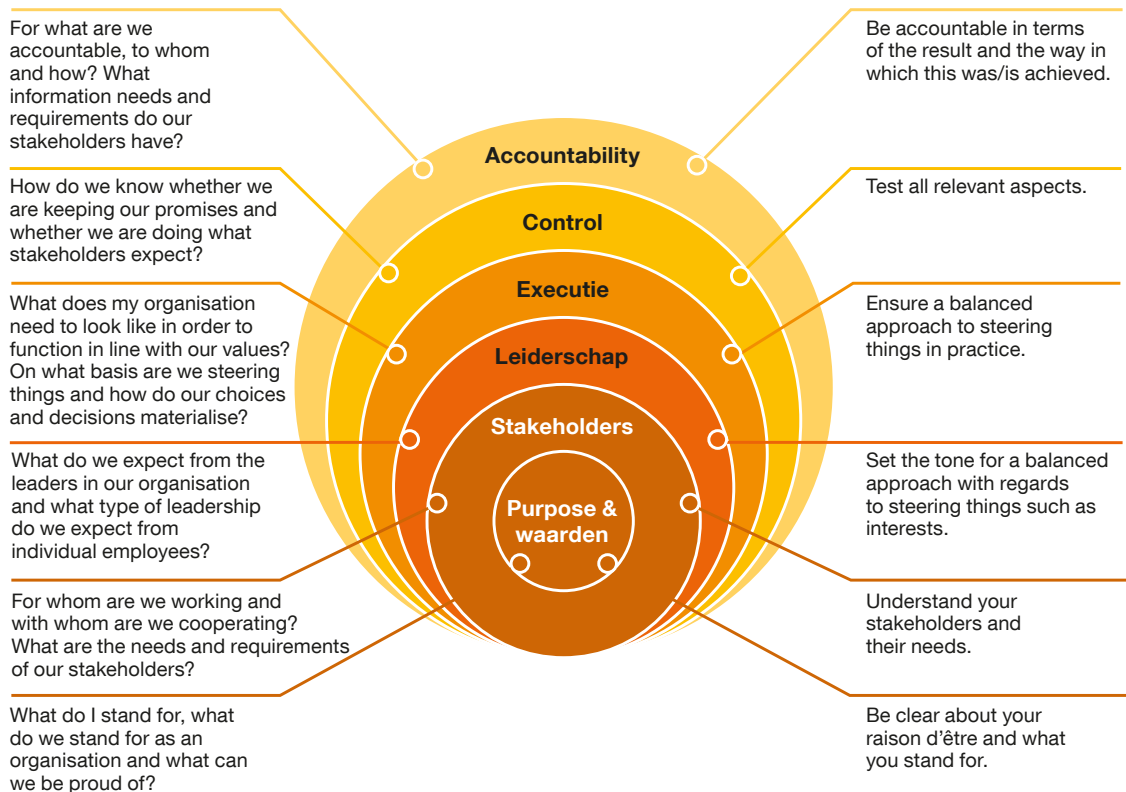
All topics that are usually subject to intense discussion with the supervisory board. Nevertheless, decision-making often focuses on the financial aspects and the commercial risks rather than on conformity with the core value system, or the impact on culture and conduct or the external environment.

The supervisory board member can add value, precisely by raising these questions for discussion as well. Particularly at the present time, when organisations are faced with social choices requiring a fundamental approach, such as an ageing population, diversity and sustainability.

Six dimensions for the integration of culture and conduct into business operations

One practical guideline, to this end, is the integration model: six dimensions for the integration of culture and conduct into all aspects of business operations, plus accompanying core questions (see Figure 2).

Figure 2 Integration model for culture and conduct: the six dimensions



‘Leaders have to indicate what conduct they expect from their staff and lead by example.’

From the inside to the outside

The direction of application of the integration model is from the innermost layer to the outermost layer; after all, organisations are first presented with the task of shouldering responsibility for their culture and conduct, before they can be held accountable for these things. The six dimensions:

1. Purpose and values

A clear purpose is an engaging vision of the organisation’s *raison d’être*, constituting a response to the question ‘where are we headed?’ It is from the perspective of this higher goal that core values and business principles emanate.

2. Stakeholders

In order to put stakeholder interests centre stage, organisations first need to know who their most important stakeholders are and what their expectations or requirements are. To this end, organisations should think from the outside to the inside, engage in continuous dialogue with stakeholders and inventory and prioritise the interests of stakeholders. Stakeholders often have conflicting interests; the organisation can weigh

these up against one another and against the organisation’s own purpose and values and make choices accordingly.

