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THE KEY TO SUSTAINABLE RISK GOVERNANCE: STRONG CORE VALUES, DELEGATION AND ACCOUNTABILITY

TORBEN JUUL ANDERSEN
Copenhagen Business School
Department of International Economics and Management
Porcelænshaven 24A, 3.78
DK-2000 Frederiksberg
Denmark
Phone: +45 3815-2572
Email: tja.int@cbs.dk

GREGORY L. SHAW
George Washington University
Institute for Crisis, Disaster, and Risk Management
1776 G Street, NW Suite 101
Washington, DC 20052
USA
Email: glshaw@gwu.edu

CGSR

Center for Global Strategic Responsiveness

Department of International Economics and Management ● Copenhagen Business School

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The Key to Sustainable Risk Governance: Strong Core Values, Delegation and Accountability

Abstract

Purpose – The article brings attention to the importance of corporate values and concrete leadership enactment of those values as a necessary condition for effective risk management outcomes.

Design/methodology/approach – The content is based on practice-based research experiences supported by relevant literatures on risk governance and values-based management complemented with insights from case analyses and empirical studies.

Findings – The paper explains why formal risk management approaches have limitations and outlines how the presence of official policies and codes of conduct is insufficient to deal with dynamic and complex high-impact situations where strong core values heeded by the corporate leadership, in contrast, leads the way to better risk behaviors throughout the organization. Major disasters in British Petroleum over the past decade illustrate how a formal code of conduct failed to do the job when the leadership in reality gave first priority to profits at the expense of the stated environmental values. The prioritized code of the US Coast Guard is used to illustrate the circumstances where core values support effective crisis, disaster and risk management outcomes.

Originality/value – The paper goes against conventional wisdom of imposing tighter rules and regulations with formal controls as a panacea to cope with major disasters and shows why simpler means of guiding core values combined with delegation of responsibility to act under unexpected conditions is important in both private and public enterprise.

Keywords: code of conduct, core values, corporate culture, crisis, disaster, enterprise risk management, leadership, risk governance

Major crises have regularly affected highly reputed business enterprises and public institutions over the past decades with significant negative impacts on value creation and social welfare. Many of these events seemingly happened without ill-intended human interventions and despite seemingly good governance practices, executive intents and managerial efforts. However, these cases often display a striking discrepancy between what executives thought, and said, was being done and what actually took place within the organization as business activities were carried out in practice. To remind ourselves we can just think of Lehman Brothers during the financial crisis and British Petroleum (BP) in the Mexican Gulf.[i] Lehman Brothers had excellent risk management capabilities but the board still accepted higher exposures to the market for sub-prime loans. BP had a clear code of conduct emphasizing safety and environment as prime concerns but still pushed the organization into risky drilling ventures. These crises were caused by a diversity of factors ranging from lack of oversight and excessive risk-taking to the impacts of operational hazards and external economic phenomena. Yet, as a typical trait across incidents there was a shortage of behavioral guidance and core values, or if such were in place, they were somehow not respected or adhered to when push came to shove. In short, the organizations were exposed to poor risk governance and leadership practices that beg the question why such events happen time-and-again and what top managers and directors can do to safeguard against these kinds of devastating outcomes.

More often than not the response to major crises and reported scandals has been to impose more regulation, tighter rules, increased scrutiny and more detailed reporting to enforce compliance such as the imposition of the Sarbanes-Oxley Act in 2002. However, there is little evidence to show that these approaches actually advanced the cause they were intended to support. At best we see no effect from intensified monitoring and tighter controls and at worst it increases the burden of bureaucracy and kills creative efforts devoted to search for better responses to unexpected conditions. Instead we suggest that good risk management behaviors derive from relatively mundane but essential and fairly costless leadership traits. We find it is important that essential *core values* are instituted and followed by the top executives both in spirit and in terms of specific actions because the example of good leadership decisions inspires people in the organization to follow the lead. It might be necessary to express the core values in words displayed in a formal code of conduct in general view for everybody, but it is insufficient to formalize the principles in glossy policy documents. The values and the principles behind the codes and core values must be enacted from the highest level of the organization through executive deeds and concrete actions.

