



Chartered Institute of  
Internal Auditors



AUDITBOARD

London  
Business  
School



Leadership  
Institute

# Cultivating a healthy culture:

Why internal audit and boards must take  
corporate culture more seriously in a  
post-Covid world

March 2022

# Foreword

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## **A healthy corporate culture differentiates an organisation and impacts customers, financial performance, growth, reputation, recruitment, and retention.**

An unhealthy or sub-optimal culture impacts all these categories. At its worst it is a critical risk to the attainment of the organisation's aims and objectives and the sustainability of the organisation in the longer term.

These facts have been widely recognised in the internal audit profession for over a decade now and are repeatedly highlighted by a wide range of events we see in the media, regulators' commentary, and the analysis of the root cause of company collapses.

Given this background, the need for internal audit engagement is clear. Culture is a risk and is fundamental to the success of every organisation.

Against this backdrop we must ask ourselves: "Are boards and internal audit focussing enough on corporate culture and are they taking it as seriously as they should?". For many there has been strong progress, but for some the answer is no. It is clear from our research that not enough boards and internal audit functions are taking culture seriously, and now is the time for the profession to step up and do more. Urgent action is required to cultivate a healthy corporate culture to protect value, reputation, and long-term sustainability.

This report seeks to identify where good progress has been made, challenge the profession to up its game, and provide guidance for those who have yet to start or are early in their corporate culture journey. We urge you to read on to get the facts, get informed, and get ahead of the curve!

**John Wood**

Chief Executive Officer  
Chartered Institute of Internal Auditors

**Richard Chambers**

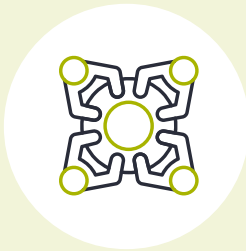
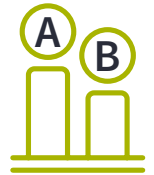
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# Key highlights from our research



**70.5%**

said the board had established and articulated what culture it wants for the organisation.



**65.7%**

believe the UK Corporate Governance Code should be further strengthened in regard to the responsibilities of company directors to promote, monitor, and assess the corporate culture.



**52.4%**

had not been asked by either the board or audit committee to provide reports on culture and/or inclusion, equality, and diversity initiatives.



**60%**

of respondents said their **audit plan included culture** within it:

**37%**

*said culture was integrated into standard audits*

**5%**

*said they planned on doing a standalone audit focussed on culture*

**18%**

*said they planned on auditing culture both in standard and standalone audits*



**44.4%**

said that they conduct interviews with members of the board to assess corporate culture.

**74.1%**

*said members of the executive team including the CEO*



**In the last 12 months**

**41.5%**

said they'd been invited to discuss the risks posed by corporate culture with the audit committee.

**30.5%**

*said executive management*

**13.4%**

*said the board*

## The Top 5

methods used to audit behaviours and culture are:



*Interviews*  
(64%)



*Surveys*  
(51.2%)



*Assessment of the timely and effective resolution of audit issues and/or risk exposures* (50%)



*Behavioural observation*  
(48.8%)



*Root cause analysis*  
(48.8%)

proxies for auditing culture are:



*Staff surveys*  
(73%)



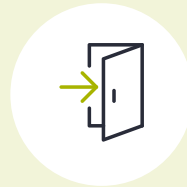
*Whistleblowing activity*  
(69.7%)



*Governance structures*  
(64%)



*Values statements and their incorporation into recruitment and performance management* (60.7%)



*HR grievance data and exit interviews*  
(56.2%)

## The Top 3

skills and competencies internal audit needs to audit culture are:



*Professional judgement*  
(74.4%)



*Soft/interpersonal skills*  
(69.5%)



*Use of experienced/senior internal auditors to lead the work* (63.4%)

business functions internal audit collaborates with when assessing culture are:



*HR*  
(71.4%)



*Risk management*  
(48.8%)



*Compliance*  
(42.9%)

## The risks

that have the most impact on corporate culture within an organisation are:



*Human resources, talent management, recruitment, and retention*  
(64.5%)



*Inclusion, equality, and diversity*  
(34.1%)



*Health, safety, and staff well-being*  
(31.6%)

## About the research and methodology



**Over September and October 2021, we conducted a survey of 110 senior internal audit executives (around half were chief audit executives) from all sectors of the UK and Ireland. Just over half of the respondents were from organisations that can be regarded as being ‘Public Interest Entities’. This includes FTSE 100, FTSE 101-350 and other publicly listed firms, and large private companies.**

The aim of the survey was to gain insights on what the internal audit profession is doing to support boards and audit committees in monitoring and assessing corporate culture, including insights on the approaches, methods, skills, and competencies used to audit corporate culture and behaviour.

