Governing Values
a guide for boards of financial services companies
Introduction
by The Rt Hon The Lord Mayor

“The City’s reputation for integrity and solid values remains key to the continued success of the UK’s financial and business services sector and enhances its competitiveness in world markets.

We know from experience that if values and standards are to be embedded and ‘lived’ day to day in our businesses ‘the tone’ must be set from ‘the top’.

The Governing Values guide provides a ‘roadmap’ to help chairmen and boards to calibrate their specific approaches to the oversight of these issues in a thoughtful and coherent way”.

Alderwoman Roger Gifford

The Rt Hon The Lord Mayor of London,
Alderman Roger Gifford

This initiative is supported by the City of London Corporation
“Purpose and values require leadership from the top since they involve both strategy and example. They are critical to the success and sustainability of any major enterprise today – they must be driven by the board, led by the chairman and embedded in the thinking and processes of the business.”

Sir Win Bischoff

“It is not just the business you do but the way you do the business that makes such a difference and it is the way that chairmen conduct themselves that sets the example.”

Sir Roger Carr

“The chairman must take responsibility for setting the ‘tone from the top’ – otherwise it becomes the tone from halfway down which just doesn’t have the same impact.”

John Griffiths-Jones
Our financial institutions are deeply interwoven in the fabric of society. They play a role that no other sector plays in supporting the livelihood and success of individuals and businesses. In recent years too many instances of failure and inappropriate behaviour have come to light and both public perceptions and public expectations have changed fundamentally.

If we are to reinforce the international competitiveness of the City of London, and its long standing reputation for fair dealing, we must learn from these failures and act decisively to raise the bar. This is a matter for board leadership and governance not regulation – although any failure on our part will doubtless prompt a regulatory response.

A critical part of ‘raising the bar’ is for boards to set the ‘tone from the top’ in terms of values. Values are the visible, everyday manifestation of the culture of any business – they are how it is ‘lived’ and how it impacts on society. Boards have a responsibility to ensure the values they set for an organisation are being ‘lived’ throughout the businesses in a consistent and coherent way.

In this guide we examine the issues facing chairmen and boards in governing values, propose an agenda for the board discussion, explore best practice and what can be learnt from others, and set out a ‘roadmap’ to help companies tailor their own approach. We are not prescriptive and do not propose a voluntary code or standard. We recognise that every organisation is different in terms of heritage, reputation and challenges – such recommendations as we propose are intended as guidance to help boards shape their own thinking.

Governing values well is a prerequisite for a truly sustainable business – failure constitutes a significant risk and can threaten a company’s ‘licence to operate’ or its very survival. The need for the board of any financial services business to govern values is now central to its agenda – not an ‘optional extra’. Integrity, trust and values have moved irrevocably from the ‘nice to do box’ into the ‘must do box’.

‘Governing Values’ will help us all rise to that challenge.

Richard Sermon MBE, Chairman
The City Values Forum
A board summary

The financial services industry in the City leads the world in its competence and its innovation. This is the time for it to lead the field by using these same capabilities to restore the reputation of the industry. Values are now fundamental to a company’s long-term sustainable success. A strong values-led culture is a key asset. It helps distinguish a company from its competitors. It helps boards navigate their way through change and manage risk by acting as a touchstone against which all business decisions can be measured.

Values matter because of reputational risk... recent research has shown that for every corporate catastrophe the operational failure that caused it was the result of human behaviours. If employees do not make key decisions in line with a clear and consistent set of values then companies expose themselves to significant reputational risk.

Values matter because of regulatory threat... regulators have long memories and will continue to seek assurances that action has been taken until they are fully satisfied that appropriate action is being taken consistently. Being able to show that the company is on the front foot in tackling perceived cultural problems by adopting good practice is vital to developing trust with regulators and avoiding regulatory costs and sanctions in the future.

Values matter because of business performance... having a clear set of values helps attract and retain talented people, investors and loyal customers. Companies with clear values achieve the greatest engagement and performance from their people. Communicating and rewarding clear and consistent values and expected behaviours can also help create the consistent culture, across diverse operational units and different ethnic and religious cultures, critical for success in a global market.

Values matter because of society... financial institutions support and enable the livelihood and success of every individual and business and their collective success maintains society’s success. Financial institutions operate on trust. Their products are often intangible. With a piece of furniture it is clear a screw is missing. With a financial product customers may not realise that it is not fit for purpose until far into the future. Those selling financial services have a greater responsibility to ensure that their products are fit for purpose not only in meeting a customer’s needs but also delivering the wider social value society expects.

To help rebuild trust and ensure the continuing success of their businesses, chairmen of boards must ensure that the businesses they lead are clear about the company’s values, how these connect with the company’s purpose and strategy, how they create value for their key stakeholders, and what behaviour is expected of everyone.

“In particular an effective board... demonstrates ethical leadership, displaying – and promoting throughout the company – behaviours consistent with the culture and values it has defined for the organisation”

The Financial Reporting Council, Guidance on Board Effectiveness
This report is therefore focused on the key role of boards, and in particular chairmen, in governing values.

Our research has found that there is an abundance of advice for executive teams on the management of behaviour and values but little beyond guidance from the Financial Reporting Council, Financial Conduct Authority and Prudential Regulation Authority which can help boards provide robust rigorous leadership and effective oversight of how well their values are being ‘lived’ throughout the business. This guide addresses this gap.

How boards measure values and behaviours is still being developed. This guide pushes at the boundaries of this vitally important, but relatively new, area for the board agenda. We have therefore looked at how leading businesses, inside and outside the City, are governing values to identify good practice.

Our findings indicate that boards who govern values well take a systemic and holistic approach and focus on the following six key building blocks, each of which is important, working together to govern values in a holistic way:

- inspiring through purpose and values
- aligning corporate strategy and organisational capability with values
- incentivising values-based leadership and behaviours
- measuring values through behaviours
- using values to guide decisions
- promoting values-based leadership.