3. Leadership

The transition from current culture to desired culture (and the balanced protection of interests of those stakeholders that are part of it) calls for solid leadership: leaders must indicate what conduct they are expecting from their staff, even leading by example (‘walk the talk’), bolstering the culture and conduct change, by means of appropriate symbols and concrete decisions and embed these within the structures and systems. We encountered this earlier, in the description of the essential characteristics of a robust culture.

4. Execution

Fancy words are not enough, however; purpose and values and desired culture and conduct need to be integrated into the value-creation process. After all, only then will it be possible to steer things efficiently, consistently and transparently. Consequently, culture and conduct will have to be translated into quantified KPIs (key performance indicators) and KBIs (key behavioural indicators).

KBIs are derived from the conduct aspects towards which the organisation would like to move and indicate the extent to which staff are exhibiting the desired conduct. KPIs and KBIs make it possible to manage, measure and monitor cultural and conduct changes.

5. Control

Permanent testing of the framework of standards must clarify how successfully the organisation is transitioning to the desired culture and fulfilling stakeholders' expectations. The compliance officer navigates the organisation towards conduct that complies with the requirement of integrity, the internal auditor holds a mirror up to members of the executive board and the members of the supervisory board monitors the wide-ranging consideration and protection of interests. Good testing generates internal feedback to enable more targeted steering in terms of culture and conduct as well as information for the purposes of external reporting. Furthermore, a robust culture usually also entails bottom-up control: members of the executive board and staff expect to be addressed on the way in which they

are putting purpose and values into practice.

6. Accountability

The way in which the organisation makes itself accountable must dovetail with the purpose and core values formulated. Here too the imperative to 'walk the talk' applies: if the organisation is keen to be open and transparent, is striving towards wide-ranging protection of interests and wishes to create lasting value, then this also needs to be evident in its reporting.

An integrated report tells how organisations are *creating value in the short, medium and long term* for its stakeholders, by presenting a description of their key objective, business model, external environment, strategy, assurance within the organisation and expectations for the future. In their supervisory board report, members of the supervisory board can account for their monitoring of culture and conduct, what issues played a role in that regard, and how they addressed these.

'Good testing generates internal feedback to enable more targeted steering in terms of culture and conduct as well as information for external reporting purposes.'

Testing cohesion and consistency

During the integration process, and as follow-up to dialogue with members of the executive board, members of the supervisory board must test the extent to which culture and conduct have been integrated into the company's operations.

The table below (Figure 3) will help with testing. The table links the consistency and interdependence between the dimensions from the integration model at a glance. Depending on the progress of the integration process, the challenge will reside more in the internal organisation ('inside') or in the external justification ('outside').

Members of the supervisory board at organisations still heavily involved in the integration process, can work through the model from top left to bottom right. Members of the supervisory board at organisations already further into the integration process, can focus on one of the six dimensions and from that perspective test the consistency with the other dimensions. For each combination, the table specifies the core question that members of the supervisory board can put to the members of the executive board. The translation of stakeholder focus into leadership could generate such questions as: Are the leaders reliable in the eyes of stakeholders? To take another example, integrating purpose and values within the execution. The salient question here is: Are purpose and values tangible within the value-creation process?

Figure 3 Testing cohesive and consistent

	Purpose and values
Purpose and values	Are we clear about our raison d'être and what we stand for?
Stakeholders	
Leadership	
Execution	
Control	
Accountability	

embedding of culture and conduct at a glance

Stakeholders	Leadership	Execution	Control	Accountability
Do we know where our interests are in line with or in conflict with those of our stakeholders?	Do our leaders understand the set objectives and how these tie in with the intended long-term value creation?	Is our organisation functioning in line with our purpose and values?	Are we translating our purpose and values into controls?	How are we accounting for accomplishing purpose and values?
Do we have relationships with all of our stakeholders and are we familiar with their needs?	Do our leaders know what our stakeholders expect from us?	To what extent are we involving our stakeholders in the way in which we are implementing our purpose and values?	To what extent are we capable of fulfilling our promise to our stakeholders?	For what things are we accountable to stakeholders?
	Are our leaders setting the tone for balanced steering towards long-term value creation and are they fostering a culture of openness and approachability?	Are we giving our leaders the right incentives to steer things in a balanced manner?	Are we giving our leaders the right incentives to steer things in terms of interests?	How are our leaders justifying the way in which they are steering things in a balanced manner?
		Are we ensuring a balanced approach to steering things in practice?	Do our performance reviews constitute a living example of the desired culture? Is the culture a subject of review?	How are we reporting on the way in which we are implementing our purpose and values?
			Are we testing all relevant aspects?	Are we making it clear how testing will be done and what factors should be tested?
				How are we accounting for the result and the way in which this was achieved?