In addition to the survey, we also held two roundtable discussions with senior internal audit executives representing a range of sectors. Organisations represented included: InterContinental Hotels Group, Ministry of Public Expenditure and Reform (Government of Ireland), the Bank of England, the Scottish Government, South West Audit Partnership (SWAP), Persimmon Homes, Lloyds Banking Group, Standard Chartered Bank, Taylor Wimpey, Culture Lab Consultancy, 3i Group, and BAE Systems. The roundtables were also attended by Vyla Rollins, Executive Director at the London Business School’s Leadership Institute who provided further insights.

The roundtables with senior internal audit executives helped shed further light and provide in-depth insights on the survey results, as well as shared best practice in corporate culture and behavioural auditing. We would like to thank them all for their contributions. Their involvement does not mean that they endorse the contents of this report.



## Introduction and context

**Organisational culture and the risks arising from an unhealthy or weak culture, are once again rising up the corporate agenda. This is in part being driven by changes and operational disruption brought about by the coronavirus pandemic. With large swathes of the workforce being forced to work remotely for much of the last two years, and the move towards “hybrid” working in the longer term, many organisations are grappling with the challenge of how to embed and maintain their organisational culture going forwards.**

At the same time organisations are coming under increased pressure from wider society to ensure that their corporate culture embraces and supports greater levels of equality, diversity, and inclusion (EDI). This has been driven by the emergence of the social inclusion movement - including the #MeToo and #BlackLivesMatter movements - which has now become part of the mainstream. High-profile public incidents that have made media headlines, such as the recent racism scandal that has engulfed the Yorkshire County Cricket Club, have sadly shone a spotlight on the risks associated with an unhealthy workplace culture. This example also underlines the strong interdependence and interlinkages between corporate culture and equality, diversity, and inclusion.

Equally, whilst much of the debate around organisational culture has focussed on the downside risks, the opportunities posed by a healthy, strong, and effective culture, cannot be overstated. Organisations regarded as having healthy cultures tend to be those that thrive, perform better, and are more resilient, as is evidenced later in this report.

The increasing prominence of organisational culture as a business-critical risk has been reflected in our most recent Risk in Focus research, with a 35% year on year increase in the number of chief audit executives citing

organisational culture as a top five risk. A similar upward trend is seen with human capital, diversity and talent management risk, with a 14% year on year increase.

We believe internal audit has a vital role to play, working in collaboration with other business functions, in assessing, monitoring, and providing assurance on corporate culture and the associated risks and opportunities. The Chartered Institute of Internal Auditors would like to see the profession stepping up and playing a pro-active role within their organisations in the corporate culture space. Our internal audit codes of practice already make clear that internal audit should include within its scope the risk and control culture of the organisation. But because ‘risk culture’ is only one aspect of organisational culture, we would like to see internal audit functions continue to evolve and encompass other important aspects of organisational culture within the scope of their work.

Indeed, that is why back in 2016 we did high-profile thought leadership work on the role of internal audit in supporting boards to keep their finger on the pulse of their organisational culture, with our previous report ‘Organisational Culture’<sup>1</sup>. This was published as part of our involvement in the Financial Reporting Council’s ‘culture coalition’.

Since then, the Financial Reporting Council has strengthened the UK Corporate Governance Code regarding corporate culture. The 2018 version of the Code now puts far greater emphasis on the role of company directors of premium listed firms in promoting, monitoring, and seeking assurance on the corporate culture, as well as the need to report on it.

Disappointingly, the evidence consistently suggests that the adoption of these new requirements by company directors appears to be moving at a glacial pace. The Financial Reporting Council's annual review of the UK Corporate Governance Code published in January 2020 concluded that only a small number of boards disclosed that they already receive reports on culture to aid their discussions. Only a handful regard culture as a key risk and there is limited discussion of assessing and monitoring culture.

