Implementing Sustainability:

THE ROLE OF LEADERSHIP AND ORGANIZATIONAL CULTURE

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Executives recognize the importance of social and environmental responsibility—corporate sustainability—but they seldom implement it successfully. The challenge lies in how to actually integrate sustainability into operational and capital investment decision making and implement it successfully in large, complex, for-profit organizations. The financial executive plays a vital role.

Top management typically cascades these management decisions down because sustainability impacts are often local, so usually only a small number of these decisions are made at corporate headquarters. As individual managers at the business units, geographical units, and facilities make these decisions, they also must make the appropriate tradeoffs regarding social and environmental impacts vs. financial ones. Typically, the vice president of sustainability, who reports to the CEO, requests improved sustainability performance, while the CEO and CFO demand improved financial performance. At the same time, a company provides little guidance and support to senior- and middle-level operations managers to aid in the decision making and tradeoffs. How can they manage this challenge successfully?

Field Study Brings New Findings

In the January 2008 issue of *Strategic Finance*, Marc J. Epstein presented the Corporate Sustainability Model, a comprehensive approach for examining, measuring, and managing the drivers of corporate sustainability. The model can help managers incorporate a sustainability strategy into daily operations and link that strategy to specific actions that improve both sustainability and financial performance.

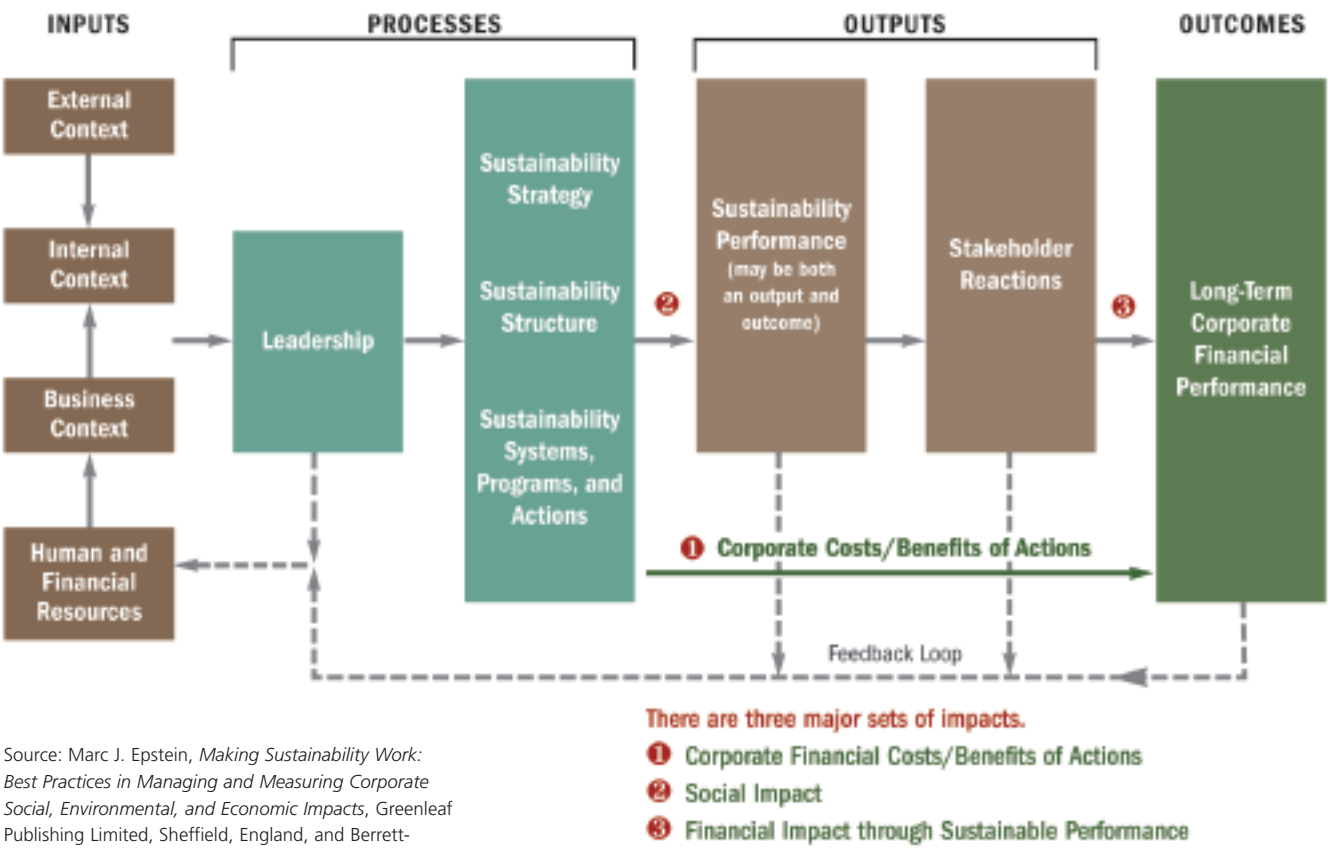
Epstein argues that, to improve the sustainability strategy implementation process, managers should carefully identify and measure key performance drivers included among the various inputs and processes. The drivers of the model include:

