Co-Authors
Amy Conway-Hatcher, Partner, Baker Botts
Sheila Hooda, Independent Board Director and Strategic Advisor

The Road Ahead on #MeToo: Board of Directors' Governance Challenges in Setting Strategy, Fostering Culture, Leveraging Talent and Mitigating Risk

In the year since the #MeToo movement shined a spotlight on workplace conduct, high profile scandals have consumed the news and our social discussion. Only yesterday, thousands of Google employees staged a "walk out" from offices around the world to protest the company's handling of sexual misconduct in the wake of a bombshell New York Times report. Today's headlines are questioning the impact on Google's brand and its standing as an "aspirational workplace". But Google is not alone. Crisis counseling firm Temin & Co. reported 900 cases of sexual misconduct by senior leaders that made news headlines in the last year. "Every sector has been affected" and "CEOs and board directors – are looking for insight on why, why now, and how we can address the reputational risk of toxic workplace cultures."[1] Temin noted the numbers represent only the "the tip of the iceberg" as the majority of cases are never reported or publicly disclosed.

While the Temin data and scandals like Google are shocking, the importance of the #MeToo story for Boards of Directors is broader than sexual harassment. #MeToo has proven to leaders the enormous toll that workplace misconduct and abuse of power can take on an organization's culture, value, sustainability and reputation. And, it has highlighted the loss of control by organizations to contain scandal in today's era of technology and disruption.

The fact is #MeToo has propelled forward the "culture discussion" in a way that no other scandal has in recent memory. PwC's Annual Corporate Directors Survey, "The Evolving Boardroom: Signs of Change", found that "culture" is at the top of the agenda for Boards.[2] The prioritization of culture is driven by two factors - the severe impact on companies affected by #MeToo, and questions increasingly confronting Boards about their own role (or perceived failure) in addressing toxic work environments and misconduct by leaders or high profile figures.

> *"Corporate culture has taken center stage in recent years. Scandals ranging from cheating to meet government standards, to mistreating customers in order to hit unrealistic performance goals, to pervasive sexual harassment, fill headlines. In the aftermath of such crises, shareholders, regulators, employees, customers and others are often left asking "where was the board?"*

How It Happened? The Landscape and Factors that Drove #MeToo

The rapid escalation of #MeToo-type scandals have been fueled by social media, technology and an evolving view of social justice that crosses generations. The impact across the economic and business landscape was further driven by the intersectionality of five main factors:

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[1] http://www.teminandcompany.com/in-the-news/
[2] https://www.pwc.com/us/en/services/governance-insights-center/library/annual-corporate-directors-survey.html

- **Use of Technology:** The increased and sophisticated use of technology by mainstream society has brought about interconnectedness and disruption to social groups, organizations and business models across industries.

- **Social media platforms**: The wide spread use of technology and social media platforms enable individuals and groups to be heard easily, widely and instantaneously. Employees, global supply chains, customers and others can *be heard* when and where they want, and the information they share can proliferate faster than organizations can react.

- **Evolution of social justice and norms:** Social change is occurring more rapidly, driven by demographic changes, interconnectedness and the generation Y/millennial focus on broader societal issues like social justice, gender empowerment, equity and education.

- **Consumer engagement:** Consumers can engage in ways never seen before. They have more choices and access to products and services. They not only demand immediacy and personalization, but they are willing to use their collective and powerful voices (and wallets) to be heard on issues they care about.

- **Investor activism:** Institutional investors are more powerful than ever before, and they are increasingly more focused on ESG.[3] Investors are using their power to influence strategic, structural, financial and governance changes through their voting privileges and investments.

In the #MeToo context, these factors empowered collective voices to create disruption and force change where people believed organizational culture was flawed and leadership failed.

What This Means for Board Governance

#MeToo has proven that organizational culture is a company asset that must be thoughtfully cultivated and carefully protected. It also highlighted the risks of abuse of power on organizational culture, and how unchecked power and inadequate corporate governance can lead to costly consequences for companies, including financial, legal and reputational which can threaten sustainability and growth.

While no one can predict where fiduciary legal liability ultimately will lie, there is a growing collective view that Boards are the ultimate guardians of an organization's financial, human and reputational capital and that addressing culture issues falls within the Board's responsibilities – the buck stops with the Board. In parallel, stakeholders expect board governance to more closely align with cultural and social issues that drive sustainability, innovation and revenue.

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[3] According to PwC's survey, institutional investors now own 70% of US public companies.

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Five Key Areas of Focus and Lessons Learned for Boards in the Wake of #MeToo:

Boards are increasingly viewing broad workplace misconduct issues and movements like #MeToo with a wider lens and as a key business risk to carefully manage through more proactive oversight and thinking through strategies if the worst happens. Here are five key areas of focus in the year ahead based on the lessons of #MeToo:

1. **Board oversight of strategy and risk.** Disruption presents opportunities for new business but also emerging risks that can exacerbate reputational, business and legal exposure. The Board's proactive and thoughtful engagement can help mitigate those risks through strong leadership and probing on issues that may affect companies in ways not previously seen. Areas of risk include abuse of power, increased intolerance for social injustices and workplace inequities that negatively impact the workforce, and technological advances that allow stakeholders to speak up. Boards are weighing specific risk areas, including new and evolving state legislation and legal risk, such as forced arbitration, mandatory annual training and Weinstein type clauses on M&A transactions. In the wake of cases involving senior management and the large payouts often involved in these terminations, we expect to see more companies and Boards pay closer attention to employment contracts with top executives to be more explicit about what counts as a "cause" for termination and to add references to sexual harassment to the wording of severance arrangements. In the face of the issues facing Google, we expect Boards will want to be informed of the terms of higher risk departures to evaluate the reputational risks of "golden parachutes" and may seek independent legal advice on the advisability of such payments. Strategy, risk and crisis management planning are likely to appear at the top of committee or full board agendas for the foreseeable future.