If the leaders in charge pay lip service to the core values of the organization and make decisions without any regard for them, or apply incentives that contravene these values, then people working in the organization cannot be expected to adhere to the underlying principles either. Good risk behaviors derive from good leadership conduct as practiced by the top executives, and by extension, by the managers that operate at all levels of the organization leading the daily execution of business activities. Investing in extensive risk management systems without supportive leadership in spirit and action can be a waste of money and effort and may become an excuse for inactive leadership. Sometimes poor leadership traits derive from engrained behaviors embedded in the way organizational members think and act as implanted by generally accepted conduct over prolonged periods of time, which is often referred to as the *corporate culture*. In particular executives that gained most of their managerial experience in a single organization with the same contextual background should be cognizant of this phenomenon, but we all are prone to it.

Since corporate cultures to a large extent are established, influenced and subsequently changed by the executive echelons it may take a strong and diverse board to identify such traits and actively engage to have them instituted across the organization in a proactive and effective manner. Humans, and thereby also executives, are exposed to particular perceptions and views of the world that derive from their own personal experiences and hence it is sound practice to involve people with diverse backgrounds and experiences in major decisions about complex strategic issues and potential disaster scenarios. That is, good risk management practices entail attentiveness and engagement at all levels of the organization with open and honest communication about what may turn out to be early warning signals revealing emergent risks and potential opportunities.

Every streak of risk events seem to stir an urge towards legislative, regulatory and corporate governance initiatives with the intent of restraining similar events from ever happening again in the future by imposing more elaborate and comprehensive restrictions. While being well intended, this can unfortunately lead us into a false belief about our ability to control human behaviors in highly dynamic and complex environments. It also displays the human shortcoming of not being able to see low-probability high-impact events in advance while seeing too many shadows pointing in that same direction after a major event has occurred. This bias often results in the futile exercise of "closing the barn door after the horse has left", and closing it with a slam. But doing things too late does not help, no matter how hard they are done. A better response might be to try to understand how the adverse situations arose in the first place and then learn from the mistakes.

In the early 2000s we saw a number of corporate scandals caused by executive misbehavior in some cases bordering on fraudulent actions including corporations like Enron, Global Crossing, WorldCom and Tyco where executives purposely misreported for personal gains. The Sarbanes Oxley (SOX) legislation was a direct outgrowth of these events and imposed new reporting demands on US listed firms while holding executives personally responsible. These requirements would encourage top managers to engage in stringent compliance exercises hiring external consulting outfits to implant state-of-the-art control systems and demonstrate that best efforts had been done. However, this inadvertently promotes a protective and defensive behavior, where the exercise has more concern for covering ones behind, rather than ensuring the organization is more alert, engaged, responsive, and on its toes to deal with the unexpected that always will arise along the way. To little surprise then, we saw that a SOX compliant super-bank, Société Générale, was able to lose close to €5 billion in January 2008 due to an individual so-called rogue trader, Jérôme Kerviel[ii]. During the evolving financial market crisis in 2008, we saw other compliant financial institutions budge due to reckless risk-taking pursued by dominant executives condoned by their boards in established companies like Bear Stearns[iii] and Lehman Brothers[iv]. In these cases, the shareholders lost most, if not all, their invested money, while the executives continued to rake home their sizeable bonuses.

Other events are more subtle in nature and not necessarily ill intended, although the disastrous consequences often will be the same. Two examples from the United States National Aeronautics and Space Administration (NASA) organization include the *Columbia* and *Challenger* disasters, both caused by systemic internal priorities arising from an institutional environment of budget controls and an accounting culture that gradually induced decision makers to ignore the potential for major disasters (Vaughan, 2005). In the corporate sector some comparable examples may include the major explosions at the *Texas City* refinery and the *Deepwater Horizon* platform operated by BP in the Mexican Gulf. While the corporate governance practices at BP for all intents and purposes appeared to be perfect and run by the book, it was still possible for the company to incur two major industrial disasters within a relatively short period of time despite corrective changes in the executive management team. This pinpoints a number of challenges, such as, how to establish an effective culture of risk awareness throughout the organization, how to ensure that risk is handled by all organizational members in accordance with the corporate aims, how to motivate employees to act as effective risk managers, and how executives and directors can engage to ensure better risk leadership.

We believe an important part of the answer to these essential questions lies in the leadership approach taken by the executive team and the directors that oversee them. It is not a question of control and compliance, which represents a false sense of security in dynamic, complex and unpredictable environmental settings. The issue rather becomes how to ensure that early warning signals identified throughout the organization are communicated, probed, and interpreted in a timely and proactive manner, so the corporate executives are in a better position to deal with the unexpected event that can lead to crisis and disaster. This requires clear moral standards and prioritized core values imposed on the organization and enforced through executive example. It further demands delegation of authority where local managers and employees in general can act knowing that their superiors support them and trust their ability to respond properly while they are accountable for actions taken, or not taken.

