

Tone from the Top

Transforming words into action

Nearly **90%** of survey respondents agree that Tone from the Top is critical in the effective mitigation of risk to their organisation around Fraud, Corruption and Ethical Behaviour

This is yet to translate into a common understanding of what Tone from the Top means and what it takes to transform words into action

Are leaders just playing lip service to ethics?

Develop a risk resilient organisation.
pwc.co.uk/riskresilience

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Executive summary

This survey, commissioned by PricewaterhouseCoopers LLP (“PwC”), has shown a resounding agreement from our respondents that Tone from the Top is vital in developing and maintaining the ethical integrity of the business. Without it, the ability to mitigate the risk of something going wrong is significantly impaired.

The survey demonstrates that there are a wide range of approaches being used to establish the foundations for ethical tone. These include establishing a set of core values and principles, regular communications of ethical values by leadership, and even declining business where it is not aligned with the ethical values of the business. This is encouraging news and positive affirmation that organisations are responding to the emerging and increasing risks around conducting business on an ethical basis across the globe.

However, transforming these words into actions is proving much more challenging

There appears to be a flurry of activity around short term actions without understanding what is required to embed longer term behavioural change. Examples include an absence of measurement of ethical risks, low levels of regular and updated training to enhance awareness and application of ethical standards, a small number of mechanisms in place to recognise and reward good ethical behaviour, and a number of businesses with few or no means by which to gain assurance over their systems and processes to support ethical behaviour.

46% of respondents reported that leadership do not always act as role models in setting the right tone from the top. This may be a judgment based on the perception of individuals and also perhaps the nature of the business and its inherent risks, but it does beg a serious question:

Do you understand what Tone from the Top means and how is this reflected in the existing culture of your organisation?

This report is the first step in a journey towards gaining a better understanding of what Tone from the Top means in reality to organisations and the individuals within it. We will be asking further questions and continuing to develop our thinking that will encourage leaders to define their culture and take responsibility for the integrity of their organisational business behaviour.

- What is the existing culture of your business?
- Who is setting the Tone from the Top in your organisation?
- Are you just paying lip service to ethical behaviours or are you measuring and reporting on the ability of the organisation and your employees to act with integrity?
- How is ownership of the organisational culture permeated to all your employees?
- Should leaders be assessed by their ability to understand the need to act with integrity and deliver the right culture?

Tone at the Top is about creating a culture where everyone has ownership and responsibility for doing the right thing, because it is the right thing to do. Our practical experience and expertise in helping clients define and develop their approach to building an ethical culture has identified the following principles as key to establishing and sustaining the right Tone from the Top:

- Consistent and visible executive sponsorship for ethics and compliance-related issues is not just key, it is mandatory, if change is to occur
- Understand what the prevailing culture is first, before attempting to make any wide-sweeping changes, to inform and drive your Tone from the Top messages
- Leaders must consistently “do as they say”, not “do as they want to do”, in a way that is aligned and enforces the values and ethical standards of the business
- Good behaviours must be rewarded and recognised, poor behaviours must be acted upon and necessary action undertaken, openly and transparently
- Embedding systems and processes to support the Tone from the Top as “business as usual” will help shape the organisational culture and measure the effectiveness of leadership actions and behaviours over a period of time

The aims of the survey

Setting the right Tone from the Top is increasingly viewed as a critical leadership skill in leading and growing successful organisations, whatever the size, location or nature of the business. It is a phrase that is becoming increasingly associated with developing and defining standards of ethical business conduct and the role of leaders in setting the ethical culture, of which managing bribery and corruption risk is an integral part.

PwC has commissioned this survey as part of its commitment to develop the thinking on Risk Resilience for our clients, including the way that leaders of businesses behave and the impact on managing risks, and the preparations that organisations are currently undertaking in light of the new Bribery Act. Tone from the Top is likely to be a key component of the Government's guidance on how to prevent bribery as part of the establishment of Adequate Procedures in the 'failure to prevent bribery' corporate defence.

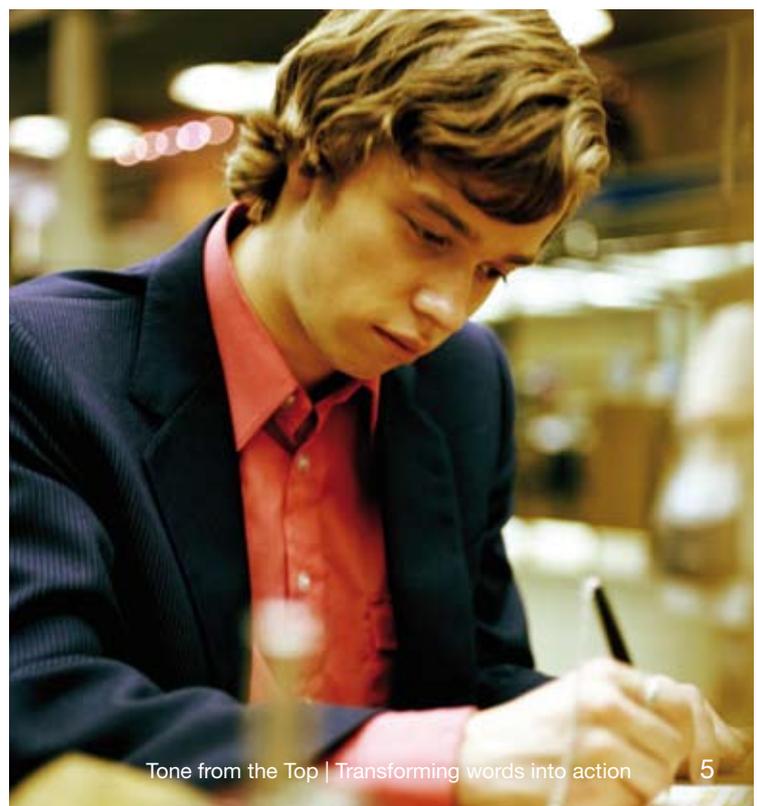
This thinking will translate into advice and support for our clients in defining and embedding what Tone from the Top means to them in a sustainable and measureable manner and as part of an organisation's approach to managing ethical risk and increasing its overall risk resilience.



