ETHISPHERE®

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Leading Practices and Trends from the 2019 World's Most Ethical Companies®

An Ethisphere Insight Report Series

Volume 1: Focus on Reporting Transparency, Governance, and Written Standards

Preface

2018 saw a tremendous focus on the role of ethics and culture in business, from the annual letter from Larry Fink, CEO of Black Rock, to the recent announcement by State Street that it will put an increasing focus on culture. Maintaining transparency around corporate behavior is more important than ever, and increasingly all stakeholders—employees, customers, investors, etc.—are demanding that companies think about how and why they do their work and not just what they do. Here at Ethisphere, of course, we have long been proponents of the idea that it is possible to do well by doing good, and our World's Most Ethical Companies (WMEC) process is built on that foundation.

Our own research demonstrates this principle in clear terms. Once again, our WMEC honorees outperformed the market, as they consistently have since we began the process in 2006. This year's cohort of publicly traded honorees outperformed the U.S. Large Cap Index by more than 10 percent over three years, and by almost 15 percent over five years. This "Ethics Premium" data draws a strong correlation between culture, community engagement, governance practices, and financial performance.

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THREE-YEAR ETHICS PREMIUM: 10.5%

Performance of the listed 2019 Honorees as compared to the Large Cap Index from February 2016 to February 2019

- ● 2019 ETHX
- ● LARGE CAP INDEX

February 2016   **February 2019**
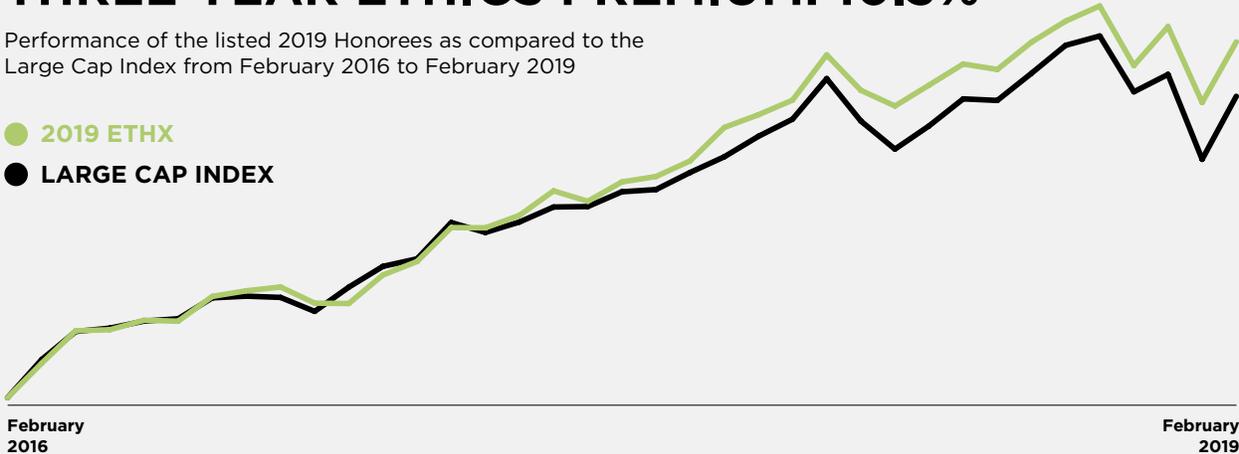
Ethisphere's Ethics Quotient® Survey (EQ) framework is designed to capture information that leads to practical decision-making. Those who complete the survey are often surprised by not only what they learn just by gathering the information needed to respond, but also how their practices compare to those of organizations recognized as the World's Most Ethical Companies. This benchmarking exercise leads to serious, fact-based conversations that inform resource planning, professional development, and executive interaction with the compliance and ethics team.

This report is based upon responses to the 2019 EQ. To help identify developing trends, we've also included year-over-year comparisons for certain data points.

In this report, we've divided our analysis into three main areas where we saw appreciable change or interesting developments over the year:

1. Monitoring and auditing and the role of transparency
2. Governance: how leading companies are engaging an increasingly diverse board
3. Written standards: how companies are communicating with a global workforce

We hope this information is useful to you and your team. At the conclusion of this report, we've outlined additional ways you can engage with the Ethisphere team and our data as you look at your own program and ways in which you can continue to improve.

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Ethics and compliance is complicated. Companies with a global workforce have a lot to manage—both internally and with external shareholders and stakeholders. The importance of transparency and open discourse is a theme that runs through the practices of the World's Most Ethical Companies.

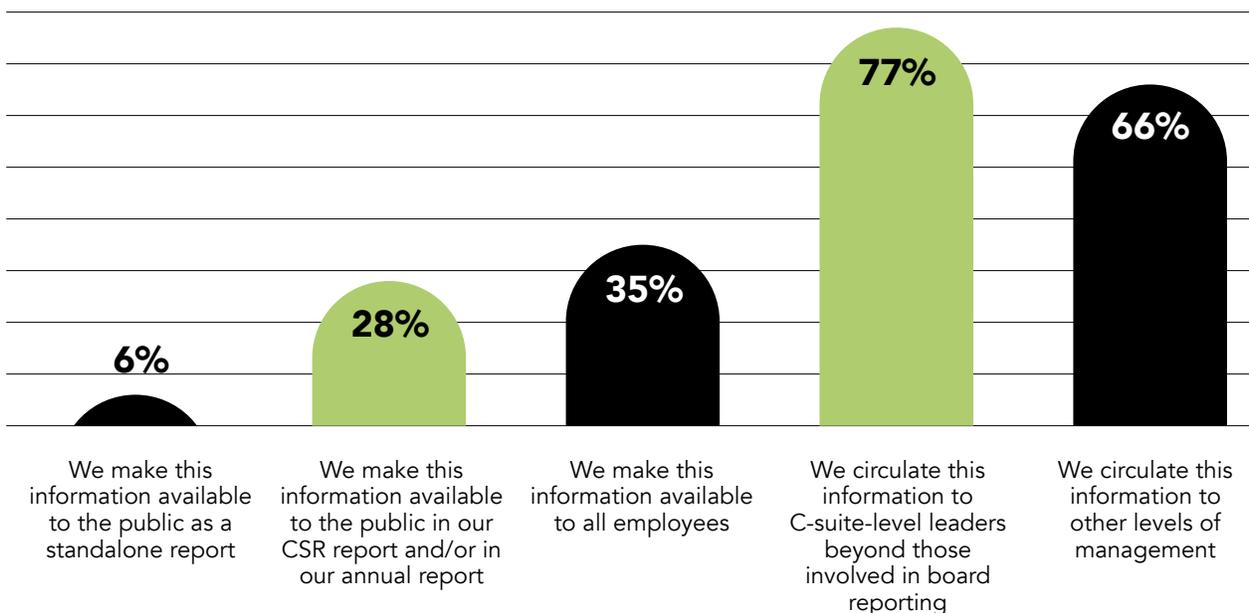# Establishing Trust Through Transparent Reporting