- External context (regulatory and geographical),
- Internal context (mission, corporate strategy, corporate organizational structure, organizational culture, and systems),
- Business context (industry sector, customers, and products), and
- Human and financial resources.

The inputs guide leaders in making decisions so they

Figure 1: The Corporate Sustainability Model

Organizational Culture (Internal Context), Leadership, and People as Critical Drivers of Sustainability Success



Source: Marc J. Epstein, *Making Sustainability Work: Best Practices in Managing and Measuring Corporate Social, Environmental, and Economic Impacts*, Greenleaf Publishing Limited, Sheffield, England, and Berrett-Koehler Publishers, Inc., San Francisco, Calif., 2008.

can develop an appropriate sustainability strategy; set up aligned structures, systems, and programs; and take action. The managerial actions lead to positive or negative sustainability performance and stakeholder reactions, ultimately affecting long-term corporate financial performance. This model should help managers better analyze and manage these drivers as well as pursue social and environmental impacts more effectively. Figure 1 illustrates the Corporate Sustainability Model.

Recently, the Foundation for Applied Research (FAR) of the Institute of Management Accountants (IMA®) sponsored a research study to examine how leading corporations integrate economic, social, and environmental impacts into day-to-day management decision making. The research focused on four companies:

- **Nike**, the world's leading designer, marketer, and distributor of athletic products and clothing;
- **Procter & Gamble** (P&G), one of the world's leading branded consumer products companies;
- **The Home Depot**, the world's largest home-improvement specialty retailer; and
- **Nissan North America**, a unit of Nissan Motor Co., a leading global auto manufacturer.

These companies have reputations for leading practices in managing sustainability and have high ratings on various indexes on sustainability performance. We conducted open-ended, semi-structured interviews with senior managers, business unit and facility managers, geographical unit managers, functional managers, and sustainability managers. The study investigated how managers currently make tradeoffs and simultaneously manage social, environmental, and financial performance. We also looked at systems and performance measures that they use to facilitate these decisions and at the characteristics of organizations and their environments, their formal and informal support systems and processes (including performance evaluation, rewards, organizational culture, leadership, etc.), and initiatives that facilitate managing social, environmental, and financial performance simultaneously. The study also attempted to better understand the role of hard or soft implementation systems. Hard systems are the formal systems that include structure, performance evaluation, and incentive systems that motivate employee behavior. Soft systems are the informal systems such as organizational culture, leadership, and people.

It's these informal systems—organizational culture, leadership, and people—that nurture a company's drive for sustainability. Although sensitive to stakeholder concerns and impacts, these leading companies are committed internally to improving corporate sustainability performance. While generally considered a significant tool to implement sustainability and align the corporation's interests, formal implementation systems have a secondary role in implementing sustainability programs successfully. All four companies incorporate sustainability issues in their corporate strategies, they have specific sustainability strategies and aligned organizational structures, and they have in place performance measurement systems with some social and environmental metrics. But leadership and organizational culture are the most crucial determinants in successfully managing the various tradeoffs that middle managers face when they try to manage social, environmental, and financial performance simultaneously. The Corporate Sustainability Model highlights the following drivers: the internal context with the organizational culture, leadership, and human resources.

We'll describe how Nike, Procter & Gamble, The Home Depot, and Nissan North America are using leadership and organizational culture to encourage employees to pursue and drive organizational success in sustainability. Only after a company uses these informal or soft systems can it use the formal or hard systems of strategy, structure, and programs to improve success.

Managing Social, Environmental, and Financial Performance Simultaneously

How to manage the paradox of improving social, environmental, and financial goals simultaneously is one of a company's biggest challenges. Integrating corporate social, environmental, and financial impacts into operational and capital investment decisions comes with a lot of tension. While social and financial initiatives may benefit one another in the long term, they're often conflicting in their need for resources and agendas in the short run. Also, clear, measurable, short-term metrics apply to financial initiatives, whereas measurements of social performance are often uncertain and long term. Sometimes there are win-win situations, such as when waste and emissions are reduced, that save both company costs and environmental damage. But often the decision alternatives are seen as tradeoffs, and managers throughout the business units and facilities must struggle to evaluate social, environmental, and financial impacts. At the end of the day, they make decisions while being accountable for excellent performance in both.