“*The results of the PwC Tone from the Top report are very encouraging. The challenge now for leaders is not only to set the right tone from the top, but also to move from a command and control management model which requires people simply to obey orders rather than to take personal responsibility for doing the right thing. A morally mature business encourages constant dialogue around common purpose, shared values, good behaviours and sustainable outcomes. This isn't new thinking, because this is how we function in our personal lives.*

We just need leaders to encourage us to be grown-up human beings first and business people second.”

Professor Roger Steare, Corporate Philosopher and Professional of Organisational Ethics, June 2010



Key findings

- 1 The importance of Tone from the Top is strongly acknowledged
- 2 There is a flurry of short term actions but little evidence of long term behavioural change
- 3 Leaders are not always doing what they say
- 4 Tone from the Top is perceived to have more impact internally than externally
- 5 Practical implementation is not easy
- 6 Ethical risks are being identified but not measured
- 7 Organisations are responding to unethical behaviour at some levels
- 8 Adequate training is not being provided
- 9 There are insufficient internal help mechanisms
- 10 Businesses are not gaining assurance over the systems and processes supporting ethical conduct

“*In any discussions about procedures within the corporate we shall be looking to find evidence of adequate procedures to assess how successful the corporate has been in mitigating risk. We shall also be looking closely at the culture within the corporate to see how well the processes really reflect what is happening in the corporate. For example, we shall look for.....a clear statement of an anti-corruption culture fully and visibly supported at the highest levels in the corporate*”

*Approach of the Serious Fraud Office to Overseas Corruption
July 2009*

1 The importance of Tone from the Top is strongly acknowledged

“87% of respondents agree / strongly agree that culture contributes to the mitigation of risk around fraud corruption and ethical behaviour”

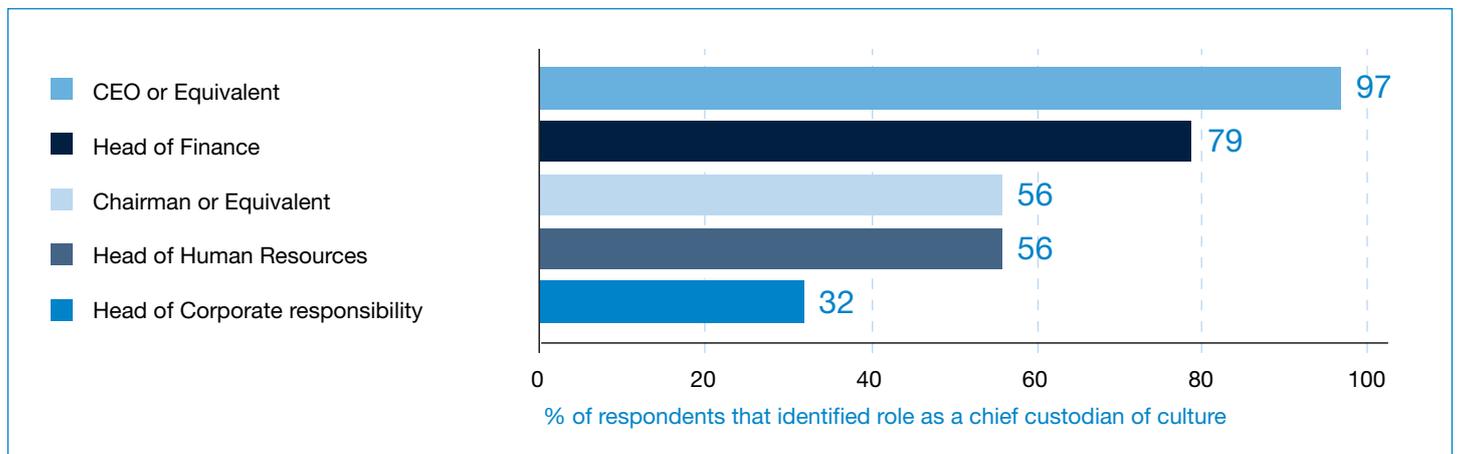
This statistic supports our core hypothesis behind this survey that Tone from the Top is critical in addressing fraud and other ethical risks and for setting the ethical culture of an organisation.

This view is one shared by external bodies and regulators alike, for example, being referred to in the OECD Business Approaches to Combating Corrupt Practices and the US Federal Sentencing Guidelines. As part of the guidance on the Bribery Act to be released by the Government on how to prevent bribery, Tone from the Top is very likely to be positioned as a critical component in addressing bribery and corruption risks.

