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Organisational culture as part of effective governance and performance - best practice guidance for UKGI shareholder teams and NEDs

In representing government's shareholder interest, UKGI proactively challenges and supports its portfolio assets' (its 'Assets') effective governance and performance.

Good organisational culture is a key component of effective governance. It supports better and effective performance¹, and decreases risk. Conversely, bad organisational culture, if not recognised and addressed, can lead to significant reputational damage and other impacts for an organisation, for example, FIFA² and Carillion³.

This guidance note provides an overview of:

1. What is an organisation's culture, including in the context of purpose
2. What we expect of our Assets in this area
3. What we expect of our NEDs and shareholder teams in this area, and how they should promote and challenge in this area
4. How to assess and measure culture

¹ <https://www.managers.org.uk/~media/Files/PDF/Checklists/CHK-232-Understanding-organisational-culture.pdf>

¹ [a-duty-to-care_2016-evidence-of-the-importance-of-organisational-culture-to-effective-governance-and-leadership_tcm18-14220.pdf \(cipd.co.uk\)](https://www.managers.org.uk/~media/Files/PDF/Checklists/CHK-232-Understanding-organisational-culture.pdf)

² <https://www.bbc.co.uk/sport/football/29603170.amp>

³ <https://www.peoplemanagement.co.uk/news/articles/rotten-corporate-culture-carillion#gref>

Section 1: What is an organisation's culture in terms of good governance, and how does it sit alongside purpose

Directors have a duty to establish the company's purpose and culture under Principle B in the Corporate Governance Code, which states, "The board should establish the company's purpose, values and strategy, and satisfy itself that these and its culture are aligned. All directors must act with integrity, lead by example and promote the desired culture."

The Financial Reporting Council (FRC)⁴ defines **culture** as "a combination of the values, attitudes and behaviours manifested by a company in its operations and relations with its stakeholders". Organisational culture can also be defined as the collection of values, expectations, and practices that guide and inform the actions of a company and their stakeholders, or more simply "**the way we do things around here**"⁵.

The Chartered Management Institute⁶ defines **purpose** as "an organisation's **meaningful** and **enduring reason to exist** that aligns with long-term financial performance, provides a clear context for daily decision making, and unifies and motivates relevant stakeholders."

A company's purpose, values and culture should be clearly defined and aligned with each other.

Below are some positive and negative indicators we have observed, drawing on colleagues' experience, which may be helpful in making an initial assessment of an organisation's culture:

A healthy culture requires...	Positive indicators in an organisation	Negative indicators in an organisation
Effective leadership	Well-respected CEO / Senior Management team	Dominant CEO who doesn't actively develop followership
Transparency	CEO and / or Senior Leadership Team (SLT) who share Management Information transparently, including areas of concern	Command and control environment where information must be prised out
Openness to challenge	CEO / SLT actively seek out ideas of others and graciously act on feedback	CEO / SLT oversensitive, defensive or arrogant
Pragmatic control	Operating within the hard-red tramlines but flexible where necessary with others	Tolerance of frequent breaches in ethics, code or regulation
Established purpose	Organisational culture is commonly understood, bought into, and frequently discussed	Poor understanding of culture
Shared values	Pride in and shared understanding of importance of values	Values not well known in organisation and / or lack of identification with them
Team orientation	All employees talk in terms of "we", not "I" and "the organisation" separately	Overly competitive working environment

⁴ <https://www.frc.org.uk/getattachment/3851b9c5-92d3-4695-aeb2-87c9052dc8c1/Corporate-Culture-and-the-Role-of-Boards-Report-of-Observations.pdf>

⁵ Balogun and Johnson

⁶ <https://www.managers.org.uk/knowledge-and-insights/article/how-to-define-your-business-purpose-2/>

<i>Evolution</i>	Acceptance that as the organisation evolves, culture will need to follow suit	Employees commonly harp back to halcyon days of the past
<i>Continuous improvement</i>	Innovation is actively encouraged and rewarded	Same ideas are recycled on a regular basis
<i>Diversity of thought</i>	Board papers incorporate thinking from all levels and parts of the organisation	Similar small group of people lead all strategic thinking
<i>Inclusivity</i>	All voices are heard, and alternative views are considered in decision-making	Siloed working and low employee engagement
<i>Resilience</i>	Organisation bounces back rapidly from setbacks and exhibits high energy	Short-term focus on getting the job done and unwarranted pressure to meet targets
<i>Fairness</i>	Employees feel treated equitably	Issues around remuneration and opportunity for progression
<i>Positive behaviours</i>	Board, CEO and SLT role model behaviours aligned to values and this feeds through to the organisation	Frequent grievances, poor attendance and high turnover
<i>Good communication</i>	Open channels of communication up, down and across the organisation	Information shared on a need to know basis

The indicators of good or bad organisational culture continue to evolve and will always be specific to an organisation and its purpose. However, there are recognised indicators of issues with culture; the [Investment Association](#) published a culture framework which provides practical insights and self-assessment processes.