Avoiding Gaps between Intensions and Actions

So, why do we observe the apparent discrepancies between well-intended policies and general guidelines issued by the executive leadership and experienced external directors in the board? We think the answer to this question is linked to discrepancies between what the executives and the board members preach and what they practice in reality as they make major decisions on corporate resource utilization and promote people based on achieved outcomes. That is, if the official core values heeded by senior management cannot be recognized in the actual decisions made around the daily operations, people in the organization will act in accordance with the true values that motivate those decisions. Hence, we argue that managing the core values of an organization is one of the major responsibilities of top executives and directors and heeding those values is essential to good crisis, disaster and risk management practices.

According to *values-based management* one of the principal leadership tasks is to establish the core values to be adopted across the organization as guiding principles to prioritize the many resource committing decisions taken over time (Anderson, 1997). Whereas different people and groups in the firm have diverging personal interests, the core values serve to balance diverse aims by promoting a concise set of ethical principles and corporate priorities. That is, the core values constitute the means to balance the concerns and interests of the organization's important stakeholders and ensure collaboration for a common cause. The core values reflect the shared beliefs embedded in the corporate culture that influence how corporate actions are executed by people through the influence of informal leadership (Wieland, 2005). *Stakeholder theory* argues that business conduct is about "how customers, suppliers, employees, financiers (stockholders, bondholders, banks, etc.), communities, and managers interact and create value" (Freeman, Harrison, Wicks, Parmar and De Colle, 2010). This view suggests that there is a need to impose core values to prioritize essential stakeholder interests and ensure long-term performance through stakeholder collaboration where the absence of such is likely to create fundamental conflicts as the basis for future risk incidents and crises.

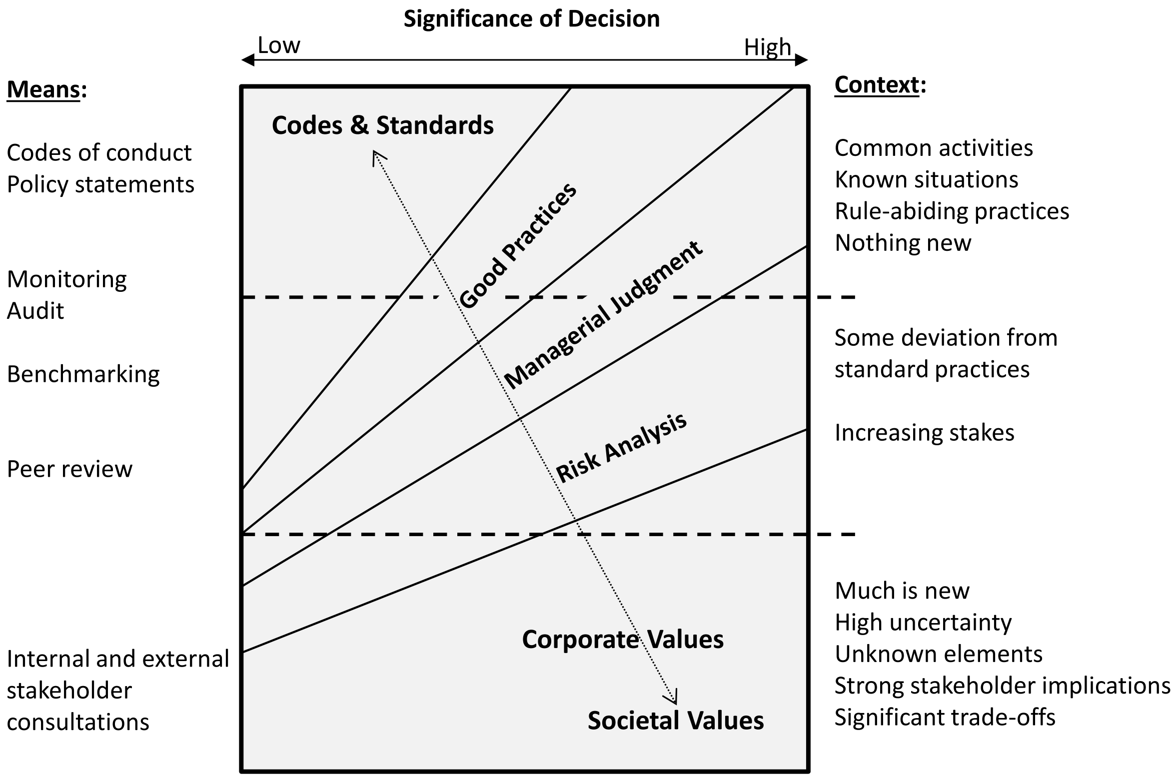
Hence, the ability to mitigate and manage foreseeable risks while preparing for the emergence of unpredictable events is the essence of good risk management practice. The comprehensive risk management frameworks, often referred to as enterprise risk management (ERM) including the COSO and ISO 31000 standards, are superbly geared to deal with foreseeable risks based on well described processes of identifying, assessing, handling and managing the embedded exposures. However, unpredictable events are by definition very hard, if not impossible, to foresee in advance and yet the organization must be able to deal with these emergent crisis situations. This is where core values embedded in the corporate culture play an important role. In contrast, the use of formal policies and codes of conduct works well where the operating conditions are well known and little new is happening in the business environment (Figure 1).