Without Tone from the Top, will other anti-bribery and corruption procedures/processes/tools ever be effective?

In terms of accountability, the survey respondents were fair to underline their own level of involvement with 86% seeing themselves as integral in setting a robust Tone from the Top. It was also identified that, whilst the CEO is seen as the primary custodian of culture in the business, the wider board members also feature strongly (figure 1).

Figure 1: Chief Custodians



“ Society is entitled to expect of the corporates these days that they have adequate anti-bribery processes and that those processes are carried out throughout the corporation. If there is a significant failure, then it is a board level failure. ”

Richard Alderman, Director of the SFO, 2009

“ Tone from the top is the most important, if it doesn't exist, then everything else will fail ”

Survey Participant

2 There is a flurry of short term actions but little evidence of long term behavioural change

“77% of respondents say leadership teams have an articulated set of values and principles but only 36% regularly assess them for relevance and applicability”

Our survey demonstrated that leadership teams are beginning to establish the foundations for setting the right ethical tone. However the results are less promising in terms of sustainable activities to drive longer term change. This indicates a real risk of values and corporate strategy being misaligned to everyday operations of the business.

23% of respondents said that there was recognition and reward for individuals when positive ethical values were demonstrated in the business (figure 2). If an action is seen to be the right thing to do, but is not recognised as such by the leadership, it may take much longer to persuade other people to do the same. On the flipside of this, what about when something goes wrong?

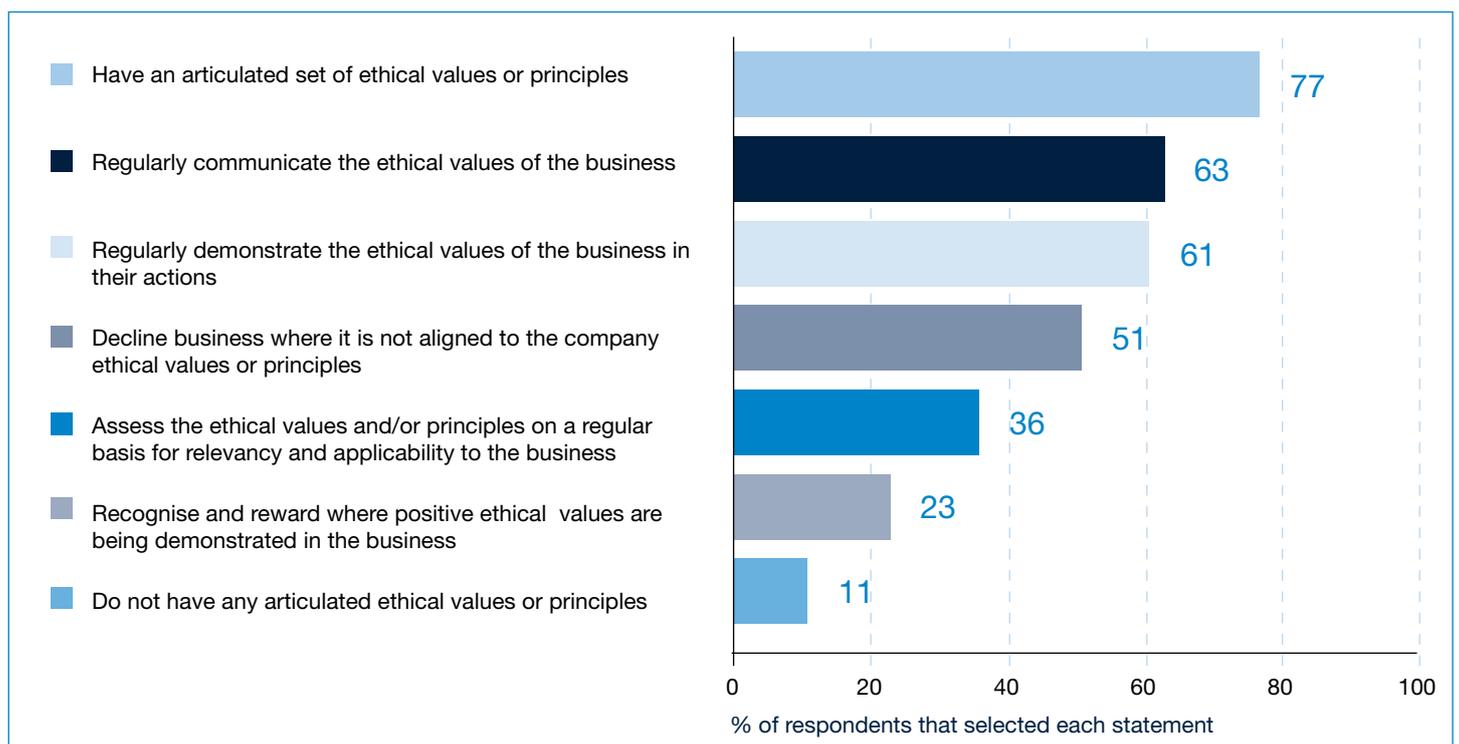
We asked if the businesses communicate non-compliance issues with employees when practicable – just 33% said this was the case.