Ethisphere's ethical culture data set shows companies struggle to address negative views of organizational justice. Employee survey data commonly indicates mixed perceptions of whether their company holds wrongdoers accountable, whether they believe their employer will fully investigate reported concerns, and whether the rules are applied equitably across the enterprise. One out of every ten employees surveyed by Ethisphere indicated that they either disagree or strongly disagree that the rules and associated disciplinary actions for unethical behavior or misconduct are the same for every employee.

Findings from the 2019 application process show that honorees are beginning to recognize the importance of transparency throughout the investigations and

reporting process as a way to combat employee misconceptions about how the company manages investigations of misconduct. Half (50 percent) of honorees provide employees with information about the number, types, and outcomes of investigations, either as a publicly available report or as an internal report for all employees.

Nearly one-third (32 percent) of honorees do communicate publicly about how many concerns were reported, the types of concerns reported, and the substantiation rates of corresponding investigations. This figure represents a noticeable increase over 2018, as less than a quarter of 2018 honorees communicated such information publicly.

Separate from reports to the Board or other governing authority, does your organization communicate how many concerns were reported, the types of concerns reported, and the results of reports and investigations? Please select all that apply.

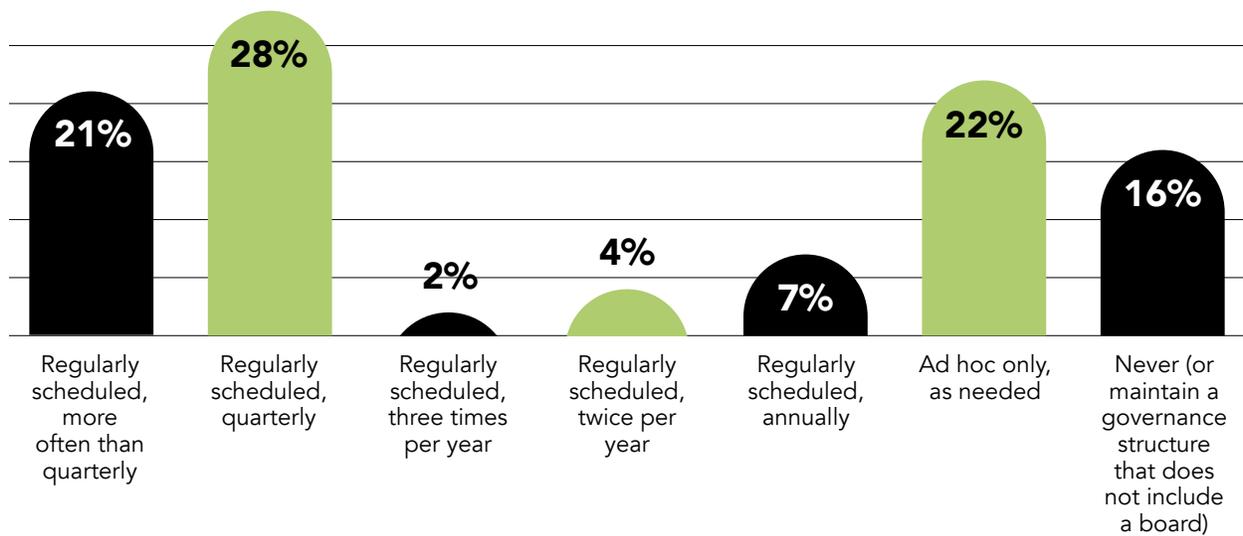| 6% | 28% | 35% | 77% | 66% |
| We make this information available to the public as a standalone report | We make this information available to the public in our CSR report and/or in our annual report | We make this information available to all employees | We circulate this information to C-suite-level leaders beyond those involved in board reporting | We circulate this information to other levels of management |

Transparency Up and Down the Organization

This trend toward open communication is not limited to employees or other stakeholders, either. An overwhelming majority (84 percent) of honorees provide executive/closed-door sessions between ethics and compliance program owners and members of the board (most often the committee responsible for overseeing the program), providing program owners with an opportunity to speak directly with non-management board members about any issues or concerns they may have, and allowing those directors an opportunity to gauge program status without management present. Nearly half (49 percent) provide such opportunities at least quarterly.