The conventional use of ethical guidelines and codes of conduct suffice when the organization deals with decisions of relatively low significance under situational conditions that are known. If the stakes increase and the decisions take on higher significance, the standards should be complemented by good practices and managerial judgment supplemented by more advanced risk analysis to assess the consequences as proposed by the formal risk management frameworks (Figure 1).

However, the real challenge arises when the organization is faced with contexts where things are constantly changing and in flux where much is new and evolving thus creating a high level of uncertainty with many unknown elements. Under these circumstances the standard approaches to risk management will not suffice because they provide general guidance with little flexibility to accommodate new and unexpected circumstances. Here the core values embedded in the corporate culture become essential as a guide to individual responsive actions throughout the organization and help prioritize decision alternatives in new not previously encountered situations (Figure 1). In the case of truly high-stakes decisions, it also becomes important to consider the societal values that might be affected and influenced by the potential outcomes.

This illustrates why the presence of core values are indispensable beyond formal codes and standards particularly in organizations operating in highly uncertain and unpredictable environments. It also pinpoints that formal codes and standards compared to core values and corporate culture are distinctly different risk management means. That is, we cannot just assume that the imposition of formal codes of conduct and policy standards automatically will lead to the existence of strong and durable core values.

Figure 1. Means of Risk Management against Decision Significance and Context



Adapted from *Risk Based Decision Making Framework*, United Kingdom Offshore Operators Association (1999).

The prevalence of core values with a good sense of direction and behavioral clues will help individuals dispersed throughout the organization act more effectively and consistently when confronted with unexpected events and unforeseeable circumstances. The establishment of core values embedded in a corporate culture can, for example, derive from a clear mission statement outlining the general aspirations with stated prioritization of essential stakeholder concerns and general behavioral guidelines (Andersen and Schrøder, 2010).

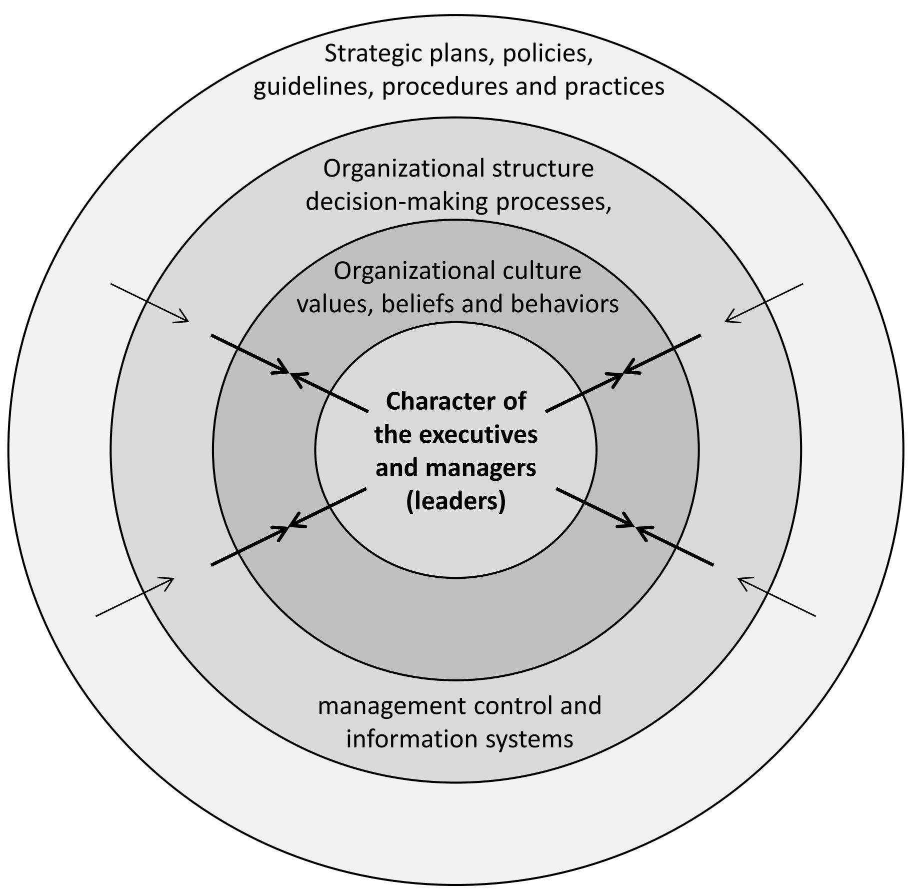
Schein (2004) argues that a corporate culture is imposed by the beliefs, values and assumptions of the founder(s), experiences among people as the company evolves, and beliefs, values and assumptions brought in by new people hired into the organization. Hence, the core values reflect the morality of the top executives and the members of the board and they earn confidence and loyalty among employees through their role modeling actions (De Hoogh and Den Hartog, 2008). That is, the moral stance of the senior executives influence the predominant core values and inspire the behavior of organizational members when the values are adhered to in practice by the corporate leaders. In other words, core values with impact will evolve from established ethical principles reinforced through the personal commitment and conduct displayed by corporate leadership.