Dialogue in the boardroom: six sample dialogues

Fundamental questions and sensitive issues

Engaging in robust dialogue with members of the executive board on culture and conduct is not always easy. After all, the questions that members of the supervisory board will ask on this subject are critical and will sometimes broach sensitive issues. Members of the executive board might not be able to (or not be immediately able to) answer some questions and may consider them to be disruptive, bothersome or irrelevant. In such cases they may well wish to dodge the discussion, by giving a non-committal or self-evident answer, hide behind other parties, or offer exceptional circumstances as an excuse or explanation.

No pain, no gain

The job of the members of the supervisory board is to not put up with vague answers and to keep asking questions, even when presented with unsatisfactory or evasive responses. In this regard, it could help to point out the pain (disadvantage) and gain (advantage) of an undesirable culture versus a desirable culture, as well as how this can be avoided or achieved. In order to facilitate the debate with members of the executive board, we have fleshed out each of the integration model to produce *sample dialogues* (zie pag. 22).

Aspects of business management

Each dialogue focuses on cultural and conduct-related elements of one aspect of business operations (purpose & values, stakeholders, leadership, execution, control and accountability). In total, there are six sample dialogues for each dimension of the integration of culture and conduct. What constitutes the most suitable dialogue will depend on the specific cultural and conduct problem in the organisation. It will also depend on the progress of the process of integrating culture and conduct into the business operations. Members of the supervisory board at organisations still right at the start of the integration process, would do well to begin with the first dialogue and finish with the sixth. Members of the supervisory board from organisations already further along the integration process, should select the dialogue which corresponds to the aspect with the same name in the integration model.

Ammunition needed to persevere with questioning

The starting point for each dialogue is a fictional though realistic and recognisable scenario, followed by questions that members of the supervisory board could ask in that regard. The dialogue also contains potentially evasive answers from members of the executive board, as well as 'ammunition' for the supervisory board member, to ensure continuous and open dialogue about the advantages and

disadvantages of healthy (or unhealthy) culture and desirable (or undesirable) conduct.

First understand the scope of the problem

Members of the supervisory board are also human, and when faced with problems, can be tempted to go along with solutions put forward by members of the executive board, without ascertaining whether the observations and/or the analysis are accurate and exhaustive. The upshot of this is that often a technical solution is chosen without people fully understanding the issue. The trick for the members of the supervisory board is to maintain a certain distance in such cases and to focus on the quality of the analysis. A good way of opening the discussion in this case, as well as cutting through (any) evasive answers, is to ask about the extent of the problem and request that the appropriateness of the proposed solution be substantiated.

Questions to fall back on:

- What has been done to compile an accurate and complete picture of the problem (root cause analysis)? And has the cause and therefore the entire issue now been mapped out?
- Does the proposed measure fit in with the objective we wish to achieve? And does the measure suit us?
- How can we ensure that the measure will genuinely have the right effect too? (Will amending a procedure really suffice?) How are progress and efficiency being monitored?
- What adjustments to the internal controls will be required?

Strategy that works - Strategy&

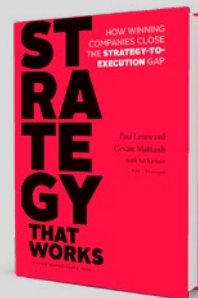
The booklet, 'Mastering culture & conduct', examines the way in which one can get a handle on a culture by integrating it into the strategy. 'Strategy that Works' allows one to grasp strategy by recognising the culture as an important tool.

'Strategy that Works' is geared towards creating/ change in the organisation to further enhance (the) executive power.

'Strategy that Works' distinguishes five principles that provide guidance on 'how' to do this, with culture playing a significant role in this respect.

Successful organisations give meaning to the five principles by consistently exhibiting the desired conduct in all activities of the business, by:

1. adopting exemplary conduct and making it explicitly in line with the culture and
2. the long-term objectives, making culture explicit in day-to-day operations and
3. nurturing informal leaders.