In our study, however, managers told us they didn't see the tradeoffs as difficult, either because they prioritized

financial performance or because their companies could accomplish both at the same time. The Home Depot, for example, doesn't view the tradeoffs between sustainability goals and business goals as problematic. They rarely see a tradeoff as a win-lose situation; when this is the case, win-lose tradeoffs are typically resolved in favor of business goals. In most cases, there are win-win situations. In fact, whenever an environmental or social issue becomes important to the customer or the public, it becomes important to The Home Depot, and addressing it becomes a win-win situation. Essentially, the belief is that "We do the right thing, and it is good for business as well." When meeting a more stringent regulatory or company-set environmental or social standard would require additional costs, managers would work together to identify areas where they could reduce other costs.

At Nike, tradeoffs are only in the short term. For example, using environmentally preferred materials may increase some manufacturing costs, but, by reducing waste, the company decreases costs. A company can reduce costs using Considered Design, which is Nike's program to improve product sustainability by focusing on design. Nike's goal is to fuel constant improvements in its design and production processes that lessen its impact on the environment and society, using sustainability as a source of innovation. Nike designers successfully innovate in how they use various materials. The choice of design and materials has produced dramatic decreases in footwear and packaging waste, which means a reduction in the use of potentially harmful chemicals while increasing the performance of the product.

P&G, too, sees innovation as the solution to the sustainability challenge. P&G managers have widened their organizational perspective to see the broader picture and capture benefits beyond a particular issue or cost. They strive to create products that enable consumers to be more environmentally sustainable. Improving efficiency of the entire product life cycle from cradle to grave is a major focus of P&G's sustainability efforts. As one senior executive stated, "We're values-based, innovation-driven, and we see the business value of sustainability." P&G thus attempts to accomplish both environmental and financial goals and performance simultaneously. For Nissan North America, the evaluation of environmental and financial impacts typically doesn't present a tradeoff because of the company's declared focus on energy-usage reduction for Nissan and its customers. This is usually a win-win scenario.

Social and environmental considerations are deeply embedded in decision making at Nike, Procter & Gamble, The Home Depot, and Nissan North America. Nike, for example, developed a strategic approach to corporate responsibility (CR) that emphasized value creation, collaboration with business units, and proactive strategic planning. This is why managers believe that they aren't typically making tradeoffs and are more often recognizing win-win situations. Environmental win-wins (decisions that simultaneously benefit the environment and corporate profits) are often more noticeable than social win-wins. This may be because of more measurement

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and evaluation techniques as well as performance measures in place for corporate environmental impacts than for most of the social impacts managers typically confront. But these leading companies have made many tradeoffs spontaneously because they've incorporated the concerns for social and environmental impacts into the culture. The role of leadership in accomplishing this is crucial.

The Role of Leadership

In all four companies, there are fewer conflicts for senior and middle managers in balancing social, environmental, and financial performance because these conflicts are resolved higher up in the organization and are well integrated into the informal systems. Upper management has bought in to the benefits relating to sustainability. Thus people are able to make certain tradeoffs because they know their leaders will be supportive.

Corporate responsibility is one of Nike's nine strategic priorities. The CEO and other company leaders support CR intensively and consider it an enhancing element in reaching strategic goals. In fact, leadership engagement is number one. "Making a sustainable decision that negatively impacts margins is not so wrong, but they have to inform me because we can offset this somewhere else," one vice president explained. "I want to give guidance to subordinates because I don't want to have them struggle with it [the tradeoffs related to making social, environmental, and financial decisions]. And we need to teach them because all these decisions cannot be done by me

alone." This training takes place through information sharing and collaboration. People learn as they become part of the process where leaders make decisions.

Similarly, at P&G the focus on sustainability starts with a clear desire on the part of the leadership to make something happen. Leadership is one of its core values, and P&G's leaders are responsible for successfully integrating sustainability into the rhythm of P&G's business. "We aim to make sustainability something the business units *want* to do because it helps build the business," stated one vice president. Once people understand the goal, creativity and innovation immediately follow.

The Home Depot views the job of the individual store manager as among the most significant in the organization. Along with the CEO, they are committed and passionate about sustainability, volunteerism in particular.