Assessing and managing the exposures of major identifiable risks is a relatively straightforward task in the case of financial, insurable and economic exposures where outcomes typically can be documented based on readily available public data. However, the same cannot be applied to unpredictable events although simulation techniques, scenario analyses and stress-testing exercises may be useful to assess potential outcome effects. Instead the ability to prepare for unpredictable and unforeseeable events requires a risk aware corporate culture where a core value induces individuals at all levels in the organization to stay alert to emergent risks and be ready to deal with the unexpected. This also provides the ability for a central risk function to collect early warning signals from dispersed organizational members where decentralized responsive actions are encouraged to fend off the preliminary effects of emergent risk situations.

Effective risk management under uncertain conditions entails conjoint efforts of analytical and coordinating activities by a central risk function and decentralized observance and responsiveness among dispersed employees operating in the grapevines of the organization where the new events typically will be visible first (Andersen, 2011). Hence, part of effective risk management entails engaging the right people to operate within a decision structure with open information and communication systems and flexible interactive controls. It implies that decision power is delegated, so organizational members can act fast within their areas of responsibility, and that the leadership trusts their ability to respond properly while they remain accountable for eventual outcomes.

The corporate leadership can enhance and support the ability to deal with uncertainty and unexpected events by developing an organizational culture with proper core values where the risk behavior primarily is driven by the character of the corporate executives and the line managers (see Figure 2). In addition, corporate leadership can support the enactment of effective risk practices by imposing organizational structures and decision-making processes with business policies, procedures and practices that are conducive to good risk management behaviors (Figure 2).

Figure 2. Leadership Influences on Organizational Risk Behaviors



Adapted from Pauchant, T.C. and Mitroff, I.I. (1992). *Transforming the Crisis-Prone Organization: Preventing Individual, Organizational, and Environmental Tragedies*. Jossey-Bass Publishers: San Francisco, CA.

(Figure 3.1, The onion model of crisis, disaster, and risk Management, p. 49)

In the case of BP[v], very elaborate and highly visible policy guidelines on corporate behaviors expressed in a formal code of conduct were imposed when Tony Heyward was put in place in 2007 as new group CEO after the Texas City Refinery explosion (see Insert on British Petroleum). But despite these concerted efforts to guide the right behavior, the company experienced another path breaking event, when an oil rig under their command exploded in the Gulf of Mexico in 2010. We now know that the discrepancy between deed and action was due to the fact that codes and standards are unable to deal effectively with new unknown situations and because the executives in reality prioritized short-term profits more than the values expressed in the official guidelines. The fact that the board gave first priority to profits was expressed implicitly by the chairman Carl-Henric Svanberg at the time: "The BP board is deeply saddened to lose a CEO whose success over some three years in driving the performance of the company was so widely and deservedly admired."[1] In other words, when the board of directors represented by their Chairman signals that profits is the primary focus, it is no wonder, that the executives under their supervision, and the managers reporting to them throughout the organization, give foremost attention to this concern. Writing a nice and possibly well-meaning story about concerns for safety and environment in an official code of conduct can do little to change this, even though it portrays the board as showing great care for societal issues.