We recommend that boards take time every year to review how well they are governing values. To assist such a discussion we have provided two tools. An ‘agenda’ for the board’s discussion taking each of the six key building blocks above and suggesting the core questions a board might wish to discuss. The second tool is a ‘roadmap’ showing the actions boards may take in answer to the questions in the agenda. It shows three levels so boards can review where they are now and determine where they want to be. Each board will prioritise differently.
Governing values: an agenda for boards

Some questions that boards can ask of themselves to help govern values.

- **Inspiring through purpose and values**
  - How well does what we do as a business fit our purpose and values?
  - When will we next review the purpose and values of the business?
  - How do we monitor the changing expectations of our key stakeholders? How do any changes get reflected in how our purpose and values are expressed in our behaviours?
  - How satisfied are we that the value we are promising to each of our key stakeholders meets their reasonable expectations?

- **Aligning corporate strategy and organisational capability with values**
  - How do our values support the long-term sustainability of our organisation?
  - To what extent are our strategy and commercial goals consistent with our values?
  - What capabilities and consistent behaviours does our organisation need to deliver our strategy? What development is required to help our people behave more consistently with our values?

- **Incentivising values-based leadership and behaviours**
  - What behaviours does our remuneration system encourage?
  - How do we incentivise behaviour aligned with our values?
  - What sanctions do we use when behaviour is not aligned?
• **Measuring values through behaviours**
  - How confident are we that behaviours across our business are consistent with our values?
  - What key performance indicators (KPIs) are needed to measure values and behaviours? How will we ensure that they are effective? When might we review them?
  - How integrated are these measures with other standards and controls?
  - How much time does the board spend reviewing these measures? Is the time spent sufficient? Is a separate sub-committee needed?

• **Using values to guide decisions**
  - How do we communicate what behaviours we want to see from everyone?
  - How do we ensure that our purpose and values shape what we do and won’t do? What are our ‘lines in the sand’?
  - What decisions are critical to our reputation? How confident are we that the people who take those decisions do so in a way that is consistent with our values?
  - How do we help our people to use our values when making decisions affecting key stakeholders? How do we test the resilience of their decision-making? What development is needed to help them?

• **Promoting values-based leadership**
  - How confident are we that the board and senior executive team have the character, experience and competencies to promote and embody our corporate values?
  - Who leads on values in the boardroom and across the business? What roles do the chairman and CEO play in promoting and embedding values?
  - What values and behaviours are most commonly exhibited in our board meetings? How safe is it for anyone to raise any issues relating to values and behaviours, including those who report to the CEO and below?
A roadmap for governing values

This roadmap is an aid to chairmen and directors to help them make an assessment of how mature the board’s approach is to governing values.

The three stages and their indicators are drawn from our research and should be used as a stimulus for discussion. It is likely that boards will assess themselves as being at different levels for different issues. Level 2 is not intended to be a description of the end of the journey more an indication that the board is governing values and culture well and as a result will be identifying new ways to carry out their role.

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| **1. Inspiring through purpose and values** | The board has a clear and shared understanding of the corporate purpose and values.  
Values are aspirational and are revisited by the board on a regular basis.  
All key stakeholders beyond investors have been identified by the board.  
The board has discussed and articulated the reciprocal value the business creates for its stakeholders and the expected behaviours. | Values have been communicated to all employees at the frontline in a way that resonates better with them leading to the values being more closely reflected in behaviours.  
The board receives an annual update of trends in the expectations of key stakeholders.  
The board clearly prioritises the value that the organisation creates for key stakeholders on the basis of mutuality and sustainability.  
The behaviour of all employees is aligned with and reflects the corporate values. | The board publishes what key stakeholders can expect from the business.  
Members of the board meet regularly with representatives of each key stakeholder group both formally and informally.  
Commercial value and/or value at risk from stakeholder pressure is a common discussion at the board.  
The value created for each stakeholder is measured and reported to the board and published externally. |
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<td>Alignment of strategy, values and behaviours is a regular board conversation. All human resources processes take into account values and expected behaviours. Product/service alignment with purpose and values is part of the approval process for research and development and marketing. The board has identified suitable accreditations for the organisation and employees to embed values.</td>
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<td><strong>3. Incentivising values-based leadership and behaviours</strong></td>
<td>Reward is tied to demonstrated behaviour. The remuneration committee receives reports on individual behaviours with all submissions for pay, bonus and promotion. Senior leaders are rewarded/sanctioned for performance against 3 or 4 ‘bottom lines’ – e.g. finance, customers, employees, society including environment.</td>
<td>Senior leaders are barred from promotion if they do not behave consistently with the values. There is automatic bonus reduction for senior leaders, or their teams, that do not demonstrate expected behaviours and values. Senior leaders who do not behave in line with values are exited.</td>
<td>Senior leaders are valued and recognised for consistent ethical and responsible behaviour.</td>
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<td>4. Measuring values through behaviours</td>
<td>The board has ways of measuring values, behaviours and culture (e.g. results of key stakeholder surveys such as employee engagement and customer satisfaction), regulator reports and internal reviews and audit reports. Internal audit covers values and behaviours contained in the above processes. The board receives regular “misdemeanour” reports.</td>
<td>The board agrees key values-based metrics for customers, employees and other key stakeholders and monitors regularly. The board has agreed ways in which it will test whether the values resonate with the people at the frontline of the organisation. The board receives an annual report on values and behaviours distilled from key performance indicators (KPIs), surveys, internal audit, human resources and other sources to assure themselves that the values are being demonstrated throughout the organisation.</td>
<td>The board publishes performance against values, and behaviours with objectives and metrics in the annual report. The board has an independent team that reviews values and expected behaviours at each of its operations on a regular basis.</td>
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<td>5. Using values to guide decisions</td>
<td>Principles-based decision-making is the norm at the board.</td>
<td>The board has a clear decision-making framework that seeks to ensure decisions and behaviours are consistent with values. The values component of reputational risk is an element of all strategic decisions and is reported to the board. Data on the alignment of values and behaviours is collected and used in strategic decision-making. Everyone in the business is trained to understand and apply the corporate values in their daily decision-making. The consistency with which values are expressed across the organisation is measured and monitored.</td>
<td>Values are always considered in every decision made throughout the organisation. Strategic discussions take into account the impact on the value created for each stakeholder and the business model.</td>
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<td><strong>6. Promoting values-based leadership</strong></td>
<td>Leadership behaviours which role model the values are clearly described.</td>
<td>Chairman and CEO live and breathe values, through all communications.</td>
<td>Board members regularly visit operational sites/branches, hold town halls and meet with individuals to promote values and behaviours.</td>
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<td>Board members and the executive are trained in ‘values-based leadership’ behaviour.</td>
<td>Board members are selected for character and ability to promote values across the business and are role models for the values and culture.</td>
<td>Society’s provision of a ‘licence to operate’ is regularly reviewed and challenged by the board.</td>
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<td>Board members are selected, in part for their high moral integrity.</td>
<td>The chairman includes values-led behaviour, when looking at the performance of board members.</td>
<td>Boardroom culture is open and self-critical. It is a safe space for concerns to be raised and discussed.</td>
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<td>Chairman and CEO demonstrate values-driven behaviour.</td>
<td>A NED or a board sub-committee is designated as being responsible for values and culture and is asked to make regular reports to the board on alignment, values and compliance.</td>
<td>The board has a team coach who focusses on values and culture, recognising the need for continuous development.</td>
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<td>Values-driven behaviour is expressed through corporate responsibility and sustainability programmes which are the responsibility of a direct report to the board and are given visible support by the chairman and the CEO.</td>
<td>The performance of the chairman is judged against the extent to which they live and promote the values.</td>
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Values are fundamental to a company’s long-term sustainable success.