2. What we expect of our Assets in this area

We expect our Assets to devote significant time and resources on an ongoing basis to planning, developing and sustaining their organisational culture.

Within the FRC Report on Corporate Culture and the Role of Boards, there are different responsibilities at board level within an organisation for ensuring good culture.⁷ Summarised below are the recommendations:

The Chair should:

- ✓ Lead the Board in promoting a culture of openness and debate in line with Principle F of the [Corporate Governance Code](#), and this should be reviewed in their annual appraisal.

The Board should:

- ✓ Observe and assess the company's culture for alignment with purpose and values.
- ✓ Engage in ongoing dialogue about organisational culture.
- ✓ Develop a common and consistent language around culture.
- ✓ Reassess and evaluate the culture on a regular basis.
- ✓ Hold the CEO accountable for driving and influencing the culture of an organisation. (UKGI should be mindful of this in our shareholder roles when appointing, remunerating and reviewing their performance)
- ✓ Periodically review MI on engagement, absenteeism, turnover, exits, whistleblowing, grievances and poor performance as well as staff survey results.
- ✓ Ensure the organisation updates HR procedures and policies including aligning incentives and rewards with culture, particularly when setting the policy for executive remuneration (Provision 32 of the [Corporate Governance Code](#)).
- ✓ Ensure the organisation builds, embeds and monitors a robust and healthy risk culture. This can be shaped by the hard controls (policies, governance, compliance) and soft controls (training, communications).
- ✓ When cultural issues are found, encourage management to use root cause analysis to understand what the issue is and take effective action to correct it.
- ✓ Look to identify and share areas of external good practice, to help drive a healthy culture and reinforce the company values.

The Board Committees should support the Board in assessing and improving culture:

- ✓ Remuneration Committees should address the alignment of executive remuneration to culture to drive behaviours consistent with the company purpose, values and strategy (Provision 40 of the [Corporate Governance Code](#)).
- ✓ Risk Committees should be in a position to support boards in evaluating alignment between incentives, values and behaviours.
- ✓ Audit Committees should be able to seek internal audits to ensure assessment and monitoring of culture is continually undertaken.

⁷ [Corporate Culture and the Role of Boards \(frc.org.uk\)](https://www.frc.org.uk/corporate-culture-and-the-role-of-boards)

Below are case studies examining how two organisations decided to drive a change in culture:

Case study: Post Office Ltd


Following a long running dispute between Postmasters and the Post Office the business committed to reset its relationship with Postmasters and its culture.

Improvements were driven by the appointment of a new CEO who made fixing the culture one of their main objectives.

POL identified the need for a wholesale culture change. As part of this several commitments made were by POL to Postmasters.

This included initiatives such as:

- Increasing Postmaster remuneration as many felt they had not received fair pay alongside POL's profits
- Putting the relationship with Postmasters at the heart of management decisions
- Appointing two Postmasters to the Board so that Postmasters voices are better represented at the highest levels within POL
- Strengthening the management team including the creation of the role of Postmaster Director
- Improving stakeholder engagement, including meeting monthly with the Minister, establishing Quarterly Shareholder Meetings, and attending Postmaster curry nights
- Formalising many of these in POL's Framework Document, as well as updated Articles of Association
- Using the [OHI](#) reporting framework to understand, monitor and improve culture
- Reviewing and upgrading POL's core processes as they affect Postmasters with the help of external advisers



IRRELEVANT

3. What we expect of our NEDs and shareholder teams in this area, and how they should promote and challenge in this area

Considerations of culture are relevant across the core activities we carry out in our standard shareholder role, as framed by our [Portfolio Operating Principles](#). Shareholder teams need to consider the health of their Asset's culture on a regular basis, as well as at key decision-making points or reporting events.