How often does the person with overall responsibility for the ethics and compliance program normally meet in closed or executive session to discuss the ethics and compliance program with the Board without management present?
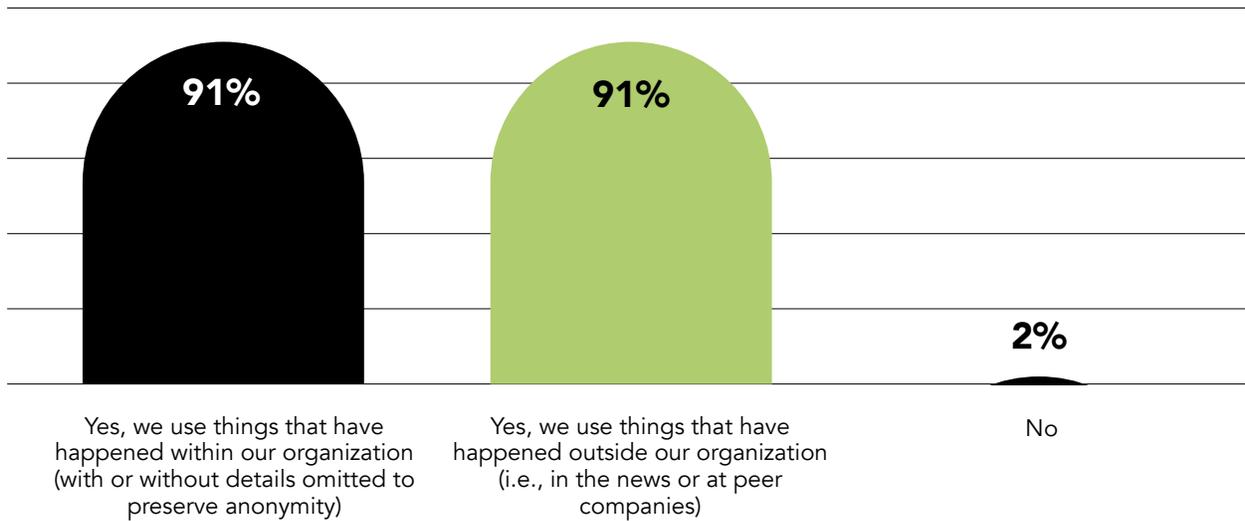
Regularly scheduled, more often than quarterly	Regularly scheduled, quarterly	Regularly scheduled, three times per year	Regularly scheduled, twice per year	Regularly scheduled, annually	Ad hoc only, as needed	Never (or maintain a governance structure that does not include a board)
21%	28%	2%	4%	7%	22%	16%

As compliance professionals develop new ways to deliver the message of transparency regarding investigations, 91 percent of honorees are using events that have happened inside their organization in their ethics and compliance communications (with identifying details removed). This figure has steadily increased over the past few years as companies figure out how to balance confidentiality with showing "yes, this really does happen here."

Does the ethics and compliance function include examples of real world ethical or compliance dilemmas or issues in their communications?
Please select all that apply

91%	91%	2%
Yes, we use things that have happened within our organization (with or without details omitted to preserve anonymity)	Yes, we use things that have happened outside our organization (i.e., in the news or at peer companies)	No

Transparent Cultures Require Support and Infrastructure

A company's ability to measure, manage, and subsequently communicate investigation metrics requires an appropriate level of internal coordination and technological infrastructure. The majority (84 percent) of honorees in 2019 use a tracking tool or case management system that tracks all reports and related investigations, regardless of how the report was originally made. Such a system would, for example, provide the ability to track reports made to a manager outside of a formal hotline system. Given that an employee's immediate manager is the most commonly used resource for not only asking questions but also reporting observed instances of misconduct, supporting middle management with tools to ease the report intake process is foundational to understanding where potential issues may lie and subsequently communicating reporting trends broadly.

Does your company have a system or tool to manage reports and subsequent investigations?

We use a tracking tool or case management system that tracks reports and related investigations regardless of how the report was originally made — **84%**

We use a tracking tool or case management system with the ability to log and track reports and related investigations, but only for reports made or originated through the misconduct reporting system — **9%**

Other — **7%**

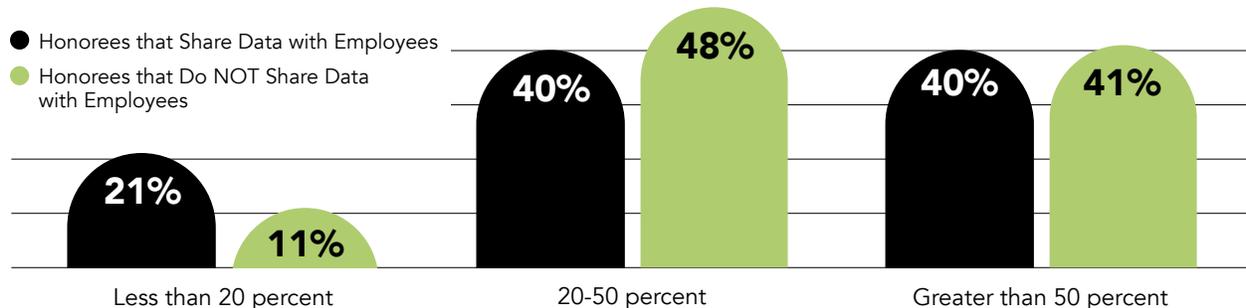No, our company does not have such a system or tool in place — **1%**
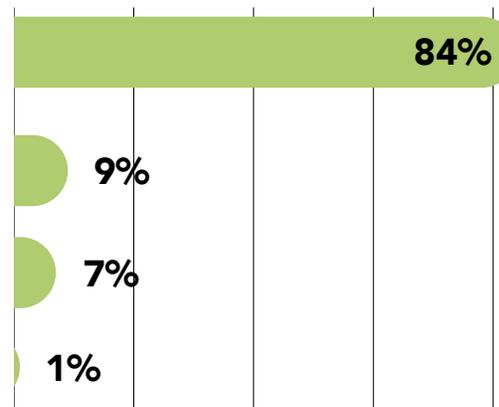
When assessing reporting metrics, a common question is whether a change in the proportion of anonymous reports is a positive or negative development. While every 2019 honoree reports using a misconduct reporting system that allows employees to remain anonymous where allowed by law, there is little consistency with respect to the volume of reports received that remain anonymous. Interestingly, the proportion of reports received that come in anonymously does not clearly correlate with whether companies disclose investigations data publicly.

Percentage of Hotline Reports Received That Are Anonymous

● Honorees that Share Data with Employees
● Honorees that Do NOT Share Data with Employees

|	Less than 20 percent	20-50 percent	Greater than 50 percent
Share Data	21%	40%	40%
Do NOT Share Data	11%	48%	41%

Diversity at the Highest Levels

This year's honorees continue to pave the way for more inclusive workplaces at both the board level and the leadership level. Among the 2019 honorees, women hold over a quarter (28.1 percent) of the director positions, representing almost a four percent increase over last year's data. This proportion is striking when comparing the gender gap among honorees to other companies; only 21.1 percent of the S&P 500's board seats are held by women, and the proportion only goes down from there. Indeed, in Deloitte's 7,000 company study of Women in the Boardroom, women comprised only 15 percent of board seats.