A strong values-led culture is a key asset.

Boards, and particularly chairmen, have a vital role to play in governing values. This creates value inside and outside the organisation.

Why governing values matters

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Building block 1

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Aligning corporate strategy and organisational capability with values:
Building block 2

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Governing values in practice: the building blocks
Why governing values matters

In the wake of the financial crisis much has been said about the critical importance of culture and values and the need for leadership, integrity and setting the right ‘tone from the top’.

In this debate, there is often confusion between the use of the words culture, values and behaviours. For the purpose of this guide we define culture as being the way we DO things around here. It is the result of a web of interrelated artefacts, rituals, values and assumptions which if left unmanaged can absorb precious energy and put the handbrake on the organisation achieving its purpose. But if led and managed well culture is the rocket fuel for delivering value to stakeholders.

Values are part of a company’s culture and manifest themselves through the behaviours of all those in the organisation. If lived by everyone and used to inform every decision made, values are a key asset in delivering the company’s purpose and strategy, and help create value for the company and for its key stakeholders.

Boards are the ultimate custodians of a company’s values. The board’s role, led by the chairman, is to live the values, assure themselves that the values are embedded and lived throughout the organisation and are reflected in all the relationships through which value is created.

Living the values is vital because everyone in the company watches what the leaders do. Whether speaking in public at select committees or in private discussions in far flung corners of the business, employees pay very close attention to what board members say and do.

Governing values is a journey. Our research shows that while many companies, in both the financial services sector and others, recognise the importance of values to their business success, most still have progress to make in terms of governing values well.

Some boards seem almost complacent and take for granted that the published values are being lived. In some cases these are the lucky ones where values and behaviours have been lived consistently since the company was founded. In today’s world even these companies need to be clear about how they know that their values are reflected in the company’s behaviour.

Governing values is also a dynamic process. Boards need to be alive to the changing expectations of key stakeholders and to the pressures of these expectations on the behaviours and decisions of those on the frontline.

“A director of a company must act in the way he considers, in good faith, would be most likely to promote the success of the company for the benefit of its members as a whole”

Section 172 of the Companies Act 2006
“To generate their full potential value, companies today must have a culture, governance and ways of behaving that are values-based. This cultural alignment is becoming a prerequisite for each company’s licence to operate and ultimately its survival as an organisation.”
Dick Olver, Chairman, BAE Systems

“In many ways trust is the most important piece of glue we can have. So many financial institutions have lost that, possibly never to be regained. The most important way to maintain a reputation is to maintain trust.”
Mark Nicholls, Chairman, Rathbone Brothers and West Bromwich Building Society

“Our philosophy is about having a very clear differentiated business model. It’s about creating a culture that’s aligned to and underpins that model and then a very clear plan of execution. One sees so many organisations where the culture is dissonant of the model.”
Anthony Thompson, Former Chairman, Metro Bank

“There are many things we do that on a short term basis would be easier not to do. But we know they would cause a lot of problems down the road and not be in line with our ambition to be a truly responsible ethical company.”
Lise Kingo, Executive Vice President and Chief of Staffs, Novo Nordisk

“There have been large companies, fewer now, who have not given thought to how they govern values and just think it’s about a process of osmosis... that everybody knows how to behave, that we trust our employees and we don’t need to give them guidance. This misses the point. Having such guidance for staff can actually be part of your measures for protecting or mitigating your reputation risk.”
Philippa Foster-Back, Director, Institute of Business Ethics
Inspiring through purpose and values:
Building block 1

The best companies are clear about their purpose, their values, their key relationships and the reciprocal value created through those relationships.

Purpose and values equip the organisation to be consistent while also being adaptable. They shape its view of success, and underpin its approach to engaging in all its relationships.

Every company has a unique purpose – its reason for being. From this a set of values will flow that are necessary to achieve this purpose. Most large companies in financial services have set their values and publish them. Fewer make it clear what their purpose is.

Not only do boards need to be clear about purpose and values they need clarity about who they value – their key relationships such as customers, employees, suppliers, investors, regulators and the communities and wider society in which the company operates.

Relationships are reciprocal. Each of these relationships has value to the company and the value that the company promises for each relationship needs to be made clear in return. Boards have been excellent at being sensitive and responsive to the changing expectations of investors. They now need to apply the same sensitivity to the expectations of other key stakeholders.

It is this reciprocal value created through each key relationship that differentiates a company from its competitors. When boards do not provide sufficient clarity about who and how this value is created, employees on the front line will find it difficult to know what behaviours are expected and to act consistently in these relationships.