Similarly, the latest review of corporate governance reporting published in November 2021 found that once again not much has changed. It found little progress in monitoring, assessing, and embedding culture, and its alignment with purpose, values, and strategy. We believe the audit regulator clearly needs to do more to encourage and support company directors in meeting their responsibilities on corporate culture. The low levels of implementation of the Code's new corporate culture requirements, three years after its publication, is simply not good enough.

Given this context we felt it was high time for a refresh of our thought leadership on this business-critical risk area. Internal audit is one assurance provider that could and should be providing the audit committee with reports and independent insights on corporate culture, including for discussion at board level.

Our latest research, based on a survey of over one hundred senior internal audit executives working in all sectors across the UK and Ireland, paints a mixed picture in terms of internal audit's corporate culture journey and suggests that progress in this area may have plateaued. It is encouraging that 60% of internal audit functions we surveyed

said that their internal audit plans included culture within them, and that a further 14% said that while it wasn't in this year's plan, they were planning on including it next year. However, that still leaves just over a quarter that aren't looking at it yet or planning to look at it.

Meanwhile, our survey suggests that nowhere near enough audit committees and boards are taking the risks posed by corporate culture seriously. Over half (52.4%) of senior internal audit executives we surveyed said they had not been asked by the board or audit committee to provide reports on corporate culture or EDI initiatives. Less than half (41.5%) said that in the last twelve months they'd been invited to discuss the risks posed by culture with the audit committee, and only 13.4% said the board. This is quite surprising given that corporate culture-related risk has been impacted because of the coronavirus crisis. Although we appreciate that at the same time, many businesses have been grappling with a myriad of other business-critical risks.

*Based on these research findings, our strong message to internal audit functions is clear: be proactive when it comes to corporate culture – don't wait for the board or the audit committee to come to you before undertaking a culture-related audit engagement. Be prepared to put your head above the parapet if you have concerns regarding your organisation's culture, use your voice, and ask searching questions. In particular, chief audit executives need to be braver and more courageous in having sometimes difficult and challenging conversations about corporate culture, and be willing to speak truth to power.*



At the same time, boards and audit committees should have greater confidence in seeking independent assurance and harnessing the skills of their internal audit function that the organisation has a healthy corporate culture, that is aligned with its purpose, values, and strategy.

Organisations and their internal audit functions must not wait for a major corporate culture related risk event to erupt, a crisis to manifest itself or the company to topple over, before doing something about it. Instead, organisations should get on the front foot and get ahead of the curve.



# What is corporate culture and why is it important to the work of internal auditors?



**Corporate, or organisational, culture, is broadly defined as being the shared attitudes, behaviours, principles, and values that drive action and purpose within an organisation and its people. Corporate culture is commonly referred to as being “the way things are done around here”, a phrase first coined by organisational culture expert Charles Handy in his 1981 book ‘Understanding Culture’.**

Organisations’ cultures differ greatly and come in all different shapes and sizes. They can be shaped by the sector they operate in, for example, the culture of an investment bank, in all likelihood, will differ greatly to that of a healthcare provider. Or a publicly listed company may have a very different culture, to that of a smaller family-run private firm. The lifecycle of a company can have a significant impact – for example the culture of a start-up company may differ greatly to a firm that has been around for decades, or in some cases centuries. Organisational culture may also be shaped and influenced by demographics, geographical location (including the national culture), along with the political, economic, and social environments they operate in. As well as of course shaped by the leadership styles of those in charge and the tone from the top. The culture of an organisation should be set by the board and cascade through the organisation by management, including the setting of clear expectations.

This definition of organisational culture was broadly reflected when we asked

senior internal audit executives to provide their own concise definition in the survey we conducted. Many cited the values, behaviours, ethics, attitudes, beliefs, thinking patterns, and tone from the top at an organisation, as the key things that constitute a corporate culture. However, perhaps a more interesting insight by some was that a corporate culture can also be defined by “how people act when nobody is watching”, “what our people do when nobody is watching”, or “how we do things when people are not watching”.

Organisational culture should matter to internal auditors, because having the right corporate culture, aligned to the organisation’s purpose, values, corporate strategy, and vision for the future, is fundamentally important to the effective leadership, sustainability, resilience, and governance of an organisation. An organisation’s culture can also have a significant impact on the risk management and internal control environment, and touches upon a broad range of other business-critical risks.