The following sets out minimum actions that shareholder teams should undertake in relation to each of the relevant Portfolio Operating Principles in terms of culture:

Principle A: Establish and maintain appropriate and effective corporate governance foundations which govern the Department-Asset relationship

- UKGI shareholder teams should seek to ensure that an emphasis on culture and values is a feature of the Chair's letters that Departments issue annually to Asset Chairs

Principle B: Promote effective objectives, business planning and performance against business plan:

- UKGI shareholder teams and NEDs should be able to articulate what the culture, purpose and the values of an Asset are, and how an Asset's culture is embedded in its strategy and business plan

Principle C: Promote strong corporate capability

- UKGI shareholder teams should understand how well internal risk and whistle blowing processes and systems are complemented by the right behaviours in order to be effective – in particular teams should note the related Guidance Notes on *Risk Management* and *Whistleblowing Policies and Complaints*, in terms of how culture is a central consideration for these aspects of corporate capability

Principle D: Promote effective leadership (high quality boards and senior management)

- UKGI shareholder teams should use board effectiveness reviews to assess whether an Asset is acting in accordance with the culture and values it articulates. As part of assessing a board's effectiveness, UKGI should seek to assure itself that the Asset's culture is open, transparent and one where "bad news" can be surfaced without defensiveness, with the Board having the ability to take a detached view of the culture in the Asset (including how the leadership is living the culture and values)
- UKGI shareholder teams should seek to ensure that performance reviews of Chairs and CEOs also focus on culture and values.

Principle E: Promote effective relationships between the Department and the Asset

- UKGI shareholder teams should table "culture" as a regular agenda item at quarterly shareholder meetings and in discussions with the Asset's CEO and Chair.
- Where UKGI has concerns or misgivings related to culture, this should be a red flag for both the UKGI NED and shareholder team. Extra vigilance in terms of monitoring these concerns should be undertaken, including formal escalation to the Asset's Chair, and alerting the relevant Permanent Secretary and/or Ministers as appropriate

More generally NEDs and shareholders teams should consider if there are issues or misalignment with their Asset's culture, purpose or values.

A list of questions that shareholder teams and NEDs can use to consider and challenge culture in their Asset is provided at **Annex A**.

4. How to assess and measure culture

There is not a unified set of measures to assess culture. However, there are several frameworks that can be used to enable comparisons across the organisation and measure improvements over time⁸. Please see **Annex B** for the different frameworks.

Boards should discuss and agree the most suitable metrics and KPIs, to monitor and assess good culture that fit their organisation depending on the outcomes they are looking to achieve. We have highlighted in red minimum indicators shareholder teams and NEDs should expect to see:

- **Regular employee engagement surveys**, (from pulse, open feedback and focus group sessions) giving quantitative and qualitative metrics for employee engagement, motivation, and satisfaction
- **Absenteeism data**, on how often staff are off sick (including for stress), and whether there are any underlying reasons
- **Staff turnover** and retention rates within the company
- **Employee Assistance Programme** participation
- **Staff training data** including data on personal development or skills to enhance performance and if this is by choice or recommended through managers
- **Exit interview** information on culture and personal experience from leavers
- **Whistleblowing incidents, grievance and 'speak-up' data**, with numbers and types of cases
- **Poor performance data**
- **Diversity and Inclusion (D&I) data**, in relation to staff composition and recruitment by organisational area and by different characteristics including gender and ethnicity
- **Key Behavioural indicators**, which can include monitoring employees' motivation, satisfaction, commitment, and loyalty to the organisation, indicating how good or bad the culture is.

Please get in touch with IRRELEVANT for any queries.

⁸ <https://www.cipd.co.uk/knowledge/culture/working-environment/organisation-culture-change-factsheet>

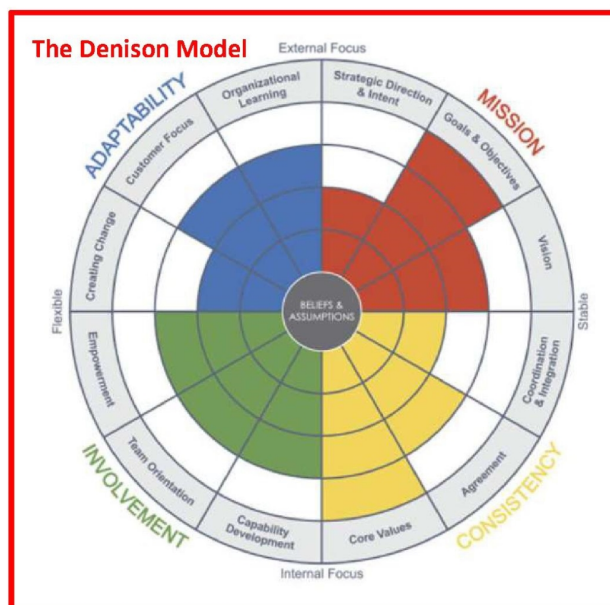
Annex A – Suggested questions teams can use to consider and challenge culture in their Asset