'Focus on understanding the problem rather than finding a solution'

Sample dialogue 1

Purpose & values

What do you stand for as an organisation and what are you proud of?	
Situation	Within the organisation, has the policy with regard to long-term value creation been fleshed out clearly on paper? As a member of the supervisory board you will be keen to know whether the policy is in line with the purpose and values and whether it is being implemented as powerfully in practice as it is in writing.
Questions	<ul style="list-style-type: none">• How was this policy created? Who was involved in that process?• How is the connection with purpose and values being safeguarded?• How have conflicts between policy and purpose and values been dealt with?• What role did you yourselves have in this, in the capacity of member of the executive board?
'Evasive' answer from members of the executive board	<p>'I'm fully behind it, that goes without saying.'</p> <p>'Sure, but we're in this for profit, we're not a charity.'</p>
Return	Risk
<ul style="list-style-type: none">• What needs to happen to harmonise the purpose, with the values, policy and execution?• What will be the effect if the purpose and values are clear throughout the organisation and to all stakeholders? (For example, in terms of the positioning of the organisation towards various stakeholders, in terms of the quality of the leadership, the executive power, the cost of control, the accountability, etc.)• Where in the policy is it evident that the purpose and values are given priority?	<ul style="list-style-type: none">• As members of the executive board, how do you know that the policy adopted is in line with the purpose and values?• Were any/all issues discussed when formulating the policy? If so, what? How did you deal with these? What impact did this have on the organisation's risk profile?• What actions were taken to help manage these risks?• How is our governance supporting the purpose and values and the policy (what duties, roles and responsibilities have been allocated and assigned to this end?)• To what extent is the business capable of implementing this policy (is our governance sufficiently clear, are we organised in such a way that its implementation is possible, are our processes and systems strong enough,

Sample dialogue 2

Stakeholders

For whom are you working and with whom are you collaborating? What needs and requirements do your stakeholders have?	
Situation	The organisation is positioning itself to be an ambassador in sustainability within the value chain and explicitly expresses this ambition in formal communication. As a member of the supervisory board you are keen to know how members of the executive board are dealing with the inherently conflicting interests of various stakeholders vis-à-vis sustainability.
Questions	<ul style="list-style-type: none"> • Do we know all of our stakeholders and their interests? • Have we been developing relationships with all of our stakeholders? • Which stakeholder interests have prompted us to position the organisation as a leader of sustainability within the (value) chain? • Are there any conflicts between our interests and those of our stakeholders?
'Evasive' answer from members of the executive board	'Obviously we can't please everyone.' We're doing our best, but it's difficult.'
Return	Risk
<ul style="list-style-type: none"> • How do we involve stakeholders in purpose and values in order to eliminate or mitigate conflicts? • What potential capacity will you be unleashing if you make the differing interests compatible? • How can you ensure that the organisation builds and maintains a relationship with its stakeholders? 	<ul style="list-style-type: none"> • How does the organisation deal with potential conflicts of stakeholder interest? • Is there a clear picture of conflicts? How was this picture formed? By whom? • Is the way in which the organisation deals with these conflicts concrete? • How do we know that we are communicating about these disputes with sufficient clarity?

Sample dialogue 3

Leadership

What are you expecting from members of the executive board and staff?	
Situation	As a member of the supervisory board you are keen to discuss the extent to which the purpose and values are identifiable from the tone at the top as well as the conduct of leaders within the organisation.
Questions	<ul style="list-style-type: none"> • As a member of the executive board, how do you know that good leadership is being modelled within the organisation? • How do leaders ensure that their objectives dovetail and cohere with our organisation's purpose and values? • How do staff - and members of the executive board in particular - know what leadership is expected from them? • What role do you have in this, as a member of the executive board? What feedback are you receiving? • What guidance are you giving to leadership?
'Evasive' answer from members of the executive board	<p>'Yes, we took care of that. HR has got a programme for it.'</p> <p>'That's definitely important, for sure. We'll include it in the assessments.'</p>
Return	Risk
<ul style="list-style-type: none"> • How do you ensure that leadership is approachable and accessible? • How can you involve staff and stakeholders in determining desirable leadership and conduct? • In your own communication, how do you see to it that everyone understands what desirable leadership is? • What do you hope will improve once it is clear what kind of leadership is desirable, in the event of frequently occurring issues? • How is exemplary conduct rewarded? • Has space been made for honest feedback, and is this being monitored? 	<ul style="list-style-type: none"> • What is exemplary conduct on the part of leadership taken to mean? • How is conduct addressed as a discussion point? • How is this determined? Is this known to everyone/all stakeholders? • Are measures taken for unsuitable conduct on the part of leadership? • How do you deal with undesirable conduct exhibited by key talent? • How do you ensure that people are able to raise their issues? • How is this communicated?

Sample dialogue 4

Execution

As a member of the executive board, do you have an overview across all business units? & is this in line with the purpose and values? & are you acting in the interests of all stakeholders?

Situation The organisation comprises various subsidiaries and the parent company sets the overarching strategy and objectives. You are keen to know how desirable conduct is being promoted during its implementation.