There are numerous examples of what happens when the culture, or attributes that comprise the culture, fails. An unhealthy culture can have a significant adverse impact on an organisation's long-term sustainability. Indeed, many major corporate collapses can be attributed to organisations that had unhealthy or 'rotten' corporate cultures, often fuelled by misconduct, the wrong tone from the top, and the mismanagement of risk<sup>2</sup>. For example, the Work and Pensions and the Business, Energy, and Industrial Strategy (BEIS) Committees' joint inquiry final report into Carillion's collapse was highly critical of the company's corporate culture and it was cited as a key reason for its failure<sup>3</sup>. Other examples include Enron, WorldCom, BHS, Patisserie Valerie, Wells Fargo, and Wirecard. On the other hand, a healthy and strong culture can help to enhance an organisation's long-term sustainability and they are likely to outperform their competitors. For example, scientific research studies suggest that a strong corporate culture is the most important factor in driving innovation, which in turn helps drive economic growth<sup>4</sup>.

It is therefore vital that internal auditors champion in collaboration with other business functions to monitor, assess, and provide independent assurance on corporate culture.



*“It is becoming increasingly clear to the ‘person on the street’ that the dramatic examples of governance breaches are driven by the mindsets, behaviours, and beliefs of those in the boardroom and C-Suite.”*

*Vyla Rollins, Executive Director, Leadership Institute, London Business School*

2. 'Rotten corporate culture' blamed for Carillion's downfall, People Management, May 2018

3. House of Commons Business, Energy and Industrial Strategy and Work and Pensions Committees Inquiry into Carillion, May 2018

4. Corporate Culture Is Most Important Factor In Driving Innovation, ScienceDaily, November 2008

# How has the Covid-19 pandemic impacted corporate culture?



There can be no doubt that the Covid-19 pandemic has impacted the corporate culture of organisations. This is particularly the case for organisations where much, if not all, of the workforce has needed to work remotely. Meaning that boards and executive management have faced significant challenges in promoting, embedding and more importantly, sustaining their corporate cultures.

But it is important to understand that not all the impacts have been negative, there have been some positive impacts too. This was highlighted in the discussions that we had with senior internal audit executives. Participants observed that within their organisations the pandemic has driven a laser-like focus on health and safety, to a far greater extent than ever before. This is even more the case for the travel and hospitality sectors. With hotels, restaurants, and airlines having to implement stringent enhanced hygiene processes to protect the health and safety of their customers and staff. This has meant that the culture within these organisations has had to evolve to help meet the challenges of the business.

Others observed that it was their organisation's strong corporate culture that helped them to get through the pandemic. But there were now some real challenges going forwards in maintaining their corporate culture, as it had been developed over time by people spending time together face to face. For example, companies where creativity and innovation are an important aspect of the culture, are facing significant challenges. This is because cultivating creativity and innovation is much harder when people are working remotely and unable to meet in person to share ideas and bounce off one another.

*The key dilemma many organisations are grappling with is how to sustain the strengths of their culture and stay connected to the workforce, which is likely to remain a challenge as organisations look to adopt hybrid working solutions longer-term. This has meant that organisations are looking for new ways to sustain, cultivate, and maintain their culture going forwards.*

However, without new measures and processes put in place, many of the senior internal audit executives that we spoke to highlight the real risk of cultural erosion and decay over time.

On the downside impacts, senior internal audit executives also observed that many of the internal control and risk management processes had been “thrown out of the window” during the height of the pandemic, as decisions had to be made quickly.

A good example of this would be in the public sector, where swift decisions needed to be made over the procurement of PPE, meaning normal stringent approval processes were often by-passed. This created significant challenges for maintaining the risk and control culture and in some cases resulted in procurement breaches i.e. PPE did not meet the correct standard and due to high demand resulted in excessive expenditure.

On the upside, working remotely has also delivered some cultural benefits and opportunities. The greater use of online meetings and team collaboration platforms has brought global and sometimes national teams in different geographical locations, much closer together through the normalisation of using the virtual world to stay connected. These will remain important communication channels for maintaining the corporate culture and team cohesion in the future.