The Nissan CEO sets the corporate direction and centralizes *corporate social responsibility* (CSR). The company develops a midterm plan that addresses the question "How do we grow in harmony with sustainability?" and publicly commits to a plan. In Nissan North America, the managers' role in leadership is to promote stakeholder value with specific orientation to environmental concerns. There's the belief that it's very important to get people in the decision-making roles who have the mind-set of "Now we have limited natural resources." Leadership support in promoting sustainability is of great importance.

The Role of Organization Culture

A typical culture that builds on sustainability helps managers and other decision makers deal with the tradeoffs that the simultaneous management of social, environmental, and financial goals often causes. At Nike, P&G, The Home Depot, and Nissan North America, the corporate culture emphasizes norms critical for innovation, such as openness, autonomy, initiative, and, in many cases, risk taking.

The Home Depot's culture, for example, is all about an entrepreneurial high-spiritedness and a willingness to take risks, as well as a passionate commitment to customers, colleagues, the company, and the community. "Orange blood" runs through the veins of its associates. Employees view sustainability performance as vital to The Home Depot's long-term financial success even though incentives aren't based on social and environmental performance. Also, many Home Depot employees are environmentally and socially conscious and have been the driving force of some environmental initiatives, such as the Framing Hope project, which donates to nonprofit organizations damaged and outdated product that would otherwise go to landfills. The company strengthens and transmits its culture by maintaining transparency and open lines of communication. It runs a weekly televised show for store and department managers that discusses issues of interest for company employees that may include policies, products, programs, personnel, and the like, and that provides an opportunity for better communication throughout the company. The CEO can talk to employees and get feedback from them. The Home Depot also provides a mechanism for employee feedback through the company's intranet.

P&G, an innovation-driven and values-based company, values everyone's opinion, so there's a good deal of discussion, even at the lowest level. It does things from the bottom up and by consensus, and it focuses on "the right thing to do" even if sometimes that's more expensive. P&G took this motto from one of its core values—integrity—that says, "We always try to do the right thing." Since people come in young, move through P&G, and create organic networks, there's a strong sense of trust and unity. Like The Home Depot, P&G promotes primarily from within, which makes it easier to build a strong corporate culture since most employees have a long tenure with the company. P&G is also encouraging sustainability behavior and culture through another core value—ownership—that expects employees to act like owners, treating the company's assets as their own and behaving with the company's long-term success in mind.

A lot of Nike employees intuitively believe that sustainability is the right thing. This mind-set builds the brand. Sustainability is integrated into the rhythm of the business, including employee engagement and encouraging employees to contribute their ideas. Young employees, many of them ex-athletes with a strong spirit of competitiveness and entrepreneurship; young customers; and a strong culture around sustainability, success, and innovation reinforce and support the sustainability actions.

At Nissan North America, the mind-set and actions focus on environmental impacts. Environmental issues cascade down to the analyst level. "I'd like to think our culture has evolved such that we weave in environmental concerns," one senior manager said. To shift mind-sets, 99% of the staff has gone through green training to gain understanding and sustainability awareness, which the company views as integral for acceptance of corporate social responsibility initiatives. At the core of the company's corporate culture is the Nissan Way, which includes a

"cross-functional, cross-cultural" business approach and a "commit and target" strategy. Nissan expects to achieve profitable, sustainable growth into the future. Creating a corporate culture that values the environment continues to be one of Nissan's major objectives. Activities vary across the plants, but they generally include monthly newsletters to raise staff awareness about the environment, participation of the plant's workforce in facility inspections and lectures, participation in environmental management system training, etc.

Sustainability is a personal issue at all four companies. They want to do something good. Company leaders at Nike don't tell people what to do but rather—"just do it." The P&G motto is "go and make it happen," so employees find a way to make it work. These aren't companies of dictates.

These companies perform annual culture assessments and encourage employees to participate in anonymous surveys. Employees participate because they've already experienced that their voices were heard. The Home Depot's CEO, for example, reviews all employee suggestions—some 300 to 400 per week—and posts responses to many of them. Nissan regularly carries out worldwide employee surveys, gauging employees' attitudes and using the survey results to help improve the company's management and corporate culture.

The Home Depot, in particular, has found volunteerism to be a critical building block of corporate culture. The company espouses eight core values: excellent customer service, entrepreneurial spirit, taking care of our people, respect for all people, building strong relationships, doing the right thing, giving back, and creating shareholder value. It views giving back as the most important. According to a senior vice president, "There's a strong cultural tie to volunteering. If we post a sign that says 'sign up for KaBOOM [a volunteerism effort to build children's playgrounds]…' it fills up fast. If we mandate it, it loses its effectiveness." The company doesn't feel the need to additionally promote sustainability, and forcing things would push store managers to just "check the box."