Questions

- What operational objectives are associated with the purpose and values?
- How are these embedded within the organisation?
- How are the purpose and values and/or culture and conduct discussed as a topic during performance reviews?
- How are successes celebrated?
- (How) Are best practices shared?

'Evasive' answer from members of the executive board

'Everyone knows what's expected of them.' **'That's not necessary in our culture.'**
'Members of the executive board aren't open to this way of managing things.'
'This would call for a new members of the executive board style or even a different culture, which would be something we'd have to invest in and we don't have the time/money for that.'

Return

- What incentives do leaders have, to exhibit desirable conduct?
- What role do the purpose and values play in this regard? What is the benefit in the short and long term of acting in line with the purpose and values?
- What tools do you offer to encourage desirable conduct?
- What is the role of risk members of the executive board, internal audit and compliance?
- How do you monitor that desirable conduct

Risk

- What incentives can trigger undesirable conduct?
- What risks are run by the organisation if the subsidiaries do not act in line with the purpose and values? How are these risks calculated? Who was involved in defining this?
- What actions have been taken to help manage these risks?
- What control functions exist to monitor progress and to report on this to management or to the board

Sample dialogue 5

Control

As a member of the executive board, do you know whether the organisation is doing what stakeholders are expect?

Situation An international organisation has an entrepreneurial culture, with a considerable degree of autonomy and rapid growth. As supervisory director you are keen to safeguard the continuity and reputation of the organisation and are curious as to how compliance risks are being managed.

Questions

- How are the purpose and values translated into compliance risks and accompanying hard and soft controls?
- To what extent is the organisation capable of managing compliance risks?
- How do we deal with incidents?

'Evasive' answer from members of the executive board

'The organisation's infrastructure and policy are lagging behind the strategy/regulations.'

'More time and money are needed to boost the quality of implementation.'

The priorities within the organisation aren't there at present - we need to grow first.'

Return

- What tools are we giving our people to choose the right focus and make sufficiently judicious choices?
- What incentives are we giving our people to deal with risks in a well-considered manner (i.e. to do business effectively)?
- Going forward, is the extent of managing these risks a topic of discussion in performance reviews?

Risk

- As a member of the executive board, how do you know where the organisation is exposed regarding compliance risks?
- As a member of the executive board, how do you know where and when limits are being reached and/or exceeded?
- Has the potential impact of risks on the business portfolio been outlined?
- How are violations of the risk policy dealt with? What considerations do you use in this regard? How do you communicate on this matter?
- How do members of the executive board form a picture of the impact of these risks on different stakeholders?

Sample dialogue 6

Accountability

**What are you accountable for and how do you account for it?
What information needs and requirements do the stakeholders have?**

Situation

In the capacity of a supervisory board member, you receive a large number of reports from the organisation. These appear to be technically correct and provide plenty of information on the past. Nevertheless, you are keen to acquire a greater degree of insight into how things will progress going forward.

Questions

- Does the way in which we are accountable fit in with what we would like to be as an organisation, e.g. more transparent?
- Are the ambitions of the organisation and the supervisory board in line with the reporting method?
- As a member of the executive board, how transparent do you aspire to be in your reporting?
- How do you strike the right balance in this respect?

'Evasive' answer from members of the executive board

'We don't have any space on the agenda for reporting.'
'The reporting lines are unclear/don't work in practice.'

Return

- How do you know that our reporting satisfies the information requirements and expectations of your stakeholders? (Is any dialogue held on the reporting [content & method]?)
- Does the annual report provide an adequate reflection of the real situation/business?
- Does the reporting (or method thereof) contribute towards trust in the organisation?
- Is importance attached to the information needs of all stakeholders?

Risk

- Do important communication and reporting standards make it clear what the organisation stands for?
- How are key questions from stakeholders handled?
- How are incidents reported?
- How are stakeholders informed about important decisions that have been or are being made?
- How are members of the executive board held accountable? By whom? What role do members of the executive board



Changing and embedding culture and conduct within the executive board

Request follow-up

Monitoring culture and conduct goes beyond merely engaging in dialogue with members of the executive board. After all, serious follow-up is imperative rather than optional, just like the other subjects that the supervisory board discusses with members of the executive board. Supervisory board members will need to ask specific questions about this follow-up and its progress, such as the status of the agreed timetable for cultural change, the role of the members of the executive therein, etc.

Be conscious of (non-verbal) signals

Members of the supervisory board must also be vigilant regarding the culture within the executive board itself: the way in which they are cooperating; the prevailing sense of ethical standards; and common values.