So, just as good behaviour is not being openly recognised and rewarded within the business, neither is improper behaviour being publicised and resulting sanctions and actions transparently communicated. Both are required to drive long-term, sustainable behavioural change in mitigating integrity risks.

One reassuring figure was one of leadership starting to put ethics ahead of profits – in 51% of cases the respondents acknowledged that the organisation had turned business down where it was not aligned with the values of the business.

This tells us that some organisations are willing to accept a shorter term pain or loss in recognition of the longer term strategic aim of aligning corporate strategy and values on a consistent basis.

Figure 2: My leadership team.....



3 Leaders are not always doing what they say

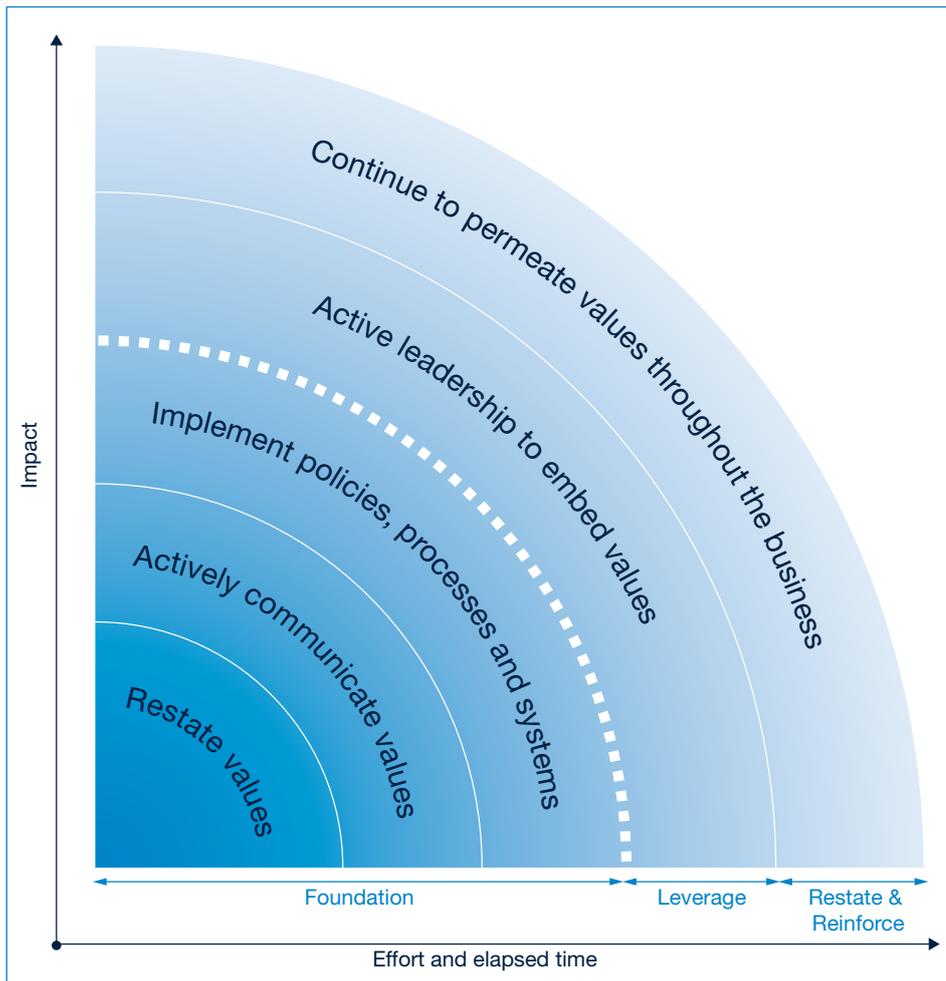
“Less than half of respondents say that senior leadership always act as role models in setting Tone from the Top”

43% of respondents also said that on the occasions where Tone from the Top had been undermined it was due to the fact that leadership actions did not reconcile with the ethical messages being delivered.

It is critical for senior leadership to act as role models through their behaviours, actions and words to encourage and motivate others to do the same – after all, if senior leadership do not “do as they say”, why should anyone else? Leaders must not only be judged for their technical competency to lead but also by their ability to understand the need to act with integrity and deliver the right culture.

Figure 3 illustrates the effort required and the amount of time it takes to embed and reinforce values and ethical standards in the business. Only by continually repeating and consistently restating values through coherent and clear leadership behaviours will the ethical standards permeate into the DNA of the business and its people.

Figure 3: Build consistently repeated leadership behaviours



“
The leader must walk the talk and lead by example. Ethical leadership permeates an organisation. Conversely, unethical leadership also permeates an organisation”
Survey participant

“
The ultimate driver is the need for leaders themselves to be ethical (towards employees, customers, suppliers, shareholders and regulators), not just to do it because it sounds like a good idea”
Survey participant