Key UKGI NED and shareholder questions to ask to ascertain culture wellbeing:

- Does your asset have a clear purpose, values and culture which are aligned?
- Does the Board understand its duties in relation to organisational culture?
- What is the external reputation of your company's culture?
- How is your asset encouraging honest feedback about the culture?
- Are there weaknesses in the culture that need improving?
- Is culture considered in remuneration incentive schemes?
- What risks does the current culture create for the organisation?
- Is culture on the Board agenda? Is it discussed in enough depth?
- Do the Board Committees support the Board on culture?
- Could the Board benefit from a specific conduct, ethics or culture Committee?
- Is the CEO willing to listen, take criticism and let others make decisions?
- Does the Chair set the tone from the top?
- Do the Board understand the employee perspective on their organisational culture?
- When cultural issues are found do management use root cause analysis?
- Is organisational culture measured/calibrated in the Board effectiveness review?
- Does the annual report include the Board's activities in relation to culture and any action taken?
- What is the company's approach to investing in and rewarding its workforce, in relation to culture?
- Are cultural questions included in employee surveys?
- Does the Internal Audit plan include an assessment of culture?

Annex B – Frameworks for measuring culture

- [Organisational Health Index](#) (OHI) designed by McKinsey and Company provides some insights into what key indicators can be used in measuring good culture
- The [Denison culture index](#) defines four traits (see diagram), which can be measured and an improvement plan produced
- The [Organisational Culture Assessment Instrument](#) is another common framework that assesses culture against 16 measures
- The [Organisational Culture Inventory](#) includes behavioural norms – how people 'fit in' and meet expectations and the impact on performance
- The [Investment Association](#) has also provided a range of different indicators on measuring culture.



Bibliography

For further information please see the list of documents below:

Title	Author	Link
The Emotional Intelligence (EI) Institute	Peter Salovey and John D Mayer	The Emotional Intelligence Institute - What is emotional intelligence? - 4. Mayer and Salovey model of emotional intelligence (theeiinstitute.com)
What you need to know about Emotional Intelligence	Healthline	Emotional Intelligence: What It Is and How to Apply It to Your Life (healthline.com)
Understanding Organisational Culture	Chartered Management Institute (CMI)	https://www.managers.org.uk/~media/Files/PDF/Checklists/CHK-232-Understanding-organisational-culture.pdf
A duty to care? Evidence of the importance of organisational culture to effective governance and leadership	CIPD	a-duty-to-care 2016-evidence-of-the-importance-of-organisational-culture-to-effective-governance-and-leadership tcm18-14220.pdf (cipd.co.uk)
The Board's Role in Corporate Culture	Diligent Insights	The Board's Role in Corporate Culture Diligent Insights
Corporate Culture and the Role of the Boards	Financial Reporting Council	Corporate Culture and the Role of Boards (frc.org.uk) Referenced to Balogun and Johnson
Developing organisation culture: six case studies	CIPD	developing-organisation-culture 2011-six-case-studies tcm18-10885.pdf (cipd.co.uk)
Culture, a practical framework for sustainable change	The Investment Association – Latham and Watkins	Cultureframework-thirdedition.pdf (theia.org)
Five steps to making culture work for the board	P A consulting	Five steps to making culture work for the board PA Consulting
How to Define Your Business Purpose	CMI	https://www.managers.org.uk/knowledge-and-insights/article/how-to-define-your-business-purpose-2/
Why Culture is more important than ever	KPMG	https://home.kpmg/au/en/home/insights/2020/11/adv-why-culture-is-more-important-than-ever.html
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Five ways to enhance board oversight of culture	Ernst & Young	Five ways to enhance board oversight of culture EY UK
14 signs of a bad company culture and how to improve	Builtin – Kate Heinz	https://builtin.com/company-culture/bad-company-culture
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