The purpose and values of a business only need to be revisited every now and again. However, the reciprocal value from each key relationship may need more frequent review as stakeholders’ expectations change. For example, in financial services, understanding the social value created is increasingly seen to be important e.g. Lloyds Bank mission “Helping Britain Prosper” where prosper is defined by using the triple bottom line or the Barclays Citizenship element of their balanced scorecard. Mergers and acquisitions can substantially change the business model. Changing stakeholder expectations constantly shift the line that separates what wider society considers morally acceptable or not. An example being the public reaction to what is seen as tax avoidance.
Questions boards can ask of themselves

- How well does what we are seen to do as a business fit our purpose and values?
- When might we next review the purpose and values of the business?
- How do we monitor the changing expectations of our key stakeholders? How do any changes get reflected in how our purpose and values are expressed in our behaviours?
- How satisfied are we that the value proposition for each of our key stakeholders meets their reasonable expectations?

Stages of the journey...

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“…the real impact, and acid test, of a company’s culture is its impact on and alignment with the external stakeholders with whom it interacts and forms relationships. To work well and create the most value, these relationships need to be based on mutual values, trust and openness.” Dick Olver, Chairman, BAE Systems

“Boards have to decide for themselves what is right. We do have debates increasingly often about the relationship of our business to the communities in which we operate in and aspects such as our responsibilities to the exchequer. That is a very positive development.” Ian Durant Chairman, Greggs and Capital and Counties Properties

“If you are going to get the sort of engagement that can bring about culture and behavioural change in tens of thousands of people then the proposition needs to be not only something that resonates with people at an emotional level but also that resonates with the organisation at a commercial level.” Philip Bramwell, General Counsel, BAE Systems
Case study: Deutsche Post DHL

Happy workers make happy customers make happy investors: that is the simple message which the board drives throughout the organisation. It can be easily understood by the managers as well as the staff in our team of more than 470,000 employees and is consistently communicated through all internal channels – from posters on blackboards to blogs in the intranet.

A Guiding Principle (Respect & Results) as well as a Customer Promise (Simplifying Services & Sustainable Solutions) have been defined to make this message even more tangible and give concrete guidance for the employees. The three bottom lines have been added with a fourth one: under the brand of Living Responsibility the Group engages in environmental protection, disaster management and education in order to make a positive contribution to our natural and societal environment.

The progress in delivering against those bottom lines – beyond the financial result and the stock market performance – is constantly measured via tools such as the yearly Employee Opinion Survey, a range of comprehensive Customer Surveys and a sophisticated Carbon Accounting that captures our CO₂ footprint against an ambitious reduction target (30% by 2020 compared to 2007). Improvement targets related to the multiple bottom lines are derived for all managers including the board.
Aligning corporate strategy and organisational capability with values:
Building block 2

In setting direction, boards see strategy as a galvanising force for everyone to achieve the company’s purpose and commercial goals, and unlock the reciprocal value that lies in its relationships with key stakeholders. The strategy also sends a strong message about what senior leaders value and prioritise.

The strategy will only succeed if it is supported by the company’s values and behaviours.

The board’s role in governing values is to ‘kick the tyres’ of the corporate strategy and satisfy itself that the organisation has the capability to deliver it.

This includes financial capability, what additional investment may be required (for example in technology, new products and services, new distribution or supply networks) and whether its people have the skills and capability to deliver their objectives in a way that is consistent with the stated values. This includes having leaders with the capability to lead on values.

In recent years financial services strategy has centred on value creation for investors and business models concentrated on the configuration of its financial assets. This was understandable during a period of financial crisis.

Sustainable strategies of the best companies include value creation for all key stakeholders and the business model includes not only the means by which value is created for each key stakeholder, but also the investment costs to develop the organisational capability to deliver the value.

For example, in financial services, where there is a move to more customer centric strategies, the business model includes the means by which that strategy will be delivered e.g. the costs of recruiting, training and developing the people working in the organisation to adopt consistent customer centric behaviour.
Questions boards can ask of themselves

- How do our values support the long-term sustainability of our organisation?
- To what extent are our strategy and commercial goals consistent with our values?
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“Increasingly I think businesses will have to look at values and how they relate to the way they do business. Our values come from within Plan A. This extends into everything we do including the way we look after customers and their communities, work with suppliers and the way we behave. Our incentive scheme includes Plan A targets for all executive directors to align behaviours with the key business objectives.”

Robert Swannell, Chairman, Marks & Spencer

“I don’t believe that you can teach people to want to help others. Our recruitment process is about finding people who want to give good service, and then teaching them the skills to deliver this. It is about the culture first and foremost, and then about the technical skills.”

Anthony Thompson, Former Chairman, Metro Bank

“If the right capability – individual skills, organisational competence and embedded values-driven behaviour – isn’t there, the board’s strategy won’t be achieved. So it is incumbent on the board to understand any capability gaps, and ensure that there is investment in place to fill them.”

Richard Finn, Richard Finn Ltd.
The Old Mutual [wealth management] board agreed a revised definition of their corporate purpose. They defined it as to “provide the best investment and retirement solutions in the market, in the most flexible manner, with unparalleled service to our customers at great value”.

Given a mandate to pursue this vision, the executive team started by going back to basics. They asked why does the company exist? What is the social value the company adds? Having set their purpose they asked how are we going to implement it? What does it mean for our strategy? What are we going to do about it? The common purpose they arrived at for the company was “To enable positive futures”.

Within 12 months 90% of their UK and European insurance books were closed to new business and replaced by new products that were aligned to the board’s vision. Having communicated the new strategy to the market Old Mutual collected and reviewed their broker reports. All bar one (out of around 30) were supportive and bumped the share price.

The change was also reinforced by creating an aligned culture and in which everyone across the business takes responsibility for their decisions. A part of this is ruthless honesty and blameless communication within the organisation. The culture is one where if you have made a mistake and have bad news you should speak up – and it is only if they try to bury bad news that an employee could be reprimanded. This starts with the CEO who makes clear that nobody gets blamed for giving him bad news. The approach also means that executives do not ‘guild the lily’, which helps to ensure that information coming to the board is truthful, and so provides a basis on which to take sound decisions.