Working remotely has also helped to bring down silos and workplace cliques, although the flipside is that it has removed informal networks and conversations. No longer can employees have an informal chat at the photocopier, or when making a cup of tea in the kitchen. This type of informal face to face human engagement is a key factor in helping to develop good internal human relationships within organisations, and much harder to replicate in an online format.

In terms of the pandemic's impact on the work of internal audit on corporate culture, some senior internal audit executives reported that they had been asked to give more formal opinions on how the culture is potentially changing. Questions internal audit teams were being asked to answer included "Are we losing the culture?", "Are employees fully on board?", "Do they understand the mission?"

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*"Things have changed since Covid and since we have been working remotely and now hybrid, we [internal audit] have been asked to give more formal opinions on how the culture is potentially changing."*

*Chief Audit Executive of a major financial institution*

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*"Working from home helped to bring down siloed working, on the other hand it removed informal networks in the coffee room. The pandemic didn't bring about fundamental changes to our culture, a few tweaks, some negative, some positive."*

*Dermot Byrne, Head of Internal Audit, Ministry of Public Expenditure and Reform, Government of Ireland*





## Questions for internal audit

- What is the organisation doing to maintain and embed the corporate culture going forwards?
- How is the organisation sustaining, enhancing, and maintaining the corporate culture with people working remotely, including for hybrid working?
- How are the impacts of the pandemic on the corporate culture being managed / addressed?
- Is the organisation reflecting on the changes it made during the pandemic and either revising or consciously accepting them going forwards?
- Is there evidence that the corporate culture is being gradually eroded or decaying because of remote working? How is this being measured, monitored, and reported on?
- What are we doing to build strong collaborative relationships with other functions or players in the organisation to partner with us in making culture measurement and monitoring a more 'engaging' effort?



# Are boards and audit committees taking corporate culture seriously enough?

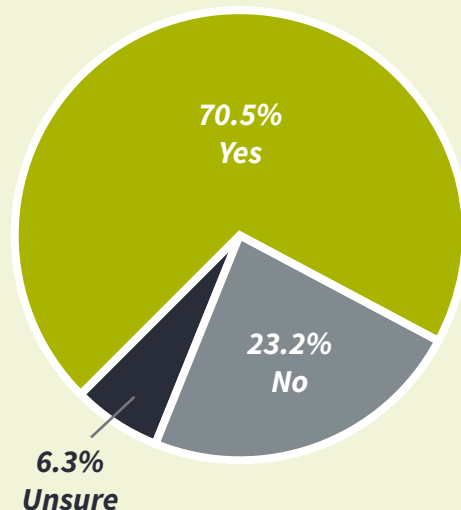


Articulating, establishing, and embedding the corporate culture is of fundamental importance to the success of organisations. The board's role in leading on this is critical including setting the tone, as well as clear expectations. The CEO's role in spearheading the culture is of particular importance and is one of the fundamental requirements of the job. No CEO can know whether the culture is what the board wants, without checking, testing, and measuring it.

However, the research that we have conducted would suggest that not enough boards and audit committees are yet taking corporate culture and the risks associated with it, as seriously as they should be. In supporting the board and audit committee to fulfill their responsibilities regarding corporate culture and diversity, we believe more should be seeking independent assurance and harnessing the skills of their internal audit functions.