After all, the tone from the top is often decisive when it comes to the culture and conduct of staff within the other levels of the organisation. Members of the executive board have primary responsibility for specifying and embodying the standards and values, by exhibiting exemplary conduct in their decisions and by setting limits, by means of the systems, processes and structures. If moral leadership is lacking or inauthentic, or if the top members of the executive board are even exhibiting, encouraging or forcing undesirable conduct, then this could call for intervention or adjustment on the part of the supervisory board, to influence the culture in the boardroom. Changes in members of the executive board can result in changes to the culture.

‘Members of the supervisory board will need to ask specific questions about this follow-up and its progress.’

Two tools to influence the culture of executive board members



1. Modify conduct at the top through the hiring process

Unsurprisingly, members of the supervisory board view the recruitment process as an important tool, to transform culture and conduct and to close the gap between actual and desired culture. This was evident from a previous study carried out by PwC⁵.

They consider the hiring and dismissal of members of the executive board as one of the best ways of exerting direct influence on conduct at the top. Furthermore, this sends an important message to the rest of the organisation.

Incidentally, the same appointments policy can get in the way of the supervisory board, if a member of the executive board is exhibiting undesirable conduct. After all, they were the ones who appointed that member of the executive board, thus making it harder for them to speak to him or her regarding the conduct in question, or to proceed with dismissal.

2. Reward not only the ‘what’ but also the ‘how’

Members of the supervisory board can also use remuneration to steer culture and conduct. For example, they can see to it that the remuneration system contains qualitative, non-financial performance criteria, in addition to quantitative criteria. Therefore, it is not so much about the absolute level of the remuneration (although this will also have to tie in with the culture), but rather the fit with the organisation’s purpose and values.

It is not only the ‘what’ but also the ‘how’ that should be rewarded. In this way, members of the executive board can be encouraged to also protect the interests of certain parties such as customers, staff and other stakeholders. The rest of the pay structure in the organisation can then be built on this as a foundation.

Members of the supervisory board can also use remuneration to send a clear message to members of the executive board, the rest of the organisation and even the outside world, for example, by withholding the bonus of an executive board member for undesirable behaviour.

⁵ Remuneration, in the Members of the supervisory board’ Toolbox series.

Changing and embedding culture and conduct within the supervisory board

Document the purpose and values in the articles of association, supervisory board members' profiles and appointment records

Monitoring culture and conduct should also be embedded in the set-up and performance of the supervisory board. A strong signal is sent when the board demonstrates how the standards and values are being translated within the functioning of and dealings with members of the executive board. The way in which the supervisory board intends to focus on the organisation's purpose and values, in terms of its actions, can be embedded in formal guidelines for the supervisory board - such as the articles of association, the profiles of supervisory board members and recruitment records. This can be fleshed out in the procedural agreements, stipulating (for example) that the supervisory board will regularly seek to touch base with employees of the organisation and key stakeholders, and will regularly review standard matters related to the recognition of used standards and values.

Integrate culture and conduct into the agenda of the supervisory board

There is a certain degree of regularity in the topics presented to the supervisory board; many of them recur at every meeting or are certainly discussed during the course of the year. Collectively they make up the supervisory board's annual agenda. Culture and conduct can be integrated into this.

Speak candidly without members of the executive board present

Members of the supervisory board should also make culture and conduct a standard agenda point, without members of the executive board being present. Many supervisory boards hold 'executive sessions', which entail them holding preliminary and follow-up discussions prior to and after the meeting. The preliminary discussion should involve them jointly reviewing the requested information and taking action accordingly. The follow-up discussion should involve members of the supervisory board sharing their observations about mutual relationships and the conduct (including non-verbal conduct) of members of the executive board during the meeting; i.e. how do members cooperate; how do people get along with one another; what is the atmosphere like; how sincere does the tone at the top sound; and, besides the tone, whether you can also see it in their eyes?

The supervisory board agenda

Questions about culture and conduct to be integrated into the supervisory board's annual agenda:

1 Strategic policy

- What is the impact of the strategy on the organisation's purpose and values (or the recognition thereof)?
- What is the impact of the strategy on the interests of the different stakeholders?
- How are different divisions of the organisation involved in the strategy?
- Has the strategy been translated into financial and non-financial indicators by means of which the organisation at all levels can render readily visible how results develop?

2 Risk policy

- Do the risk strategy and the risk profile dovetail with the purpose and values?
- What disadvantages have been identified vis-à-vis culture and conduct?
- Do measures go beyond codes, rules and regulations?

3 HR policy (diversity, attracting and retaining talent, education, etc.)

- Have purpose and values been translated into competency profiles?
- How is diversity being fostered and monitored?
- How are staff enabled to model their conduct on the desired conduct?

4

Consultation with works council

- How is the works council being involved in developing the desired culture?