High level backing by the PLC board has been identified as crucial to making this change successful.
Incentivising values-based leadership and behaviours:
Building block 3

Remuneration is one of the most powerful tools through which values and expected behaviours can be both incentivised and sanctioned.

Remuneration is again in the public spotlight. Questions are being asked about the degree to which remuneration systems have led to lapses in behaviour and standards in the financial services industry.

At the same time, the industry is facing an onslaught of new regulations from Europe aimed at reducing what is seen as excessive pay within the industry.

The board’s role is to be clear about the objectives and behaviours they expect from their executive management team and, through the remuneration committee, set:

- the system
- the performance measures it includes and excludes
- the rigour and effectiveness with which it reviews performance, and
- agree the sanctions and rewards based on individual performance.

There are many ways to tie values into incentive structures. For example remuneration can be tied to non-financial metrics such as customer service rather than sales. ‘Gating systems’ can be introduced, where managers are not considered for a bonus or promotion without meeting certain values targets.

Whilst the board should not involve itself in the details of management it should regularly interrogate the executive team to test whether the tone they have set through the remuneration system of the senior management is reflected through the company’s systems and processes and particularly those relating to recruitment, training, performance and reward.
Questions boards can ask of themselves

- What behaviours does our remuneration system encourage?
- How do we incentivise behaviour aligned with our values?
- What sanctions do we use when behaviour is not aligned?

Stages of the journey…

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<td>Reward is tied to demonstrated behaviour. The remuneration committee receives reports on individual behaviours with all submissions for pay, bonus and promotion. Senior leaders are rewarded/sanctioned for performance against 3 or 4 ‘bottom lines’ – e.g. finance, customers, employees, society including environment.</td>
<td>Senior leaders are barred from promotion if they do not behave consistently with the values. There is automatic bonus reduction for senior leaders, or their teams, that do not demonstrate expected behaviours and values. Senior leaders who do not behave in line with values are exited.</td>
<td>Senior leaders are valued and recognised for consistent ethical and responsible behaviour.</td>
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“Risks and rewards in banking have been out of kilter. Given the misalignment of incentives, it should be no surprise that deep lapses in banking standards have been commonplace… Rewards for success should be better focussed on generating long-term benefits for banks and their customers. Where the standards of individuals, especially those in senior roles, have fallen short, clear lines of accountability and enforceable sanctions are needed. They have both been lacking.”
Andrew Tyrie MP, Former Chairman, Parliamentary Commission on Banking Standards

“As remuneration structures become more complicated there is a need to put in place more monitoring and controls to make sure that you get the behaviours you actually want.” Geoffrey Howe, Chairman, Nationwide Building Society and Jardine Lloyd Thompson Group

“When I consider what behaviours our incentive schemes are driving I have to ask myself does this consider not just what they have achieved, but how have they achieved it? And was the ‘how’ consistent with the values of the organisation?” Sir Peter Gershon, Chairman, National Grid and Tate & Lyle

“In the US it is not uncommon to have long established written business conduct guidelines – in IBM for example there were three key principles under the headings of ‘pursuit of excellence’, ‘service to the customer’ and ‘respect for the individual’ around which the values were built and importantly individual performance measured.” Sir Anthony Cleaver, Chairman, Novia Financial
Case Study: Metro Bank

At Metro Bank colleagues are rewarded based on the level of service they provide to customers. This builds on a core philosophy that says if you want to be a customer centric business then you need to ensure that customers and their needs are central to everything you do.

In addition to regular mystery shops to gauge levels of customer service, Metro Bank use the independently developed ‘Net Promoter Score’ as an empirical way of measuring customer satisfaction at any point. It is a mechanistic process used for scoring customer service and satisfaction. It can be used to measure any aspect of service, or combination of aspects, from across the customer journey.

While this is primarily used to review the customer experience for those who interface directly with customers in our stores and through our contact centre, similar measures to recognise and reward amazing service are applied right through the business to all colleagues.
Measuring values through behaviours:
Building block 4

At any moment someone, somewhere, in every organisation will be doing something that is not consistent with the values. But boards of large companies cannot monitor whether everyone is living the values. What they can do is insist that management develop and set metrics that include measures of behaviour for the board to then agree.

Measuring behaviours is difficult and approaches are in their infancy. What is being sought is objective evidence of how values-aligned behaviours have been applied in arriving at a business outcome. There are three main ways board members can assess and measure behaviours:

- **observation** – while not a true measure, observation can be useful. For example, observing how people behave in the boardroom, board members spending a day listening to calls at a call-centre or talking to the front line of the business. Informal evidence can also be collected from those conducting internal reviews and audits, risk and legal teams and feedback obtained from external auditors.

- **structured subjective measures** – these are the most commonly used and are helpful in terms of identifying trends. For example reports on misdemeanours, performance management, whistle blowing, internal audit and risk reviews. In addition to trend identification, employee engagement and customer satisfaction data can give some indication of potential issues or problems.

- **objective measures** – this is the ‘holy grail’. These measures focus on the outcomes of behaviours being applied in practice by using evidence about key decision-making moments to determine whether such decisions have been taken in line with the values of the organisation. Exploiting ‘big data’ within the organisation to analyse culture and values is a developing science.

We have also heard differing views as to the value of a designated NED or a board sub-committee, similar to an audit committee, but focussed on culture and values.

Over time, independent internal and/or external assurance may be possible in much the same way as companies have moved from reporting only on financial performance to now including performance in some non-financial areas.
Questions boards can ask of themselves

- How confident are we that behaviours across our business are consistent with our values?
- What key performance indicators (KPIs) are needed to measure values and behaviours? How will we ensure that they are effective? When might we review them?
- How integrated are these measures with other standards and controls?
- How much time does the board spend reviewing these measures? Is the time spent sufficient? Is a separate sub-committee needed?

Stages of the journey...