There's a strong spirit of volunteerism at the other three companies, too. Where many companies struggle to get employees involved, Nike searches for programs to keep pace with employee activism. Through volunteerism, P&G provides ongoing support, sponsorship, and leadership for many civic, cultural, and nonprofit organizations across all geographies. Nissan volunteers regularly join local cleanup efforts to help communities protect their environment. In fact, Nissan plants need to address cooperation and coexistence with local communities as one of their goals in their yearly plans.

Soft vs. Hard Implementation Systems

The study's finding of the importance of soft or informal systems and processes for successful management of sustainability might come as somewhat surprising. Most of the literature on management control and strategy implementation focuses on hard or formal systems and processes, such as organizational design, performance evaluation, and incentive systems that motivate employee behavior. But these systems alone haven't typically been successful in implementing corporate sustainability strategies. Performance measurement, incentive, and reward systems can be critical tools to implement sustainability and align the interests of the corporation, senior managers, and all employees. Yet they must usually be part of a broader set of systems aimed to motivate and coordinate employee actions and corporate culture.

Formal systems that measure and reward performance and encourage employees to pursue sustainability are often necessary to improve social and environmental impacts, communicate the value of sustainability to the organization, and hold employees accountable for their sustainability efforts. But to be effective they need to be built on principles such as measurability, objectivity, and fairness. Some companies explicitly state that they don't want to measure sustainability impacts directly because they are difficult to capture. Or they don't want to invest the effort to measure social impacts because managers intuitively believe that their sustainability efforts work. Rather, they choose metrics related to outcomes reasonably close to the cause-and-effect relationships chain. For example, measures related to the quantity of emissions are often considered satisfactory without going the next step to examine the various health and other social impacts on the population.

Companies sometimes consider social impacts more difficult to measure than financial results because they're often intangible, hard to quantify, and difficult to attribute to a specific organization, and they have a long time horizon. This difficulty often presents obstacles to producing compelling evidence of impact and mission achievement. Though increased sustainability measures are available and are often a valuable component in sustainability implementation, some leading companies haven't focused on them—or are only now focusing on measures of success. Instead, they've focused on getting

the informal systems right first before concentrating on the measurement.

For example, The Home Depot doesn't attempt to directly measure brand, community, or business impact of its sustainability efforts. There's some sense that these things are the right things to do, and, if they're measured, associates might see them as additional job requirements that they must monitor and manage. When The Home Depot evaluates a new initiative with a potential for significant sustainability outcomes, it doesn't attempt to measure specific environmental or social outcomes directly. Instead, it captures relevant outcomes in its assessment of three types of risks: business, customer, and brand. At the moment, Nike doesn't tie incentives directly to sustainability, but the overall intention is to increasingly formalize and institutionalize many of the informal processes.

Commitment to social and environmental concerns must be communicated consistently, both in words and actions.

While these companies have a formal sustainability strategy, structure, and systems in place, it seems that the internal context has a stronger impact on behavior. Corporate social responsibility or sustainability departments play an important role in educating other business units about *why* the company should engage in sustainability efforts. They do this through educational and other efforts to influence the organizational culture and values. In addition, sustainability departments influence *how* the company acts to include sustainability in decision making, such as developing tools for incorporating sustainability. Also, as we mentioned earlier, both P&G and The Home Depot emphasize promoting from within, which builds a strong culture.

If they don't use these methods, companies must find other ways to sensitize new employees to the culture. This is often challenging. When employees have a sense of long-term commitment, they're willing to volunteer in the long-term interests of the company. All four of the companies we studied educate and train individuals throughout their organizations to be sensitive to sustainability issues, and they have staff dedicated specifically to sustainability programs.

The sustainability strategy is only a minimum enabler for improved sustainability performance. Best-practice companies will also have other formal and informal systems and processes in place, of which leadership, organizational culture, and people may be among the most important drivers of effective sustainability decision making. CEOs should communicate—and overcommunicate—the importance of sustainability and establish a culture of integrating sustainability into day-to-day management decisions. Commitment to social and environmental concerns must be communicated consistently, both in words and actions. At Nike, one vice president specifically underlined the importance of leadership consistency: "Leaders must be consistent. Consistency is believed to be more important than refined measures on environmental impact and compliance."

A Win-Win Opportunity

An organizational culture supporting sustainability decisions can inspire and motivate employees to take sustainability obligations seriously. In addition, in their recruitment and development practices, companies may seek to create in their employees a passion and commitment to sustainability. This leads to contributions that are good for society, the environment, and the company's bottom line. **SF**

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