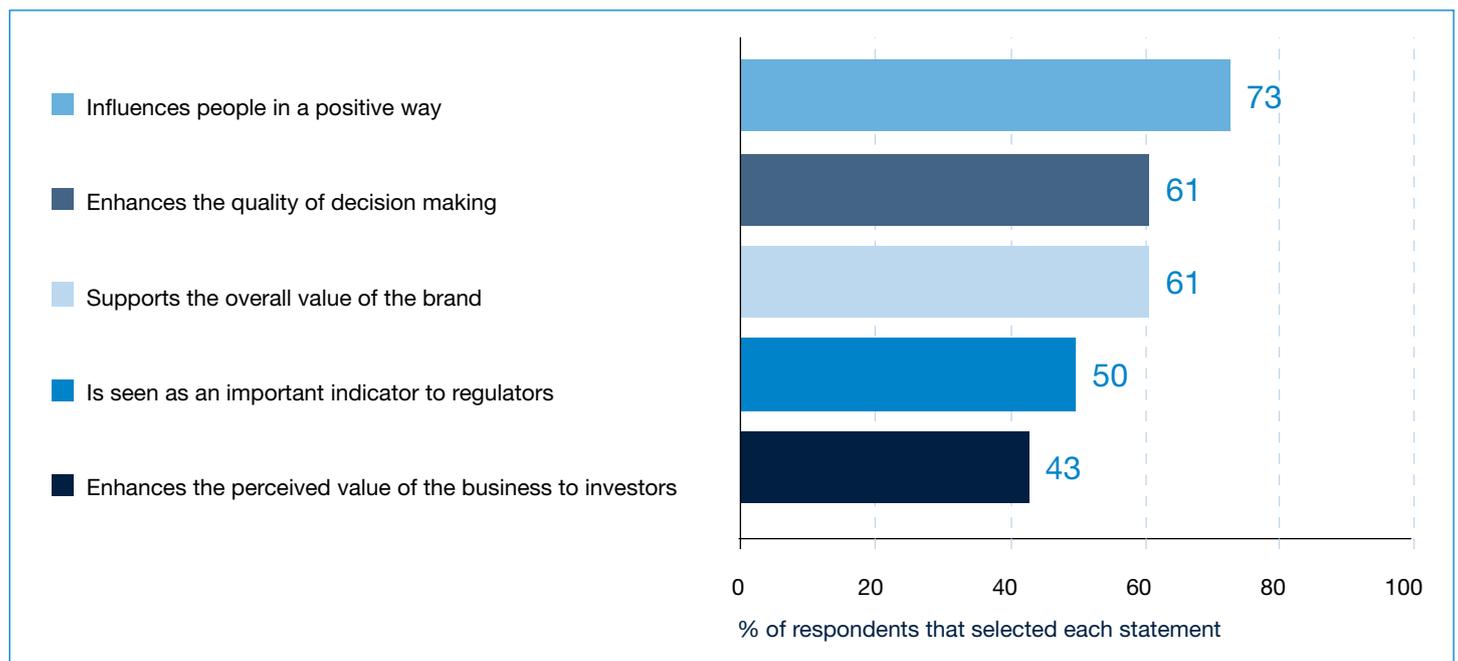
4 Tone from the Top is perceived to have more impact internally than externally

“61% say that Tone from the Top enhances the quality of decision making where as just 43% consider that it enhances the value of the business to investors”

Although Tone from the Top is critical to embedding and setting the right ethical culture within the organisation, the impact on the external marketplace should not be underestimated. How management consistently behave, and in a crisis, are seen to react, can have a critical impact on external stakeholder’s views of the business (figure 4) including regulators, shareholders, competitors, suppliers, governments and pressure groups.

There is an emerging trend for organisations and their leaders to have a stronger and more explicit obligation to wider society. A poor culture at an organisation often explicitly manifests itself in failures of governance or management, with detrimental impact on market value and investor confidence. However it is often individuals in the wider society who are the real victims, with unacceptable consumer outcomes being the end result.

Figure 4: Tone from the Top in my organisation...