Distribution of Honorees According to the Proportion of Women on Their Boards
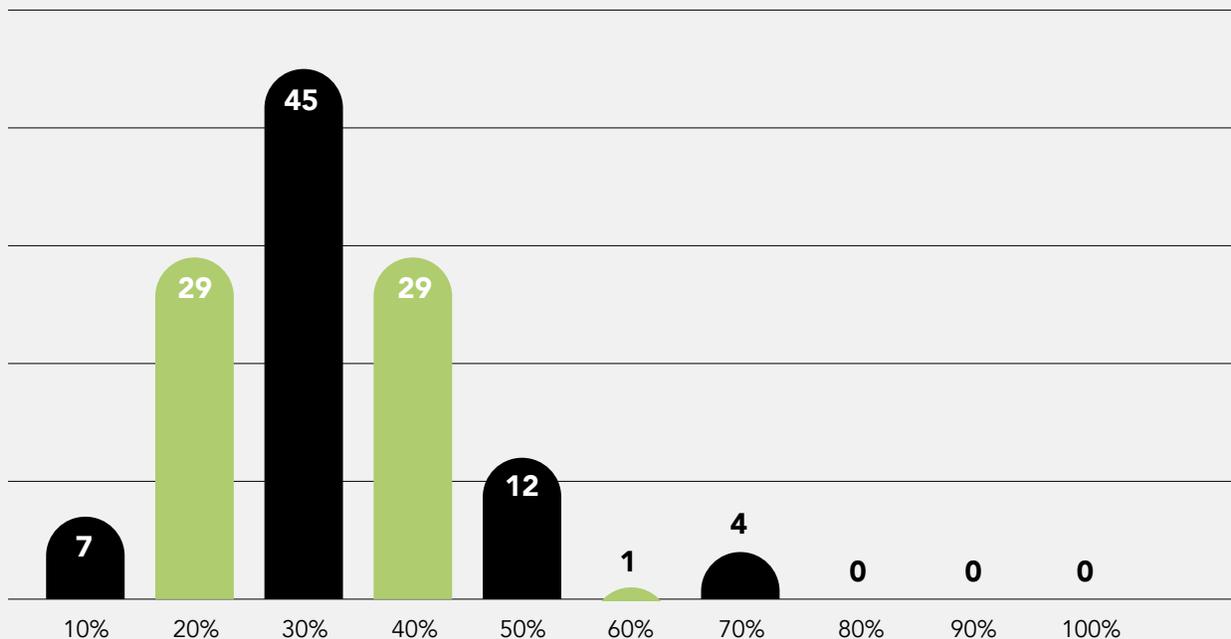
This diversity at the board level is reflected at the leadership level as well—women comprise one-quarter of the average WMEC honoree's leadership team. Again, this is a striking departure from many of the available comparisons. A CNNMoney analysis showed women hold just five percent of the CEO jobs and 16.5 percent of non-CEO executive roles in the S&P 500. Only 10 percent of 5,700 chief executive officers and chief financial officers at Standard & Poor's Composite 1500 stock index companies are women.

Distribution of Honorees According to the Proportion of C-Suite Roles Held by Women

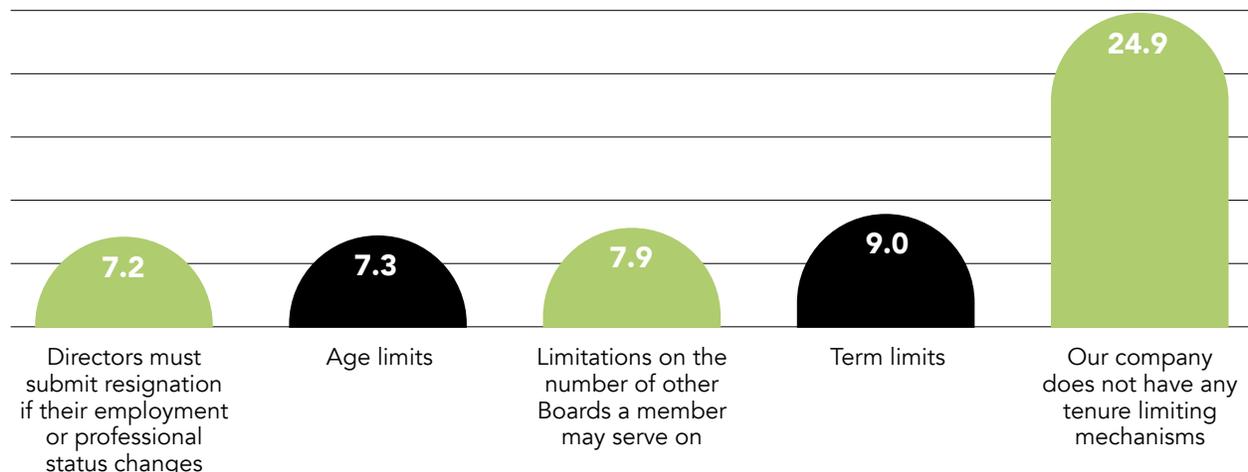| 10%	20%	30%	40%	50%	60%	70%	80%	90%	100%
14	39	41	17	10	3	3	0	0	0

In February, the SEC announced new guidance to encourage companies to report how they take diversity into consideration in making decisions about the composition of their boards. It's sensible; there is increasing investor pressure to boost diversity on boards, driven by some of the excellent research showing the link between diversity and financial performance.

One of the challenges for many organizations in boosting their diversity is finding opportunities to do so; much has been written about the long tenures of board members and the potential issues with low director turnover. Many organizations have taken steps to address "board refreshment" with an eye to balancing director tenure and skill sets with company strategy. Annual evaluation processes to review each director's strengths and weaknesses, automatic tenure-limiting mechanisms, and required annual elections of all directors are all intended to support a robust board with a strong balance of skill sets and diverse backgrounds.