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| The board has ways of measuring values, behaviours and culture (e.g. results of key stakeholder surveys e.g. employee engagement, customer satisfaction), regulator reports and internal reviews and audit reports. | The board agrees key values-based metrics for customers, employees and other key stakeholders and monitors regularly.  
The board has agreed ways in which it will test whether the values resonate with the people at the frontline of the organisation.  
The board receives an annual report on values and behaviours distilled from key performance indicators (KPIs), surveys, internal audit, human resources and other sources to assure themselves that the values are being demonstrated throughout the organisation. | The board publishes performance against values, and behaviours with objectives and metrics in the annual report.  
The board has an independent team that reviews values and expected behaviours at each of its operations on a regular basis. |
“We measure progress through improvement in three bottom lines… Employee of Choice, Provider of Choice and Investment of Choice and all my direct reports know that I and the board will ask them for progress reports on all three bottom lines” Dr Frank Appel, CEO, Deutsche Post DHL

“It is the responsibility of executive management to ensure that the values are applied throughout the business but the board must ensure it is being done. When it is well done the values become ‘second nature’ to the staff and you can see them wherever you ‘cut into’ the organisation.”
Ludovic de Montille, UK Group Chairman, BNP Paribas

“NEDs shouldn’t be concerned about testing whether the values work perfectly, the real test is, have people been able to understand the values to the extent that it allows them to articulate how the values relate to how they do their job.” Mark Nicholls, Chairman, Rathbone Brothers and West Bromwich Building Society
Values without measurement are just wallpaper.

During our research for this guide we noticed a significant trend, in the best companies, towards describing expected values-driven behaviours. In some companies the expected behaviours for all employees were described, in others the behaviour of leaders at different levels were illustrated against each value. This makes observation and structured subjective measurement very much easier. Once leaders and managers are skilled at assessment, reporting on values-driven behaviours to the Board is a relatively easy matter.

A second increasingly common practice is reporting to the board on employee engagement levels; high quality engagement measures are known to correlate with individual and organisation performance. Boards are increasingly debating trends in engagement at different levels, tenure lengths and parts of the business, to understand the quality of leadership and potential risks to business performance.

A third increasingly common practice was ‘misdemeanour’ reporting, where the board receives an analysis, often via its audit or compliance sub-committees, of reported misdemeanours to enable the board to understand the volume and locus of behaviour that is not aligned with the values.
Decisions, large or small, can quickly make or break a company’s reputation. For example, the many small decisions that in aggregate distorted the Libor rates.

Boards need to be clear which decisions are most critical to business reputation and success than others. For example, protecting the health and safety of employees, customers and society is critical to an oil and gas company. For a bank, protecting customers’ deposits is a priority. The tricky decisions are those that involve balancing the competing interests of key stakeholders e.g. return to investors’ profits vs. customer service vs. employee work life balance vs. value to society. Boards that are clear about the two or three most important priorities to the business and review these regularly will find it easier to govern values well.

Once these key priorities have been identified, the best companies put in place a framework, supported by training, to help ensure that decisions taken anywhere in the business reflect the stated values. This could be in the form of principles, a code of conduct or a ‘mantra’ that everyone in the business knows and which guides their decisions and behaviour – such as the ‘triple bottom line’ or ‘do the right thing’.

Good decision-making also means being clear about responsibilities and delegated authority, particularly in matrix organisations. For example, in his report, Andrew Tyrie identified the need for banks to ensure that the most important responsibilities are assigned to specific, senior individuals so they can be held fully accountable for their decisions and the standards of their banks in these areas.

One way to judge if the decision-making framework is effective is whether the chairman and board members talk about their decision-making framework in the same language as their employees.

A parallel can be drawn with risk appetite. The litmus test for whether a board has articulated the risk appetite well is whether the chairman can go to the most junior employee and find that they are able to explain what the major risks around their job are. A similar test might be applied to values. Can employees describe the major dilemmas they face or are likely to face around their job? Can they give examples of scenarios they have observed where the values are working and where they are not working?
Questions boards can ask of themselves

- How do we communicate what behaviours we want to see from everyone?
- How do we ensure that our purpose and values shape what we do and won’t do? What are our ‘lines in the sand’?
- What decisions are critical to our reputation? How confident are we that the people who take those decisions do so in a way that is consistent with our values?
- How do we help our people to use our values when making decisions affecting key stakeholders? How do we test the resilience of their decision-making? What development is needed to help them?

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<td>Principles-based decision-making is the norm at the board.</td>
<td>The board has a clear decision-making framework that seeks to ensure decisions and behaviours are consistent with values. The values component of reputational risk is an element of all strategic decisions and is reported to the board. Data on the alignment of values and behaviours is collected and used in strategic decision-making. Everyone in the business is trained to understand and apply the corporate values in their daily decision-making. The consistency with which values are expressed across the organisation is measured and monitored.</td>
<td>Values are always considered in every decision made throughout the organisation. Strategic discussions take into account the impact on the value created for each stakeholder and the business model.</td>
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“It always comes down to judgements and people. People need to rely on their own judgements and not rely on more processes to take them out of the firing line.” David Tyler, Chairman, J. Sainsbury

“Cultural change does not happen overnight but it is the result of patience and endurance. It needs the buy-in from the individual employee and that is why we have not imposed it from the top. Rather we have created a convincing framework with the guiding principle of “Respect & Results” at the heart and have left it up to our business units and corporate functions how to manoeuvre within this framework” Dr Frank Appel, CEO, Deutsche Post DHL

“A strong culture is a culture that encourages and ensures consistent behaviour and decision-making across the organisation – i.e. the shared assumptions are consistently understood by everyone. In a weak culture, behaviour and decision-making is inconsistent – i.e. people apply different assumptions to similar decision making challenges. Of course, both strong cultures and weak cultures can be good or bad!” Richard Sykes, Partner, PwC
Case study: Novo Nordisk

Novo Nordisk is a global healthcare company with 90 years of experience and innovation in diabetes care and a values-based management approach called the ‘Novo Nordisk Way’. It is typically reviewed every 10 years and updated to ensure that expresses clearly and succinctly the company’s purpose, values, ambitions and behaviours that stakeholders can expect employees to embody, whether towards the patients they serve, medical practitioners, politicians or members of the communities in which the company operates.