5

Annual plan and budget

- In what way are the purpose and values visible within the planning and budgeting process?

6

Annual report and annual accounts

- Are culture and conduct mentioned in the annual report?
- What will need to be done in order to transition to integrated reporting?

7

Supervisory board's report

- The report makes clear how the board uses purpose and values in decision making



Make culture and conduct a regular part of information gathering

Members of the supervisory board often wrestle with the question of how to acquire an adequate overview of the organisation (including the culture and conduct therein). They realise that they need additional and diverse information, than what they are currently receiving from the executive board. Members of the supervisory board should enquire about the following resources (for example):

- customer satisfaction surveys
- net promoter scores (NPS)
- the complaints department or committee
- the number of reports from whistle-blowers
- data on staff loyalty, staff turnover and absence due to illness
- the staff magazine and intranet
- results of 360° feedback
- the process and the results of members of the executive board assessments
- speeches made by members of the executive board
- the results of dialogue with stakeholders (in order to gain an understanding of stakeholders' expectations and the extent to which the organisation is fulfilling these)
- results of a culture survey: what differences exist between actual and desired culture? (The supervisory board could also carry out such an evaluation itself.)

Structured information on culture and conduct

It is frequently the case that formal sources of information on culture and conduct are unavailable or scarce, even though informal information is often gathered on an ad hoc basis. Being able to monitor culture and conduct requires structured information on how the culture actually is, in addition to the difference between that and the desired culture.

A cultural analysis will generate specific, detailed information that will make it easier to ask tough questions and get relevant answers. Moreover, the results of this will provide members of the supervisory board with an objective picture of the status and thus give them a handle on cultural change: periodic reporting makes it possible to monitor whether the gap between the actual and desired culture is shrinking.

Gather informal information about culture and conduct

Most supervisory boards actively seek out informal sources of information.

This varies from discussions with the second tier and the works council (during and outside of meetings), to speaking with the complaints committee, engaging in site visits and attending events such as directors' conferences, social gatherings and receptions.

This enables members of the supervisory board to obtain answers to questions such as (for example):

- What rumours are going around (about the organisation's history)?
- When it comes to important decisions and dilemmas, are people acting in the spirit of the organisation's standards and values at the various levels of the organisation?
- In the case of minor deviations from common practice: why has this happened and what is the underlying cause?

Members of the supervisory board can also collect informal information from external stakeholders, by attending external events, such as client meetings, or the shareholder meeting, as the board.

Make the composition of the supervisory board diverse

Diversity broadens the perspective within the supervisory board. This is not merely a matter of fostering a balanced ratio of men to women, but also about encouraging diversity in terms of such factors as age, ethnicity,

background and beliefs, thus enabling ‘kaleidoscopic’ supervision: the various perspectives represented within the board will give rise to a more varied, more comprehensive perspective on the expectations of stakeholders and the matters that are important in society. Furthermore, diversity offers a platform to promote engaging debate about standards and values and to enrich the decisionmaking process.

Consider appointing a member of the supervisory board with HR expertise

Financial expertise, legal knowledge and board experience are routinely present within the supervisory board, but experience with human resources is often missing. But, as stated earlier, members of the supervisory board do not require substantial expertise to discuss culture and conduct.

Nevertheless, prior HR expertise can offer added value, particularly if the organisation is facing radical cultural change. An alternative option involves having a direct line to the member of



the executive board who represents the organisation’s HR function

Set up an HR or culture committee (temporarily or otherwise)

If more attention, or a lot of attention, to culture and conduct is required, then setting up a separate Culture or HR committee (temporary or otherwise) should be considered. This would focus specifically on the definition and integration of, as well as compliance with, desired conduct, while fostering the desired culture.

‘Diversity broadens the perspective within the supervisory board.’

‘The compliance officer and the internal auditor are deployed to test the standards framework and function as the organisation’s conscience, as well as a mirror to members of the executive board.’

Regularly sound out the compliance officer, internal auditor and external accountant

The compliance officer and the internal auditor are engaged to test the values framework and function as the organisation’s conscience, as well as a mirror to members of the executive board. This can yield valuable information for the supervisory duties to be performed. The external accountant is also a valuable source of information; the supervisory board can sound him out about his impressions of the organisation’s culture and conduct during a private meeting.



Ten questions on culture and conduct for the external accountant

Members of the supervisory board can also involve the external accountant in monitoring culture and conduct. In this regard, they can share or test their observations during a supervisory board meeting, an audit committee or a private session. What impression does the accountant have of the integration of culture and conduct into business operations and its reliability and structure?