Among our honorees, the average director tenure for companies that hold annual elections for all directors is 8.3 years, compared to 9.3 years for those that do not. Tenure-limiting mechanisms had a greater effect on average tenure among our honorees, however. When compared to all other tenure-limiting mechanisms, honorees that require their directors to submit their resignation if their employment or professional status changes have the lowest average director tenure (7.2 years). Those using age limits show a similarly low tenure of 7.3 years.

Average Director Tenure by Tenure-Limiting Mechanism Selected

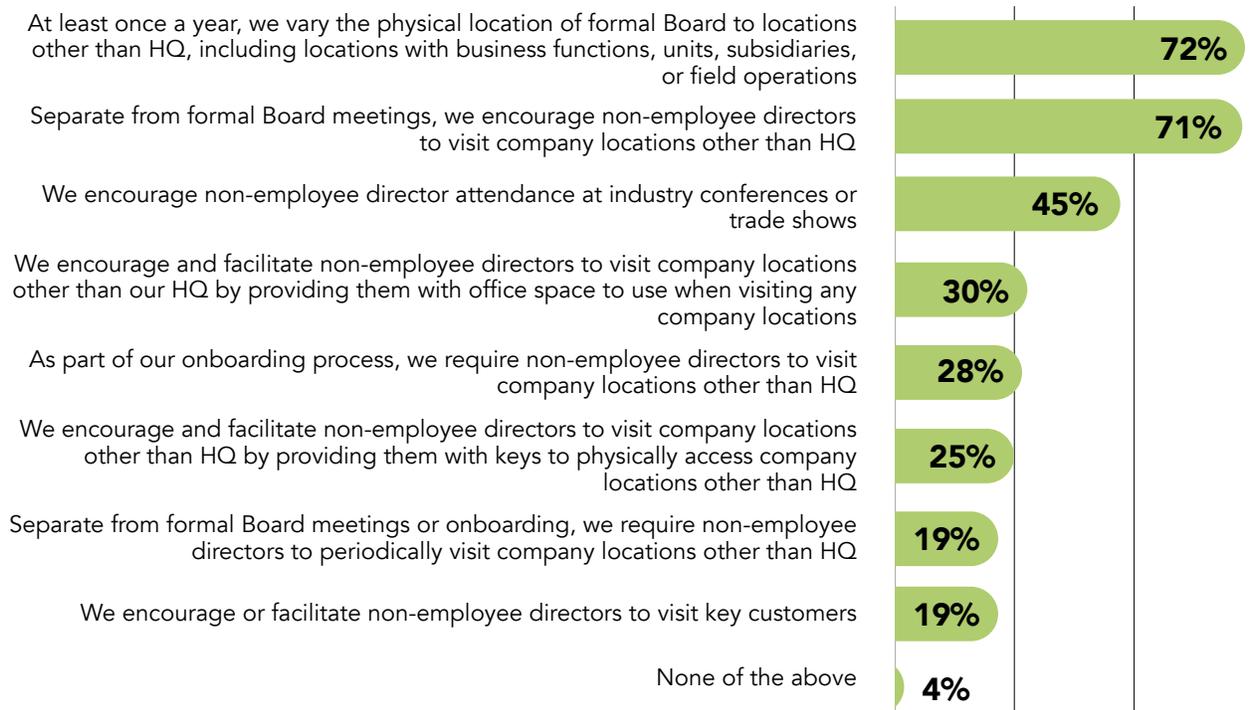| Directors must submit resignation if their employment or professional status changes	Age limits	Limitations on the number of other Boards a member may serve on	Term limits	Our company does not have any tenure limiting mechanisms
7.2	7.3	7.9	9.0	24.9

Increasing Directors' Familiarity with Business Operations

With director turnover, of course, comes the responsibility to onboard new directors and make sure they understand the business and its evolving risk profile. Impressively, nearly half of companies encourage non-employee directors to attend industry conferences. However, it is unclear how many directors actually take advantage of the offer and attend such events.

Many of our honorees do not limit their business exposure process to just new directors. A majority of companies are regularly varying the physical location of formal board meetings to locations other than the organization's primary headquarters, and a similar

percentage also encourage non-employee directors to visit other company locations. When done well, these activities serve several purposes. First, they allow directors to get a sense of the business beyond the corporate headquarters. Second, they allow employees in those regions to gain exposure to the board, potentially aiding succession planning. Finally, they give the board an opportunity to personally support the culture and tone of the organization in meetings at that location. We are encouraged to see 37 percent of honorees requiring such visits as part of onboarding or outside of regular board meetings, and we hope that this figure will continue to rise over time.

Which of the following practices, if any, does your company use to expose non-employee directors to the company's operations and risks? Please select all that apply.

At least once a year, we vary the physical location of formal Board to locations other than HQ, including locations with business functions, units, subsidiaries, or field operations	72%
Separate from formal Board meetings, we encourage non-employee directors to visit company locations other than HQ	71%
We encourage non-employee director attendance at industry conferences or trade shows	45%
We encourage and facilitate non-employee directors to visit company locations other than our HQ by providing them with office space to use when visiting any company locations	30%
As part of our onboarding process, we require non-employee directors to visit company locations other than HQ	28%
We encourage and facilitate non-employee directors to visit company locations other than HQ by providing them with keys to physically access company locations other than HQ	25%
Separate from formal Board meetings or onboarding, we require non-employee directors to periodically visit company locations other than HQ	19%
We encourage or facilitate non-employee directors to visit key customers	19%
None of the above	4%