5 Practical implementation is not easy

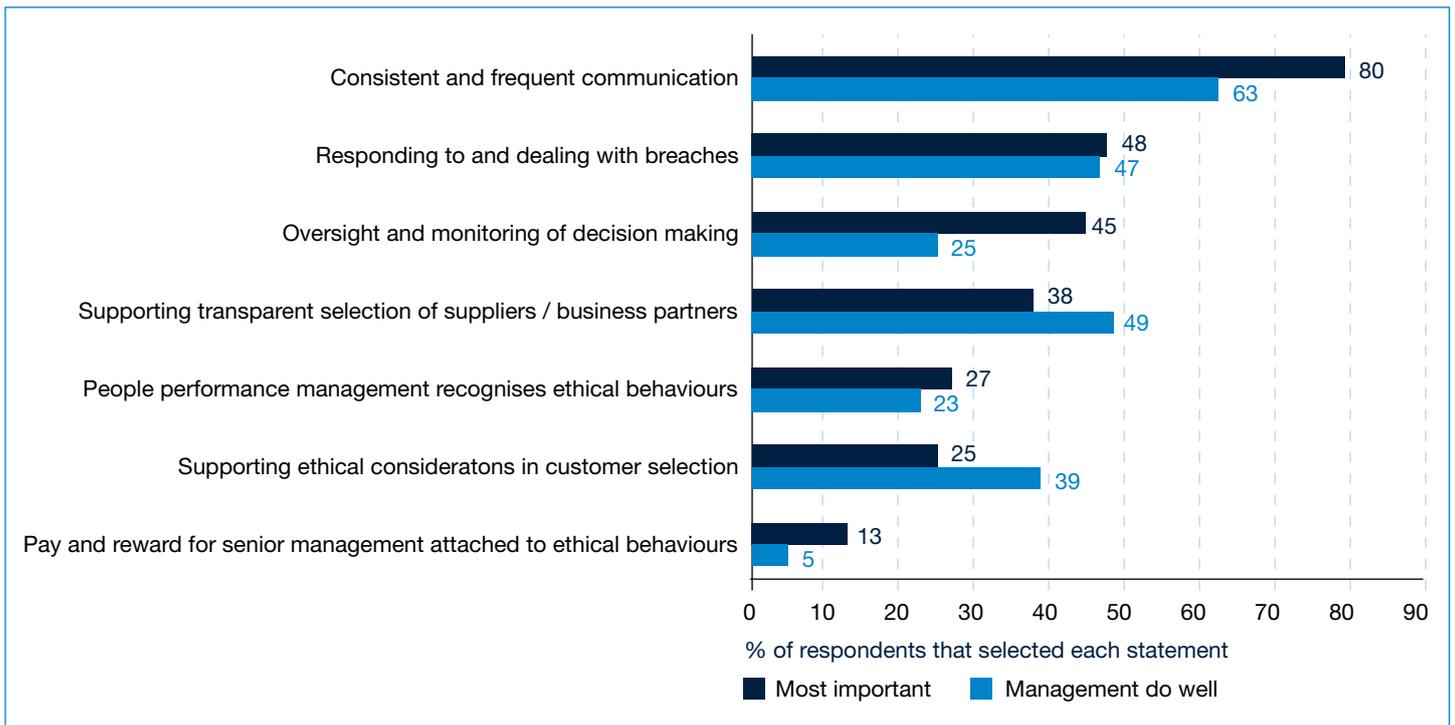
“80% state that consistent and frequent communication are important drivers but only 63% state that this is done well by management – a clear disconnect between delivery and intention”

Respondents identified some methods of implementation as being more important than others; for example, “consistent and frequent communications” and “oversight and monitoring of decision making” (figure 5) were identified as two key drivers of effective implementation of ethical conduct. In each of these two cases though, there was a significant shortfall of what leadership were considered to do well.

The overall message is that the importance being attached to the identified key elements of what makes effective Tone from the Top is not borne out by the effective implementation and delivery of these activities by senior management.

Why is this? Is it a lack of capability, a lack of resource, a lack of incentive, a lack of leadership commitment, or even perhaps a lack of ability to act with integrity?

Figure 5: What is important?



“None of the above”

Response from several survey participants when asked which elements are done well by their senior management

6 Ethical risks are being identified but not measured

“70% agree / strongly agree that ethical risks are identified but only 34% report they are adequately measured or evaluated”

Whilst most commercial organisations carry out strategic risk assessments, our experience has been that the majority of these focus on areas of operational, strategic or financial risk, but rarely of ethical risk.

This is reflected in the above results of our survey. This is further emphasised by the fact that, despite viewing ‘oversight and monitoring of decision making using ethical criteria’ as an important element in delivering effective tone from the top, only 25% of respondents thought that leadership did it well.

Are leaders taking too simplistic an approach to decision-making in areas where they do not fully understand the ethical risks? Do leaders have a clear and comprehensive line of sight on the levels of ethical risk exposure across and down the organisation?

If not, then it is unlikely that they have adequate procedures in place. See figure 6 for how an ethical risk assessment will support leaders in addressing the key questions above.

Figure 6: What will an ethical risk assessment do for you?

- Identify the potential inherent ethical risks.
- Assess the likelihood and significance of occurrence of the identified ethical risks.
- Identify and map existing preventive and detective controls to the relevant ethical risks.
- Evaluate whether relevant controls and processes are effectively designed to address identified ethical risks
- Identify and evaluate residual ethical risks resulting from ineffective or non-existent controls.
- Respond to residual ethical risks.

7 Organisations are responding to unethical behaviour at some levels

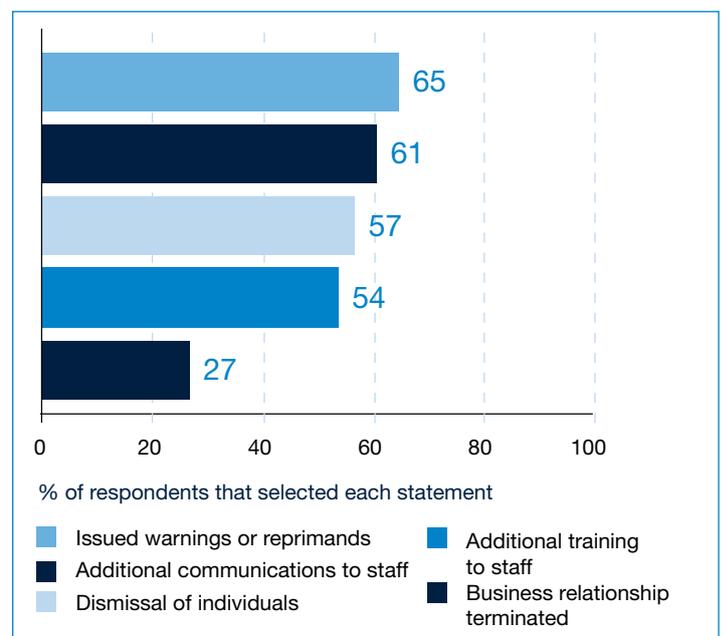
“27% confirm that their business has terminated a business relationship as a response to unethical behaviour”

Actions speak louder than words and it appears that some organisations are responding to unethical behaviour in places. However the strength of these responses and the consistency of their application is still intermittent.