Novo Nordisk recognises that by promoting responsible and ethical business practices throughout its global value chain and by continuously reducing any negative environmental impacts generated by its activities, the company stimulates economic prosperity that is socially just and environmentally sustainable. The Novo Nordisk Way and the Triple Bottom Line principle provide a framework for decision-making that delivers long-term growth for the business by building trust, protecting and enhancing its licence to operate and attracting and retaining the best people.

The Articles of Association for Novo Nordisk state that the company “strives to conduct its activities in a financially, environmentally and socially responsible way.” Novo Nordisk has built this Triple Bottom Line principle into its corporate governance structures, management tools and methods of assessing and rewarding individual performance. Overall responsibility for the company and its activities lies with the board of directors, but every Novo Nordisk employee is responsible for making their contribution to enhancing the company’s financial, social and environmental performance.

Since 2004 the Novo Nordisk Annual Report has accounted for financial, social and environmental performance in one inclusive report. This approach underpins an integrated approach to managing the company, which in turn is reflected in a unified culture throughout the global organisation.

Since the launch of the DOW Jones Sustainability Indexes (DJSI), Novo Nordisk has consistently been rated first or second in the healthcare sector.
To achieve consistent values-based behaviour throughout the organisation, the board needs to set ‘tone from the top’ and act as role models for values individually and collectively. This is what we mean by ‘values-based leadership’.

Part of this is about demonstrating clarity about the relative priority of financial performance, reputation and values.

The interests of key stakeholders are frequently in conflict with each other or with the purpose and values of the business. In these situations, boards send a strong signal to the rest of the organisation when they make the decision that is consistent with the company’s values, especially where the commercial benefits may not be immediately apparent.

Without this leadership the actions discussed in the previous sections will remain empty rhetoric. The result will be that decisions and behaviours will default to prioritise short-term returns above long-term sustainability or reputation.

Dealing with such dilemmas takes strength of character. Board members need to be seen to stand up for their beliefs and step forward in the face of serious challenge. HSBC describes the behaviours that they want to see in their senior leaders as ‘courageous integrity’.  

The chairman can enable the board to show this kind of leadership by creating a safe space for constructive challenge and for different ideas to be aired within the boardroom. For example, by ensuring that any of the CEO’s direct reports can raise an issue with the board where they have a contrary view to the CEO. A skilful chairman will be able to draw these issues out and encourage discussion.

Living the values is important and challenging. Having discussions at all levels of seniority, age and ethnicity etc. enables boards to be visible role models as well as providing valuable insights into the challenges faced by their employees.
Questions boards can ask of themselves

- How confident are we that the board and senior executive team have the character, experience and competencies to promote and embody our corporate values?
- Who leads on values in the boardroom and across the business? What roles do the chairman and CEO play in promoting and embedding values?
- What values and behaviours are most commonly exhibited in our board meetings? How safe is it for anyone to raise any issues relating to values and behaviours, including those who report to the CEO and below?

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<td>Leadership behaviours which role model the values are clearly described.</td>
<td>Chairman and CEO live and breathe values, through all communications.</td>
<td>Board members regularly visit operational sites/branches, hold town halls and meet with individuals to promote values and behaviours.</td>
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<tr>
<td>Board members and the executive are trained in ‘values-based leadership’ behaviour.</td>
<td>Board members are selected for character and ability to promote values across the business and are role models for the values and culture.</td>
<td>Society’s provision of a ‘licence to operate’ is regularly reviewed and challenged by the board.</td>
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<td>Board members are selected, in part for their high moral integrity.</td>
<td>The chairman includes values-led behaviour, when looking at the performance of board members.</td>
<td>Boardroom culture is open and self-critical. It is a safe space for concerns to be raised and discussed.</td>
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<tr>
<td>Chairman and CEO demonstrate values-driven behaviour.</td>
<td>A NED or a board sub-committee is designated as being responsible for values and culture and is asked to make regular reports to the board on alignment, values and compliance.</td>
<td>The board has a team coach who focusses on values and culture, recognising the need for continuous development.</td>
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<td>Values-driven behaviour is expressed through corporate responsibility and sustainability programmes which are the responsibility of a direct report to the board and are given visible support by the chairman and the CEO.</td>
<td>The performance of the chairman is judged against the extent to which they live and promote the values.</td>
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“We have all worked in companies where you have the company’s vision and values or strategy written in some pithy statement on a mouse mat. I have had several mouse mats during my career but I have looked up to the higher echelons of the companies that gave them to me and it never really seemed that the behaviours matched the values. Now I am the one producing the mouse mats for my company and it is up to me to make it real.” Paul Feeney, Chief Executive, Old Mutual Wealth Management

“Do the very top people in the organisation - the chairman and the chief executive make clear how important they think the values are? If they really believe it, you can get the board to buy into it and you can get the senior management to buy into it. But if you don’t really believe it yourselves, you’re not going to make that much difference.”
Sir Peter Gershon, Chairman, National Grid and Tate & Lyle

“In Greggs we have a set of values and apply them to every decision that’s made in the business, this culture has taken a long time to develop, and as the business faces new challenges, we are constantly testing the applicability of our values against management decisions.”
Ian Durant Chairman, Greggs and Capital & Counties Properties

“There is merit in the written approach, asking everyone in the organisation to ‘sign off’ on a statement of values so that that we all know what we are talking about and that it clearly and specifically comes from the top.”
Judith Hackitt, Chair, Health and Safety Executive
Case Study: BAE Systems

BAE have tried to develop a culture within which the company’s core ethical values are taken into account in every decision their people take. The desire to create this environment is driven by the belief that the only way to meet the ever changing demands placed on a company to maintain its licence to operate is through having a shared set of values that are applied consistently worldwide, and which are continually reinforced and improved over time throughout the organisation.