British Petroleum (BP)

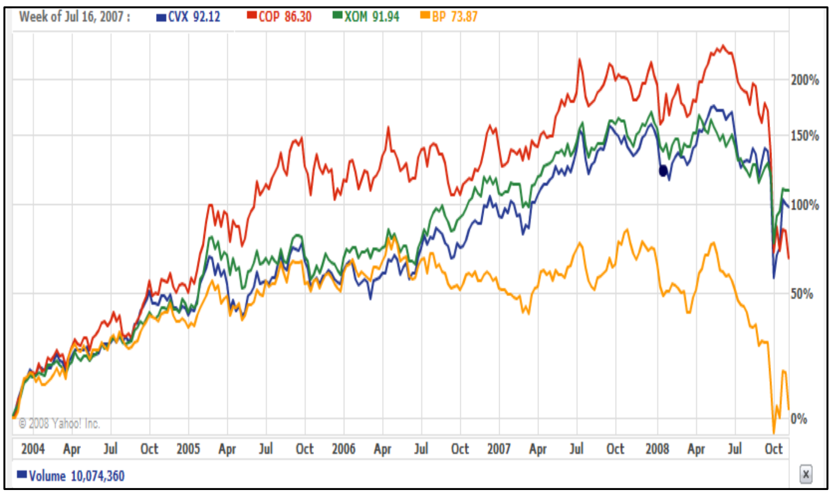
Major Risk Incidents and Environmental Disasters

British Petroleum experienced a number of risk incidents over a relatively short period of time that had some devastating impacts on their key stakeholders while hurting their own bottom line and the market value of the company.

The Group Executive Officer John Brown was famously known for BP's 'Beyond Petroleum' campaign

[1] BP Corporate Website, Press Release on July 27, 2010.

aimed at changing the corporate focus towards more sustainable energy sources. He turned BP into the largest global oil conglomerate among other things through the mega-merger with Amoco. However, in March 2005 a major explosion at BP's *Texas City* refinery that killed 15 workers and injured more than 170 people changed the course. The incident was caused by a number of confluent factors including ineffective equipment, poor maintenance, and insufficient safety precautions that had a catastrophic outcome. As a consequence John Brown retired prematurely in May 2007 and Tony Heyward became new group executive just before a panel (led by former US Secretary of State James Baker III) released a devastating report on the incidence. BP was fined close to $50 million for environmental violations with claims of more than $1.6 billion in compensation. The explosion hurt the confidence in corporate management and the stock price on BP shares suffered in the aftermath compared to the peers in the industry.



The investigative report stated: "BP has not provided effective process safety leadership and has not adequately established process safety as a core value across all its five U.S. refineries" and "found instances of a lack of operating discipline, tolerance of serious deviations from safe operating practices, and apparent complacency toward serious process safety".[2] These were serious allegations and caused BP to instate clear codes of conduct emphasizing safety and environmental consciousness (see below). Still it was reported that: "along with another BP facility in Toledo, Ohio the refinery accounts for 97 percent of all flagrant violations found in the US refining industry by inspectors over the past three years, according to the Centre for Public Integrity."[3] So, things did not really improve.

With the changes in executive leadership one should think that the board and top management would make sure things were changed. However, we know that another environmental disaster happened as the *Deepwater Horizon* rig operated by BP in the Mexican Gulf exploded in April 2010. That is, Tony

[2] Extracts from the Baker Report, 2007.
[3] AFP, August 10, 2010.

Hayward spent three years in charge to restore the corporate reputation for safety after the Texas City blast but despite these efforts the company still faced another disastrous event. It happened despite imposing a clear code of conduct prioritizing safety and environmental concern and the board abiding by all best practice governance requirements.

The code covers key areas of business operations of which the first is:
– health, safety, security and the environment –
fundamental rules and guidance to help us protect the natural environment, the safety of the communities in which we operate, and the health, safety and security of our people

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Some argued that the company had taken safety risks to save money long before the explosions possibly stemming from a market driven obsession with profits that had become an unavoidable trait of the corporate culture. Other human factors might also be in play to enhance events namely the inability to estimate the probability of unlikely events with extreme cost effects. Since the directors, executives, and operating managers had never experienced a rig explosion, they could not conceive it as happening in reality. Yet, the adverse impact on the BP stock price was very real and it continues to suffer compared to major competitors.