2. **Culture as a strategic asset.** Organizational culture is strategic asset that should align behaviors to promote team unity, shared purposes, value creation and innovation to allow companies to take calculated risks to increase profitability and long-term growth. Where culture is undefined or conduct is not aligned with a company's stated values, the company's opportunity for value creation is significantly jeopardized. At its worst, a toxic workplace culture can instantaneously destroy market cap, value and strategic assets. Management guru Peter Drucker eloquently stated: "culture eats strategy for breakfast". If culture is poor, even great strategies can fail." #MeToo highlighted the challenge for Boards to truly understand the health and risk of organizational culture through C-Suite interactions alone. Given the disruption of #MeToo, focus on culture and observations of recent surveys, we expect Boards will be taking more concrete steps to understand and influence the culture "at the top" as well as the "mood in the middle" and the "buzz at the bottom." Some steps may include increased use of employee surveys, exit interview reports, analyses of hot lines and whistle blowers, 360 degree management reviews and training feedback. However, other innovative steps are emerging using data, assessments and personal interaction with workers to more effectively evaluate culture and hold

management accountable for abuses of power or culture lapses that affect long term sustainability and strategic goals.

3. **"Tone at the Top" and consistent organizational standards.** Healthy cultures start with clear, consistent organizational standards that apply to all and comply with applicable laws. Leadership and integrity matter. Where rules are not applied equally and management or powerful individuals receive disparate treatment or lack accountability, culture will suffer every time. Boards and management should align on clear standards of conduct, integrity, accountability and well-defined escalation processes as a check and balance against potential abuses. Some companies - like Airbnb - have found that aggressively focusing on culture and intentionally setting shared expectations at the top makes it easier to maintain and enforce positive standards of conduct throughout the organization in a way that drives stronger cultures. Airbnb General Counsel Rob Chestnut, who speaks frequently on the topic, said: "Integrity doesn't just happen — it needs to be guided and addressed with specificity by leadership in a company."

   Boards must ensure that companies have processes that empower and encourage employees to speak up without fear of retaliation. Anonymity in reporting and surveys must be respected to allow for open feedback and raising sensitive issues, and there also should be opportunities for informal reporting or discussion through training or other sessions. As issues are raised, management must ensure that they are thoroughly investigated, reviewed and addressed. If there is a question about a potential or actual conflict of interest, an independent investigation should be pursued. Any allegations that affect senior or important management functions should be escalated to the Board or a designated committee of the Board to allow for robust review and discussion about risk. Where problems are found, they must be addressed – regardless of personal relationships or inconvenience. Boards can no longer afford to stay quiet or allow workplace misconduct by managers to go unaddressed or to continue.

4. **Talent as a competitive differentiator.** In this disruptive environment, talent is a strategic differentiator for innovation and risk taking. Companies like Google face stiff competition for top talent. And, scandal can serious impact a company's ability to attract and retain talent, which directly impacts innovation. With new technologies, rising automation, demographic changes, and a rising social focus on wellness, values, equality and respect, Boards are asking questions around a whole new set of considerations:

   - *Are talent acquisition, retention and promotion aligned with the values, mission and purpose of the organization?*
   - *Is there an understanding of the future skill needs and gaps?*
   - *Is there adequate investment in skill development, reskilling, upskilling, job re-design and new work force models and the gig economy?*
   - *How will work force incentive and compensation structures evolve?*
   - *How will culture and opportunity for advancement promote loyalty and commitment?*
   - *How can the company drive innovation through a safe and diverse work environment?*

- *How effective and thoughtful are the company's diversity and inclusion approaches?*
- *What are the employee risks around data, cyber, privacy and intellectual property?*

Research from McKinsey, the Boston Consulting group, the Peterson Institute for International Economics and Credit Suisse have substantiated the link between diversity and performance. McKinsey's recent research indicates that companies with ethnic and cultural diversity in the top quartile are 33% more likely to outperform peers in terms of profitability and the numbers are statistically significant.[4] The Board's intentional focus on the creation of a diverse and inclusive workforce and a safe, respectful and motivating working environment not only improves operational decision-making but allows companies to better compete for top talent, increase innovation, and grow risk-adjusted profitability.

5. Improved institutional stewardship and increasing engagement and disclosure on governance, board composition, strategy and compensation.

Public proxy fights are hitting the headlines with increased frequency by financial centric activists. At the same time, boards have to deal with investors who tend to be longer-term and ESG oriented. The result is a careful balancing act of interests, which has necessitated more meaningful engagement and disclosure around strategy, risks, compensation and performance. Going forward, Boards should expect that culture also will be a topic of interest in the upcoming proxy seasons.

In this context, a board's quality and composition are also under increasing scrutiny. There is greater attention to director skills and skill matrixes, board evaluation and refreshment processes around age and term limits, over-boarding and diversity. Investors and other stakeholders are becoming less tolerant and accepting of homogeneous boards that do not reflect the organization's customer, employee or supply base.

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Regardless of what one thinks of #MeToo or the challenges facing Google and other companies today, the movement has been a catalyst for change and it has shaken power structures in society's most visible sectors. It has forced a positive focus on culture as a core corporate asset that should not be ignored. The age of disruption and #MeToo presents a powerful opportunity and a clarion call for self-assessment and reflection by all who participate in the discussion, including directors. Forward-thinking boards will proactively seize the moment to enhance corporate governance practices and reimagine a work place that has a safe, inclusive, fair and healthy culture for long-term value creation – and we will all be stronger for it.

[4] https://www.mckinsey.com/business-functions/organization/our-insights/delivering-through-diversity