They see this boiling down to two things. First, a recognition that an ethical business culture is vital: there is no alternative. And second, that building that culture is not a single step than can be taken and then forgotten about but an on-going voyage where the destination is always just over the horizon.

As BAE’s chairman Dick Olver has stated board leadership, in being able to demonstrate that they are ‘walking the talk’, is vital to making this culture change stick, pointing out that “behaviour is critical. Having a board that says one thing and is then seen to be doing another will quickly derail any culture change.”

In 2007, before the Woolf Review, BAE rewrote the contracts for all third-party advisers worldwide and submitted each of them to a new and more rigorous approval process, including scrutiny by a panel of external experts. The process was demanding and the Woolf Report described it as being leading edge in managing ethical and reputational risks.

When the process was introduced many observed that it would be detrimental to BAE as it would mean actively turning down contracts that might cause BAE to breach their ethical code. In practice it has proven beneficial as customers across the globe have shown that they want to deal with providers who behave ethically. And in 2012 BAE’s order book doubled in size compared with the previous year.
Other useful resources

There are a number of other tools, techniques and frameworks which focus on many of the aspects discussed in this guide, such as purpose, values and relationships. Amongst those that may be helpful to boards are:

**The City Foundation Course ‘Leading with Integrity’** – a degree-level course for new managers. ([www.cityvaluesforum.org.uk](http://www.cityvaluesforum.org.uk))

**The City Obligation** – a personal pledge to uphold the City’s enduring values. ([www.cityvaluesforum.org.uk](http://www.cityvaluesforum.org.uk))

**Performance with Integrity: Linking Performance to Values** – a tool-kit and executive guide to recruitment, appraisal and development linked to ethics and behaviour. ([www.cityvaluesforum.org.uk](http://www.cityvaluesforum.org.uk))

**Integrity Resources** – a single point of access to the ethical standards and advisory materials of a number of the major professional bodies. ([http://www.cisi.org/IntegrityResources/index.html](http://www.cisi.org/IntegrityResources/index.html))


**Investing in Integrity (iil)** – a Charter Mark developed by IBE and CISI which is designed to enable an organisation to reassure all its stakeholders that it’s business can demonstrate a commitment to act with integrity at all times, through a two stage process of accreditation. ([www.investinginintegrity.org.uk](http://www.investinginintegrity.org.uk))

**The Case for the ‘Board Mandate’** – the first in a series of guides and tool-kits published by the Good Governance Forum, which is convened by Tomorrow’s Company. ([http://tomorrowscompany.com/good-governance-forum](http://tomorrowscompany.com/good-governance-forum))

**Improving the quality of boardroom conversations** – second publication of the Good Governance Forum focusing on the importance of the conversations that underpin board effectiveness. ([http://tomorrowscompany.com/good-governance-forum](http://tomorrowscompany.com/good-governance-forum))

**Leadership 21C: Board Effectiveness** – developed by the Financial and Legal Skills Partnership this programme seeks to improve the quality and effectiveness of leadership for corporate boards across the financial and legal sectors. ([http://www.financialskillspartnership.org.uk/skills-resources/Leadership-21C-Board-Effectiveness](http://www.financialskillspartnership.org.uk/skills-resources/Leadership-21C-Board-Effectiveness))
The City Values Forum works to embed the principles of trust and integrity in the financial and business services sector and to improve business cultures and behaviours.

Formed in 2011 to deliver the recommendations of The Lord Mayor’s Initiative ‘Restoring Trust in the City’, the Forum is constituted as an informal working group reporting to The Lord Mayor.

The City Values Forum is working across a broad front with City banking businesses, professional and trade bodies and academic institutions to strengthen standards of integrity in the sector.

A series of initiatives is underway addressing standards of professional competence and sharing best practice – each aimed at improving business culture and behaviour.

No single initiative can remedy the failures of integrity revealed in recent years, but by acting with the support of many organisations, working throughout the financial and business services sector, we aim to reassert the City’s longstanding reputation for fair dealing.

If we succeed together we will inspire customers and clients to entrust us with their business and earn society’s endorsement of our economic role.
Sources and notes


5 For a description of what is meant by ‘courageous integrity’ please see http://www.cimaglobal.com/Documents/Thought_leadership_docs/Leading-with-Integrity-Engaging-Hearts-as-well-as-Minds.pdf

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We hope Governing Values proves to be an invaluable resource for all those charged with the responsibility of leading financial services and other companies in the City of London and throughout the United Kingdom.

Many people and organisations have come together to share their insights, knowledge and experience, recognising the absolutely critical role that culture aligned to purpose ‘lived’ through daily judgements and behaviours must have for future success - and to building the understanding and trust on which that success must rely.

This has been reinforced by the recognition that whilst there are many such resources for executives, little has previously been written for where it matters most: the boardroom.

It is in this context of originality as well as, we hope, significance and impact of contribution that we wish to thank all those whose support has been invaluable.

In particular to Oonagh Harpur who has advised throughout, engaging in every step of the process, contributing so many rich insights, and to Richard Finn, who has been there from the very start of The Lord Mayor’s Initiative, ‘Restoring Trust in the City’, championing culture.

The members of the City Values Forum have engaged in numerous ways, critically in their generous support of this output, alongside others, so that our whole really is greater than the sum of the parts, and that individually and collectively the aspirations of the Forum are met.

Governing Values has also benefited greatly from the collaboration with the Tomorrow’s Company ‘Good Governance Forum’, and in particular Richard Sykes and Richard Emerton. And special thanks also goes to the Chartered Institute of Personnel and Development and Ksenia Zheltoukhova for the part she played.
Within the Tomorrow’s Company team, Pat Cleverly’s very special craft and intelligence have made a critical contribution; Alexander Cowie has provided the bedrock of support that has been essential; and our thanks go to many staff and volunteers, especially Katie Preiskel.

Above all of course, our gratitude to the many people we have interviewed and consulted. Governing Values is above all for those who are actively involved in the boardroom and who are striving for the highest standards.

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Chief Executive, Chairman
Tomorrow’s Company The City Values Forum
‘The City Values Forum – embedding integrity and building trust’
www.cityvaluesforum.org.uk