BP faced hundreds of lawsuits in federal court in New Orleans including claims by families of workers killed in the explosion of the drilling rig. Under the circumstances, the board decided to replace Tony Hayward as group executive and sell $30 billion of corporate assets (around 10% of the entire balance sheet) to offset cost connected to the oil spill with expected future claims estimated as high as $49 billion.

We can draw on comparable examples from public sector, not-for-profit, organizations to illustrate the importance of institutional core values combined with trust, delegation, and accountability in driving effective crisis, disaster, and risk management practices (see Insert on the United States Coast Guard).[vi] Hence, if you are faced with central commanders that try to impose controls under strained conditions due to lack of trust in their subordinates, things are likely to go wrong. Field officers need the authority, trust and support from the central office to focus on the demands of unfolding local actions when unexpected events happen to accomplish the overarching mission and safeguard the crew. This projects a model of decentralized responsiveness among operating officers in the field as they deal with uncertain evolving circumstances supported by strong core values to guide the responsive actions they take.

The United States Coast Guard

Governance Based on Mutual Respect, Trust and Open Communication

The United States Coast Guard is a military armed force with all uniformed personnel (supported by civilian employees and volunteer personnel) subjected to very specific conduct requirements laid out in the Unified Code of Military Justice (see below). For the purpose of this case study, the analogy is made of the general governance, command structure and code of conduct of the military structure to the governance, leadership and policies of a generic organization.

The general governance philosophy of the United States Coast Guard is conveyed in its core values of Honor, Respect and Devotion to Duty reflected in personal integrity, teamwork, and accountability to the public trust. Of course, these high level statements, operationalized through organizational strategies, goals, and objectives do not ensure 100% compliance at all levels of the military structure. As a microcosm of society in general, violations requiring correction and/or disciplinary action do occur. At the unit level, these organizational goals and objectives are supplemented and reinforced by more specific unit goals and objectives, policies and procedures, and most importantly, the expressed and demonstrated leadership philosophy and style of the unit commanders.

The operation of a Coast Guard cutter requires myriad knowledge elements, skills, and abilities in areas which are the province of crew members with the requisite training, experience, and qualifications. No commanding officer possesses technical and operational expertise across all these areas and she or he must place trust in the cutter's officers and crew and provide the necessary support for them to accomplish their responsibilities to the best of their ability. The commanding officer is totally responsible and accountable for the safe operation and mission of his or her unit and must establish oversight and communication channels to meet this absolute responsibility.

The commander's trust of individual crew members is earned through their observed and reported performance and is lost when performance does not meet accepted standards without sufficient reason. Trust works both ways however. A commanding officer must continually model the core values of honor, respect, and devotion to duty to earn and maintain the trust of the officers and crew who place their safety in her or his hands on a daily basis. Performing the missions of the United States Coast Guard onboard cutters is dangerous business often conducted in the worst of weather conditions under significant stress and uncertainty. To perform safely and professionally, the crew must place their complete trust in their commander to do the right thing. There can be no perception that the commander is more concerned with his or her personal agenda and advancement than with the safety and wellbeing of the crew and the requirements of the mission. Once lost, trust is seldom, if ever, earned back and can have a negative impact on morale and performance.

Core values merely expressed in words and not followed from the top down and from the bottom up in both spirit and action are a recipe for poor organizational governance and will most likely have adverse consequences. An organization whose leaders do not believe in, follow, and visibly support their own core values cannot expect the same from those people they lead. Within the United States Coast Guard, the very best units in terms of safety, morale, and mission performance are those who believe in the Coast Guard's core values supported and modeled by their leaders.

Officers are evaluated on a periodic basis using standard forms and required documentation that are based upon personal and professional qualities consistent with the core values of the Coast Guard. These evaluations largely determine promotions and future duty assignments. Personal and professional qualities requiring detailed evaluation include: Initiative – originating and acting on new ideas; Judgment – making sound decisions and providing valid recommendations based upon risk assessment and analytic thought; Responsibility – Acting ethically, courageously, and dependably and inspiring the same in others; and Professional Presence – Bringing credit to the Coast Guard through one's actions, competence demeanor and appearance. The evaluation process reflects the overall Coast Guard culture and belief in its core values. Officers who do not attain and maintain the highest standards in general have very limited career advancement and enhancement opportunities and those that do comprise the current and future leaders of the Coast Guard.