Facilitating formal interactions between the board and key third parties, such as clients, is a powerful vehicle for educating directors and exposing them to the operations and risks of the business. One out of every five honorees (20 percent) report scheduled meetings

between non-employee directors and priority clients or third parties at least once a year, which represents a small increase over the 17 percent of honorees that reported such a practice in 2018. This remains an area of opportunity for companies.
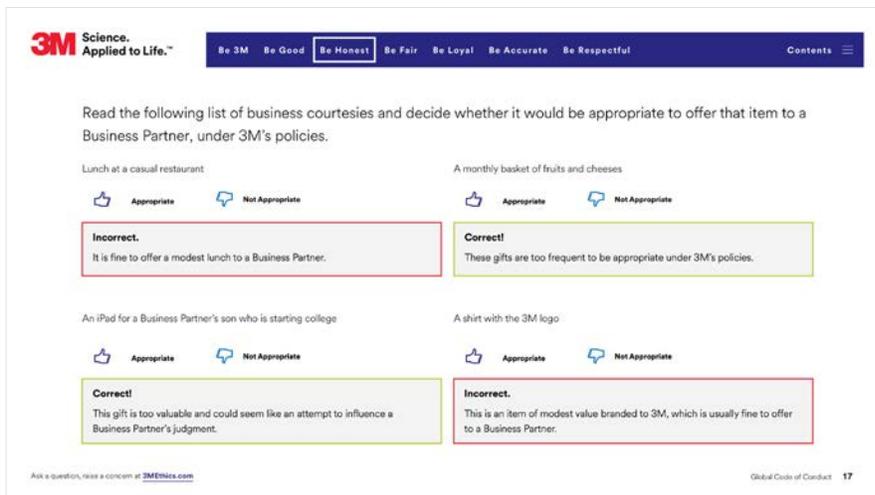
Codes of Conduct

As part of the WMEC process, we reviewed codes of conduct from all honorees. Our review was more qualitative than quantitative, but we saw several noteworthy trends among leading codes.

Leading Codes Are Utilizing Technology

In recent years, codes of conduct have moved beyond static magazine-style layouts to take advantage of the novel capabilities offered by digital media. Whether in PDF or online eBook form, leading codes now make use of videos, interactive learning aids, and interactive navigation elements. Combined, these features make for an engaging experience that keeps readers' attention and helps them better understand the guidance in the code. Other companies are bolstering their code's content by providing supplemental resources—such as Q and A's—on their intranet site.

3M's Global Code of Conduct features interactive learning aids to reinforce behavioral expectations
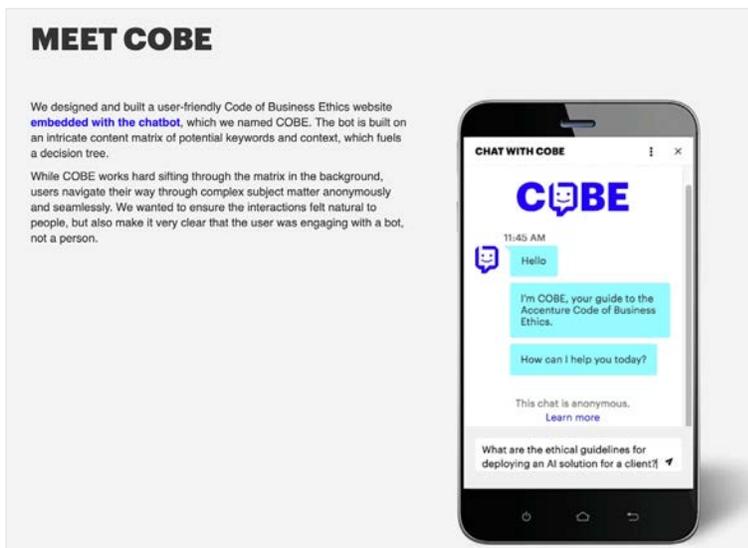
Accenture embedded within its Code of Business Ethics website an interactive chat bot to provide tailored content to each user

Thrivent's Code of Conduct uses an eBook format with scenario videos that illustrate key topics

Tone from the Top Doesn't Just Mean the CEO

Tone from the top has expanded beyond a simple introductory letter from the CEO or Chief Compliance Officer. Leading codes now incorporate messaging from additional executives, as appropriate for the subjects covered. For example, a discussion of fair dealing with suppliers may be accompanied by a statement or short letter from the Chief Procurement Officer. Other codes may opt to include a letter from the Board of Directors

or statements from the CEO throughout the code. This represents a growing awareness that true tone from the top is not achieved by a one-time message from a single executive. Instead, hearing the importance of ethical conduct from diverse voices, applied to diverse topics, helps employees understand the value of ethics and compliance in all areas of the business.

Kimberly-Clark's Code of Conduct supports its message of doing business with integrity with a message from the Chief Financial Officer

The Diversity and Inclusion Director makes an appearance in Old National Bank's Code of Business Conduct and Ethics

Codes Are More Streamlined

Though the length of a code of conduct can vary based on a company's risk profile, many leading organizations are opting to streamline and shorten their codes. A few years ago, it was common for codes to exceed 9000 words, with detailed guidance for each risk area. Now, many updated codes are closer to 7000 words. To achieve this pared-down length, companies are stating guidance in more general, values-based terms and providing links to policies and supplemental materials.

The discussion of conflicts of interest in Kimberly-Clark's Code of Conduct is kept brief using bulleted lists featuring "Essential Commitments"

Microsoft's Standards of Business Conduct focuses content by providing links to relevant policies for employees needing more information
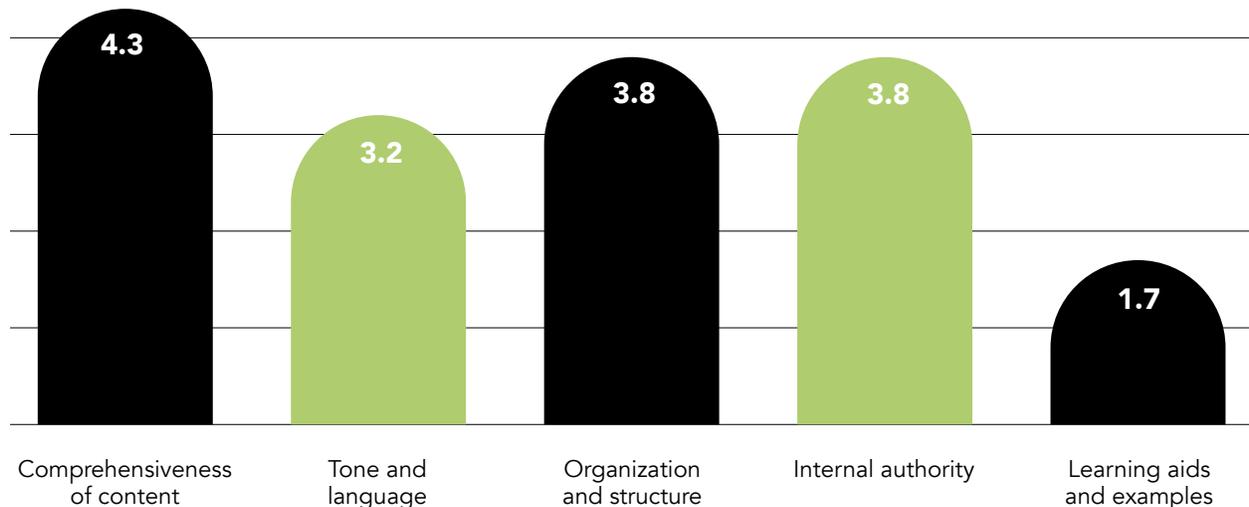
Policies