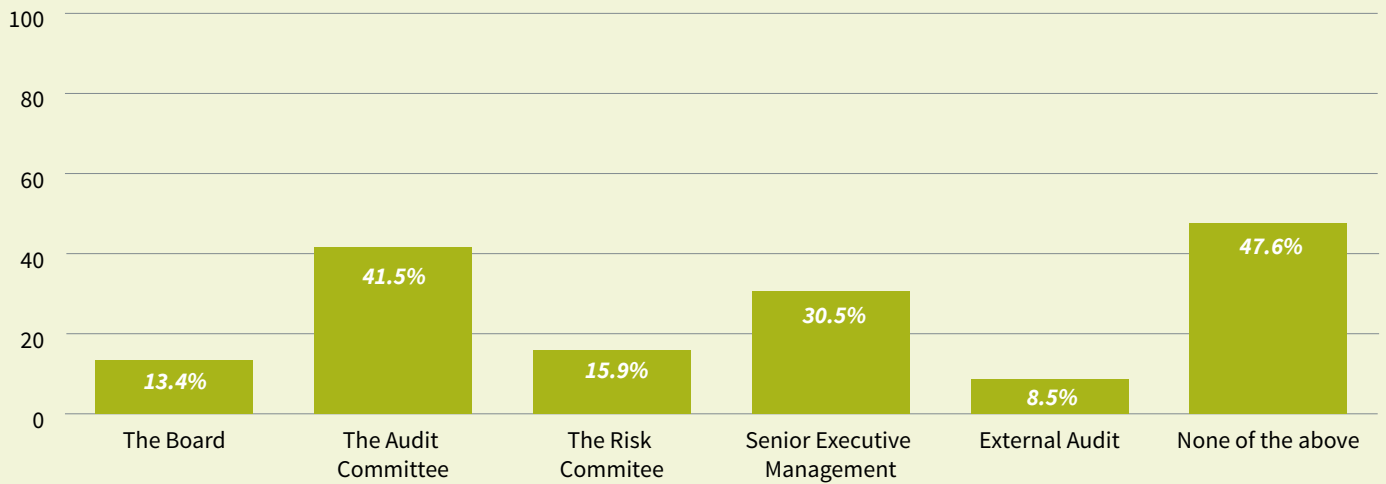
We were encouraged that just over 70% of respondents to our survey indicated that the board had established and articulated what culture it wants for the organisation, however, almost a quarter (23.2%) said their board had not. This is somewhat concerning, given that the board articulating what culture it wants and setting clear expectations, is fundamental to the effective governance, leadership, and stewardship of an organisation.

**Has your board established and articulated what culture it wants for the organisation?**



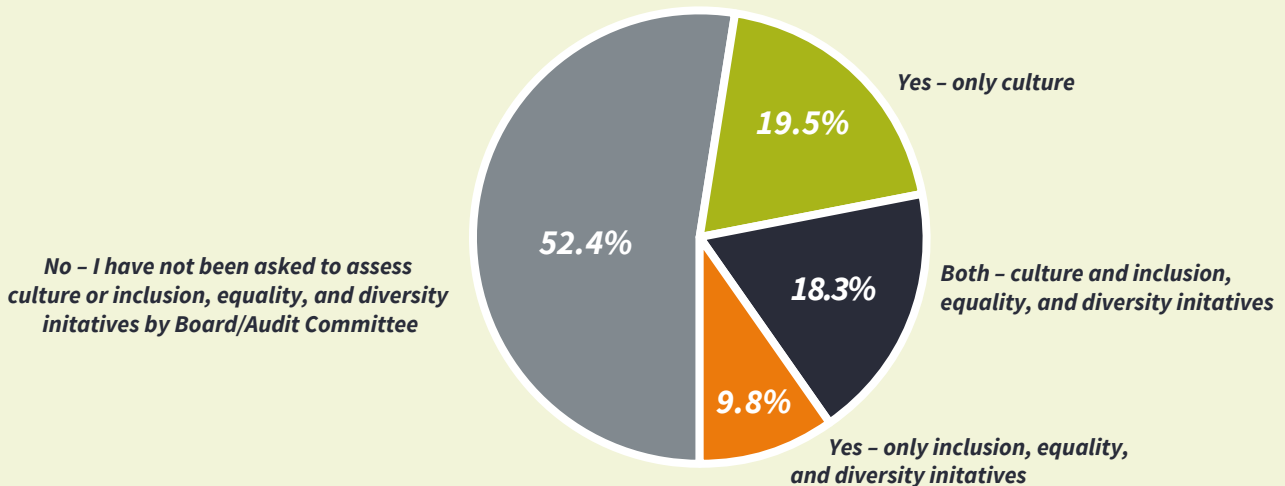
When we asked senior internal audit executives if they had been asked to discuss the risks associated with corporate culture with the audit committee, 41.5% said they had, but that means a majority have not. When asked if the board had requested to discuss the risks associated with corporate culture, the result is even fewer, with just 13.4%. It was quite concerning that 47.6% appeared not to have spoken to, or been asked to speak to, anyone in a governance role across the organisation. These results were therefore somewhat disappointing.

**In the last 12 months, have you been invited to discuss the risks posed by corporate culture with any of the following:**



It was even more disappointing that over half (52.4%) indicated they had not been asked by the board or the audit committee to provide reports on corporate culture and/or EDI initiatives. Once again underlining that boards and audit committees are not taking corporate culture and EDI as seriously as they should be, despite its importance in protecting value, reputation, and long-term sustainability.