Honor

Integrity is our standard. We demonstrate uncompromising ethical conduct and moral behavior in all of our personal and organizational actions. We are loyal and accountable to the public trust.

Respect

We value our diverse workforce. We treat each other and those we serve with fairness, dignity, respect, and compassion. We encourage individual opportunity and growth. We encourage creativity through empowerment. We work as a team.

Devotion to Duty
We are professionals, military and civilian, who seek responsibility, accept accountability, and are committed to the successful achievement of our organizational goals. We exist to serve. We serve with pride.

Hence, we see that the same approach seems to work across different types of organization whether it constitutes a private company generating returns to their owners by showing concern for other stakeholders or it is a public institution providing a common good for society. This approach builds on strong core values supported straight from the top combined with trustful delegation of authority that leaves room for local responses to evolving events where individual actors are accountable for action as well as inaction.

Discussion & Conclusion

The core values and the cultural context within which crisis, disaster, and risk management takes place should be a main concern of the board of directors and the executive management team. The corporate leadership creates and manages the organizational culture and the tone is set by the executive echelons. The corporate culture is comprised of the basic assumptions and beliefs shared by all members of the organization, which will affect how things are done. It is learned from practical experience where group members engage in repeated tasks and share in successful problem solving exercises that over time become the behavioral standard for people operating in the organization. The cultural traits are both visible and invisible where the most visible elements are the physical artifacts displayed in the firm, while the deeper elements of values constitute the invisible shared assumptions, beliefs and accepted behaviors throughout the organization.

The importance of core values is further supported by recent evidence collected among professional market participants after the financial market crisis in 2008-09 in the RiskMinds 2009 Risk Managers' Survey. This study indicated that the specification and development of risk management competencies was critical for the events. However, despite good risk management systems they were not expected to make a difference without changes in the corporate culture. This is because the effectiveness of risk management, governance and internal controls depends on the leadership and organizational climate that drives the behaviors in the organization. As a consequence, risk culture and ethical principles should be brought to the top of the agenda among corporate executives and members of the board as well as regulators and law makers.

This verdict suggests that those responsible for overseeing the actions of the executives were not competent enough, not rigorous enough, and maybe not sufficiently powerful to influence things in the right direction. However, as the press release from the BP chairman Carl-Henric Svanberg seems to indicate, the entire company board supported the prevailing practices and was as instrumental in maintaining the existing cultural traits as were the executives they had engaged. Hence, specifying the relevant risk management competence is crucial, but it will not have lasting effects without a strong corporate culture backed by core values, because the effectiveness of risk management depends on the climate in which practice is enacted. In other words, risk culture and business ethics need to be at the top of the agenda both in the board rooms and the regulators' suites.

Risk management and governance are complex dynamic activities. In many corporate failures, the directors often lacked the knowledge to effectively oversee the executives, which impaired their ability to execute their fiduciary obligations. However, this can threaten the very survival of the firm. That is, good risk governance includes the skills, infrastructure (i.e., decision structure, incentive systems, management information and control processes) and corporate culture imposed by the directors as they exercise their risk oversight duties. In short, effective management of crisis, disaster and risk requires adherence to strong core values, trust in people, delegation of authority and individual accountability.

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End notes:

[i] See, for example, the cases 'Lehman Brothers (B)', Case Centre Ref. no. 310-266-1 and 'British Petroleum: From Texas City to the Gulf of Mexico and Beyond', Case Centre Ref. no. 714-017-1.

[ii] Jérôme Kerviel was convicted in the 2008 trading loss for breach of trust and forgery as the bank claimed he worked on his own and without authorization. He later published a book in 2010 where he argues that his superiors knew about his doings as part of common practice.

[iii] Bear Stearns was a sizeable issuer of asset-backed securities with increasing exposures to sub-prime mortgage-backed assets where the Federal Reserve Bank of New York intervened to save the company but eventually instigated a sale to JP Morgan Chase for $10 a share, which was approved by the Bear Stearns shareholders on May 29, 2008.

[iv] Lehman increased its investment in sub-prime mortgage-related assets extending the leverage ratio of assets over equity to around 31:1. As the market turned, Lehman Brothers filed for bankruptcy on Sept. 15, 2008. The CEO, Richard Fuld received a US$22 million bonus in March 2008.

[v] This draws on the case 'British Petroleum: From Texas City to the Gulf of Mexico and Beyond'.

[vi] This draws upon Gregory Shaw's experience and insights from 27 years of active duty as a United States Coast Guard Officer and as Commanding Officer of four Coast Guard Cutters.