We gathered data about more than 400 policies from WMEC honorees. Each policy was graded across five criteria, each of which was scored on a 1 ("poor") to 5 ("exemplary") scale:

- Comprehensiveness of content: Does the policy address all pertinent issues and topics within the given subject with sufficient detail, including definitions of key terms? Does it specify where employees should go with questions?

- Tone and language: Is the policy written in clear language that avoids technical jargon or overly complex phrasing and utilizes an inclusive tone?

- Organization and structure: Is the policy structured so that readers can find the information they need? Do policies utilize consistent headings and organization?

- Internal authority: Is there a clear statement of which department is responsible for maintaining the policy?

- Learning aids and examples: Does the policy include real-world examples, charts, FAQs, or other methods of presenting practical guidance?

These scores were then combined for a single score for each policy, and individual policy scores were aggregated into a holistic score for each company. These aggregated policy scores comprised a portion of a company's Written Standards evaluation as part of the World's Most Ethical Companies application process. Policies vary widely based on the company in question, but several overall trends are clear.

Average Honoree Score Across Each Policy Assessment Category

Comprehensiveness of content	Tone and language	Organization and structure	Internal authority	Learning aids and examples
4.3	3.2	3.8	3.8	1.7

Policies Are Written in Complex, Impersonal Language

Across the board, many of the policies we reviewed had one major characteristic in common: they address content comprehensively, but they are difficult to read.

Consistently, policies utilize complex language that could be difficult for the average employee to understand and act upon. Overall, honorees' policies averaged a score of 3.2 out of 5.0 in the Tone and Language category. Many policies focus on legal compliance rather than explaining the cultural importance of ethical conduct. In general, they tend to use impersonal, third-person language that can alienate readers. Among all policies, those addressing insider trading and financial fraud were especially dense and difficult to parse. This raises real questions about the usability of these policies—if they are very challenging to read, no matter how comprehensive their content, employees won't understand what conduct is expected of them.

Policy Structure Is Not Consistent

When it comes to organization and structure, not all policies are created equal. Policies that are more likely to be developed and maintained by the Compliance or Legal functions—such as anti-bribery, conflicts of interest, and gifts and entertainment—tended to utilize a consistent structure with standard headings such as definitions, guidance, and revision history. For policies addressing these risk areas, the average Organization score was 4.2 out of 5.0.

On the other hand, policies about social media, harassment, and discrimination were more likely to lack these elements and averaged an Organization score of 3.5. Based on the subjects of these policies, it's possible that they may be owned and maintained by other departments, such as HR or Marketing. This contrast implies that policy standardization is an ongoing process for many honorees, with work still to be done to ensure that all risk areas are addressed equally.

Policy Quality Varies Widely by Subject

When analyzing policies by topic, clear contrasts emerge. Anti-corruption policies scored the highest, with an overall score of 3.6. These policies are also notable because they generally include learning aids and practical examples, such as lists of red flags, FAQs, and scenarios. In light of recent enforcement of the FCPA and global anti-bribery laws, this isn't surprising. The high cost—both financial and reputational—of violations of anti-corruption laws gives companies a clear incentive to make sure that employees are well prepared to face these issues.

Overall Honoree Policy Average Score by Risk Topic

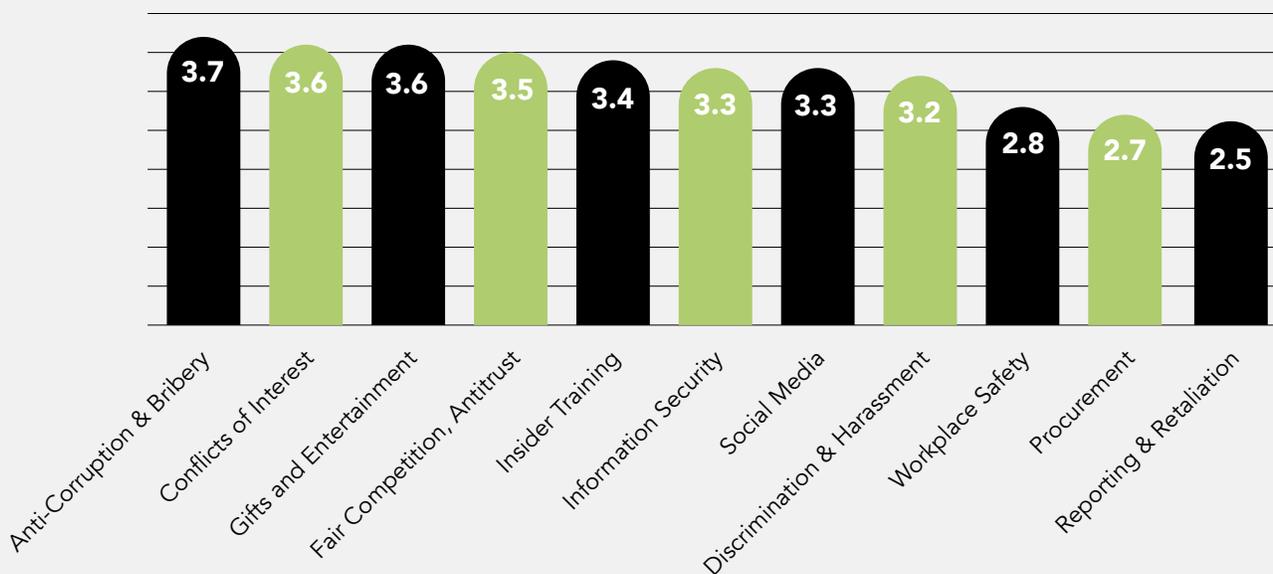| Risk Topic	Score
Anti-Corruption & Bribery	3.7
Conflicts of Interest	3.6
Gifts and Entertainment	3.6
Fair Competition, Antitrust	3.5
Insider Training	3.4
Information Security	3.3
Social Media	3.3
Discrimination & Harassment	3.2
Workplace Safety	2.8
Procurement	2.7
Reporting & Retaliation	2.5