Internally, issuing warnings or reprimands (65%) and additional communications to staff (61%) were the most popular responses to unethical behaviour, although this data should be read in the context of 32% of respondents also stated that “inadequate sanctions on those found to be in the wrong” contributed to the undermining of Tone from the Top.

This raises the question as to whether the popular responses to unethical behaviour are in fact strong enough and should more stringent measures (such as dismissal) be exercised on a consistent and robust basis (figure 7).

Figure 7: Responses to unethical behaviour



“The key is to have the courage to recognise that ethical decisions drive long term value. Courage comes from the need to sometimes disrupt short term value drivers for ethical reasons (e.g. rejecting business that does not fit the ethical stance)”

Survey Participant

8 Adequate training is not being provided

“63% of respondents report that annual refresher training on a Code of Ethical Business Conduct (or equivalent), sponsored by leadership, is not provided”

Of the remainder, only 17% confirmed that all employees received annual refresher training. This should be set against the background that training will form a fundamental component of a robust anti-bribery and corruption programme that may be used in defence of a “failure to prevent” corporate liability under the Bribery Act.

As a tool to provide guidance and advice on ethical matters, the Code (or equivalent) is a critical part of an organisation’s armoury against ethical risk. If there is a lack of regular training its effectiveness and ability to be widely understood and deployed by employees and other parties will be diminished. In addition sponsorship and endorsement by leadership is critical – not only should leaders participate in the training themselves, they must also support the investment required upfront and reinforce the significance of the training through their actions and communications (including disciplining those who do not participate).

How can you be certain that your employees use the Code and the supporting policies and guidelines to support their decision-making?

When was the last time the Code was refreshed and cascaded through a behaviour-based training and communications programme that reflects local traditions and customs, and is led by the top?

A lack of regular and relevant training can contribute to a failure to establish and maintain an effective anti-bribery and corruption compliance framework.

9 There are insufficient internal help mechanisms

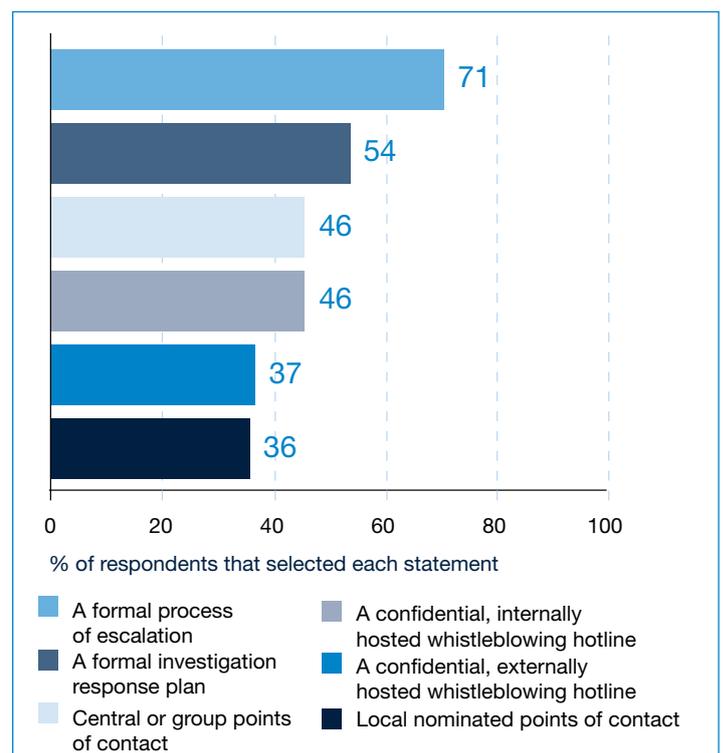
“46% of respondents have a central point of contact and 36% of respondents have a local nominated point of contact to report issues to”

To develop an environment where employees feel confident to be able to make business decisions that align with the principles and rules of the business, they need firstly, a channel to ask questions where they are uncertain and require clarification, and secondly, a channel to report issues and incidences of improper behaviour.

A majority of respondents confirmed the existence of some type of formal process of escalation in their organisation. However there were a much smaller number of positive responses in terms of existence of points of contact and whistleblowing provisions (figure 8).

This could mean that levels of identified risk around ethical business conduct in the organisation may be much higher than identified, due to a lack of incident reporting and concerns hitherto un-raised. If an employee feels strongly enough about an issue in such a situation they may decide that their only recourse is to go external to the business, with potentially disastrous consequences to the organisation and to the individual.

Figure 8: How do staff gain support?



10 Business are not gaining assurance over the systems and processes supporting ethical conduct

“22% of respondents say they have nothing in place to gain assurance over ethical tone”

Why would an organisation want to seek assurance over the systems and processes supporting its anti-bribery and corruption programme? There are a number of reasons, not least to improve the programme by assessing its robustness and comprehensiveness and identifying areas for improvement, and to safeguard and enhance its reputation as a business committed to high standards of integrity and transparency.