- 1 What is your impression of the control awareness in this organisation?
.....
- 2 What do you think of the extent of risk appetite versus risk enthusiasm?
.....
- 3 Is a suitable balance being struck between hard and soft controls?
.....
- 4 Is there sufficient space to make mistakes and learn from them?
.....
- 5 How are incidents being responded to?
.....
- 6 Is the remuneration and appraisal system providing the right incentives to encourage the desired behaviour?
.....
- 7 Are aspects of culture and conduct being examined adequately and correctly within the compass of the audit of the financial statements?
.....
- 8 To what extent are the core values and codes of conduct embedded in day-to-day practice?
.....
- 9 Does the internal audit plan devote sufficient attention to culture and behaviour?
.....
- 10 How are culture and conduct reflected in your annual reporting?
.....

Additional concluding question:

How are we performing in these areas compared to other organisations?

Include culture and conduct in the board's (self-) evaluation review

During the annual (self-)evaluation of the performance of the supervisory board, culture and conduct should also be addressed: the embedding and documenting of responsibilities; the agreements and procedures for information gathering; ways of working and decision-making; the unwritten rules for culture and conduct; and the group dynamic within the supervisory board. The evaluation can focus on the conduct of the group as well as everyone's individual contribution to it⁷.

Report about the supervision of culture and conduct in the supervisory board report

The supervisory board can also use the 'supervisory board report', which is part of the annual report, to justify supervisory activities in relation to culture and conduct. Maybe as a separate topic - perhaps linked to the analysis of evaluation results - or as an appendix to the supervisory board's activities in terms of business operations. Furthermore, the supervisory board can demonstrate how the board embeds the purpose and values within the scope of decision-making (see also point 7 in the 'annual supervisory agenda'). Inclusion in the supervisory board report renders explicit the fact that the supervisory board attaches importance to monitoring culture and conduct. This sends a clear message to the organisation, members of the executive board and stakeholders.

⁷ See "The Evaluation" pocket booklet in the supervisory board member's toolbox





Changing and embedding culture and conduct in each individual member of the supervisory board

'It is easier for individual supervisory board members to obtain information from the organisation and from important stakeholders, than it is for the entire supervisory board to do so as an entity.'

Pay attention to culture and conduct before accepting a role as a member of a supervisory board

Members of the supervisory board should endeavour to build up a picture of the culture and conduct of the organisation they intend to supervise, before being appointed. They could then ask themselves whether the purpose and values, the tone at the top, as well as the culture in the boardroom, appeal to them. Additionally, they can ask themselves what added value they can offer, for the purposes of monitoring culture and conduct.

Actively gather informal information

Many members of the supervisory board choose, independently of members of the executive board, to immerse themselves in the organisation and to talk with staff and other involved parties, to build up a picture of the culture and conduct for themselves.

In that regard, additional and informal sources of information are sought, so as to give an indication of the conduct exhibited by members of the executive board and the organisation. As stated earlier, official sources – like information acquired by the whole supervisory board – are often insufficient.

It is easier for individual members of the supervisory board to obtain information from the organisation and important stakeholders, than it is for the whole supervisory board to do so as an entity. However, it is advisable for members of the supervisory board to avoid seeking contact with staff or stakeholders off their own back, instead doing so in consultation with the (chair of the) executive board. Furthermore, a degree of care is needed when highlighting and sharing any information obtained internally/externally, without knowing the exact context. Above all, members of the supervisory board would be well advised to listen and not be lured into airing an opinion or taking sides.



Be alert to non-verbal conduct and hidden signals

Careful observation of (non-verbal) conduct and vigilance regarding hidden signs can also provide valuable information and punctually identify problems with regards to integrity, risk and conduct within the culture, or a poorly developed sense of ethical standards. Always keep your eyes peeled and ears open.

Be aware of what is going on in society

Members of the supervisory board bring the outside world in. They need

to have their feelers out to know what is going on in society, what issues and decisions will be sensitive and what expectations stakeholders are harbouring. Members of the supervisory board must thus avoid operating exclusively in either a vacuum, privileged environment or elite circles. Maintaining an overview of culture, conduct and stakeholder interests calls for regular immersion in the real world and communication with people in person: on the tram, at the market or when queuing at the supermarket checkout.



Non-executive director(s) Toolkit

These publications are part of the supervisory board toolbox. This toolbox has been developed by PwC for supervisory directors and consists of various pocketbooks that focus on relevant corporate governance topics. In addition to the theoretical background and trends, the booklets mainly offer practical instructions for your supervisory role.

You can download the pocket-sized booklets of your interest via <https://www.pwc.nl/nl/dienstverlening/corporate-governance/commissaristentoolbox.html>



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