Chart shows aggregate scoring data on risk topics for which seven or more policies were reviewed as part of the WMEC application process. Applicants were asked to submit policies as part of their application, but were not required to submit policies in specific risk areas.

Policies addressing conflicts of interest and gifts and entertainment also scored well in our review and often included learning aids and real-world examples, which help to provide practical applications of the concepts presented.

Though we reviewed comparatively few reporting and non-retaliation policies, they scored noticeably lower than most other policies, averaging a score of 2.5. These policies demonstrated several consistent issues:

- Incomplete content and little practical guidance: Policies addressing non-retaliation rarely provided clear definitions or examples of retaliation, and they did not consistently explain the concept of good faith reporting

- Lack of internal authority: Though many policies did include information about how to contact the reporting hotline, they did not specify how to ask questions about the policy or who owns the policy (e.g., Human Resources, Legal, etc.)

- Poor organization: Even for companies that otherwise utilized a consistent policy template, reporting and non-retaliation policies were often brief, general, and lacking a clear structure

In light of global and pan-industry issues with encouraging reporting and addressing employees' fear of retaliation, these issues become even more problematic. Without clear guidance about what retaliation is and how to ask questions about the policy, it's understandable that employees are reluctant to report and fearful of retaliation.

Leading Policies Are Looking for Ways to Engage Readers

Effective policies are often utilizing innovative, visual strategies for presenting information. Some policies are using the capabilities of PDFs to include roll-over definitions—in other words, when employees hover over a highlighted term, a definition appears. Other policies incorporate charts, call-out boxes, and flow chart diagrams to present information and guide employees through complex situations. These elements increase reader engagement and help to break up text-heavy policies.

Ways to Access Additional EQ Data

Since 2007, Ethisphere has been measuring companies using our Ethics Quotient® Survey (EQ). Our EQ, the foundation of all that we do, has evolved into a tool that global organizations depend upon as an independent, objective, third-party assessment of their programs, policies, and procedures and as a critical element of resource planning. The data we collect is included in our proprietary database, upon which all resulting comparisons, benchmarking reports, consultations, and recognitions are based.

For companies interested in learning more, Ethisphere provides several ways in which companies can leverage our EQ data and insights for practical program improvements:

Compliance Program Assessment
Deep Insight into Your Compliance & Ethics Program Effectiveness

Ethisphere's deepest evaluation offering—its Compliance Program Assessment—offers a comprehensive review, evaluation, and validation of your current programs and practices while fulfilling the Federal Sentencing Guidelines' element of "Periodic Review" of the program.

EQ Benchmarking and Road Map*
A Robust View into Your Program, Policies, and Procedures

Get a more complete understanding of your current program and practices with a robust view into your responses vs. leading and peer companies and present key findings to leadership with the EQ Peer Benchmarking Presentation.

Ethics & Compliance Program Maturity Index
Gauge the Temperature of Your Program

An efficient, self-driven assessment for identifying strengths and gaps of key program elements and benchmark practices against the World's Most Ethical Companies® in the areas of program structure, training and communications, and monitoring, auditing, and risk assessment.

Focused Facts*
Bespoke, Data-Driven Mini-Reports to Tackle Your Most Pressing Compliance Concerns

Focused Facts reports leverage all of Ethisphere's data sets to address your topical questions and concerns. Ethisphere's team of analysts will build a concise report customized to your most pressing compliance, ethics, and cultural concerns.

Measuring and Assessing Culture
Gain Insights into Your Most Critical Asset— Your Employees

Evaluate the effectiveness of your communication, training, and compliance efforts and the willingness of your people to raise concerns against our Eight Pillars of Ethical Culture. Using a proprietary library of survey questions, Ethisphere manages the complete administration of the survey, provides a qualitative analysis of your assessment findings, and gives you the tools to segment and explore areas of strength and opportunity across your enterprise.

*Indicates a service that is included with Ethisphere's Business Ethics Leadership Alliance (BELA) membership

For more information, contact Jonathan Whitacre at +1 (615) 210-2876 or jonathan.whitacre@ethisphere.com.

ABOUT ETHISPHERE

Ethisphere is the global leader in defining and codifying the standards of ethical business practices that fuel corporate character, marketplace trust, and business success. Ethisphere has deep expertise in advancing business performance through data-driven assessments, benchmarking, and guidance.

Our Ethics Quotient data set enables the ability to benchmark against the ethics and compliance practices of leading companies across sectors and industries. We also work with the world's largest companies to assess and enhance ethical culture capital with the insights from our culture assessment data set, which represents the views of millions of employees worldwide and is grounded in our Eight Pillars of Ethical Culture. Ethisphere honors superior achievement through its World's Most Ethical Companies recognition program and by showcasing best practices in *Ethisphere Magazine* and at global events. We also facilitate the Business Ethics Leadership Alliance (BELA), a global community committed to solving the big challenges of business integrity together. More information about Ethisphere can be found at https://ethisphere.com.

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6991 E. Camelback Rd., Ste. B-210 | Scottsdale, AZ 85251
Phone: 888 229 3207 | Fax: 480 219 7670

www.ethisphere.com