However, the survey tells us that businesses are not gaining comfort that their systems and processes supporting ethical conduct are, appropriate and effective in a consistent or robust way (figure 9).

This raises some fundamental questions that leadership should be asking:

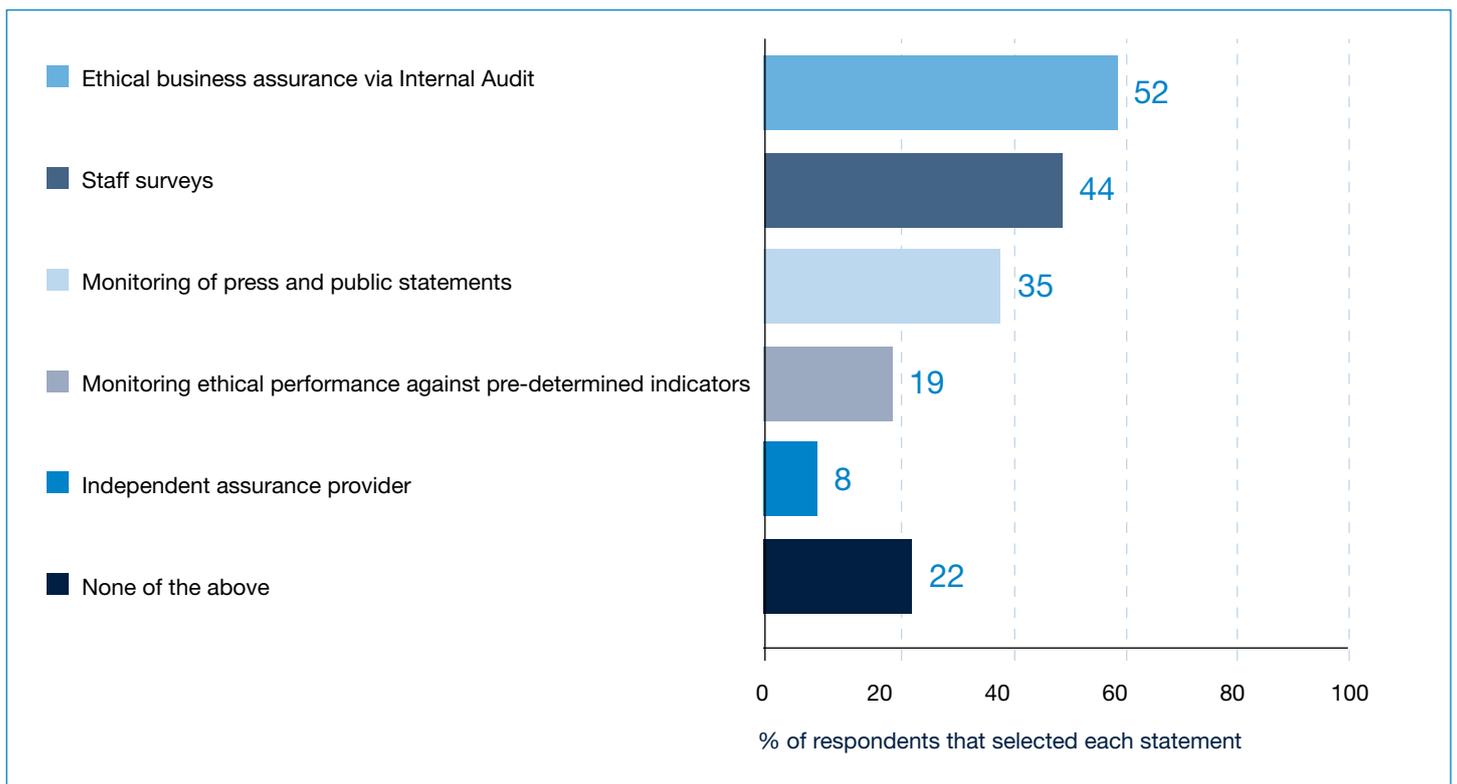
- Do we have comfort that the organisation is working to and adhering to a consistent ethical standard?

- Do we know how effectively processes, procedures and controls are designed and operating to manage ethical risks?
- Do we have the right governance and behavioural framework in place to facilitate good judgement by staff?

The benefits of gaining assurance are many, including enhancing credibility with stakeholders (internal and external) by validating the existence and design of the systems and processes supporting the compliance programme; to provide, if applicable, a basis for mitigation of sentencing in the event of a bribery incident; to restore market confidence following the discovery of a bribery incident; to meet any future pre-qualification requirements; and to show compliance with the requirements of voluntary and industry initiatives.

Why would you not seek it?

Figure 9: How do we gain assurance?



How the survey was conducted

The research for the survey was co-ordinated by PricewaterhouseCoopers' International Survey Unit, based in Belfast.

This report is based on the responses from 144 members of the PwC Fraud Academy to a survey conducted in April 2010. The PwC Fraud Academy is a community of individuals based in the UK that have responsibility for managing fraud, corruption and integrity risk to their organisation. Members receive:

- Access to regulators, experts and peers through events, seminars and webcasts
- Thought leadership, knowledge, benchmarking tools, surveys and best practice
- Regular updates and invitations to PwC Fraud Academy events emailed to you

Our members include people working in finance, internal audit, security, in-house legal and compliance functions as well as specialist fraud teams.

www.pwcfraudacademy.com

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