**Have you been asked by either the board or audit committee to assess and provide reports on culture and/or inclusion, equality, and diversity initiatives at your organisation?**





It is clear given the data generated by this survey that more boards and audit committees need to step up and pay more attention to meeting their responsibilities on corporate culture. This is also reflected in the Financial Reporting Council's own research in their reviews looking at the adoption of the new requirements on corporate culture in the latest version of the UK Corporate Governance Code<sup>5</sup>. For two years in a row the annual review of corporate governance reporting<sup>6</sup> has found glacial progress in this regard. With very few premium listed companies meaningfully and adequately reporting on how they are monitoring, assessing, and embedding culture, and its alignment with purpose, values, and strategy.

## Changing the language as a way of winning stakeholder buy-in for auditing culture

A number of the senior internal audit executives that we spoke to as part of our roundtable discussions suggested that they had experienced push-back when speaking to the board or the audit committee about tackling issues around corporate culture. Some suggested that boards or audit committees might find talking about 'culture' difficult. However, one technique for internal audit to address this could be to change the language and reframe the discussion around 'behaviours' or 'organisational behaviour' as a way of progressing the discussion and winning stakeholder buy-in for undertaking work around corporate culture.

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*“In terms of it appearing in the plan and how audit committees might start talking about it, it depends on the chief audit executive having confidence to talk about it and the resources to tackle it. If there is internal resistance, change the language. One organisation's board didn't like talking about 'culture', but as soon as you started framing and talking about it as 'behaviour/s' they were all over it. So, changing the language can be a big part in moving the issue forwards.”*

*Kami Nuttall, Founder and CEO, Culture Lab Consultancy*

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5. UK Corporate Governance Code 2018

6. Annual Review of Corporate Governance Reporting



## Questions for internal audit

- What is our blueprint for culture at this organisation?
- How does our culture align with the organisation's purpose, values, corporate strategy, and vision for the future?
- How is the board communicating and articulating the espoused culture, behaviours, and values for the organisation? Has the culture been sufficiently defined by the board and have clear expectations been set?
- What is the chief executive officer doing to spearhead, promote, and embed the corporate culture?
- What measurement and reporting on corporate culture takes place and is reported to senior management and the board?
- How many times is corporate culture referenced in the annual report and accounts?
- How often is culture referenced in the agenda and minutes of relevant governance meetings?
- Is there clear evidence that the culture set by the board has been effectively cascaded down through the organisation by management?
- What is the culture of the internal audit team, and does it mirror the culture set by the board? If not, why not?

*"A very easy way of undertaking a litmus test of culture definition at the board level is to ask every single member to put their definition of 'culture' on a post-it note without their name on it. Then you ask everyone to reveal their answers. This can also be done in a virtual or hybrid boardroom environment using some very basic tools embedded, or that are 'plugins' used in conjunction with popular video conferencing platforms".*

*Vyla Rollins, Executive Director, Leadership Institute, London Business School*





## Rising regulatory expectations

**There is no doubt that regulatory expectations are rising when it comes to corporate culture, and internal auditors in all sectors should be prepared for greater regulatory scrutiny in this area in the future.**

This could not be more the case than for internal audit in the financial services sector, with regulators now demanding far more in the corporate culture space than many of the more traditional internal audit areas like governance, regulatory compliance, and financial controls.

*The increased regulatory focus on corporate culture in the financial services sector has of course been a consequence of the financial crisis in 2008, which exposed significant issues with risk culture at a number of banks. With a high-risk culture at some banks, resulting in a systemic risk to the entire economy.*

More recent events such as the LIBOR-rigging, PPI, and payday loan scandals have also led to greater scrutiny of corporate culture across the financial sector.

This was strongly reflected in our roundtable discussions with senior internal audit executives including a number from the financial services sector, with one participant reporting that both the Prudential Regulation Authority (PRA) and the Financial Conduct Authority (FCA) demanded 100% of all the cultural work their internal audit team did. Highlighting that there was a keen interest from regulators on internal audit's corporate culture work, and that they would come and discuss those items in more detail than some of the other larger pieces of audit work. With one chief audit executive reporting that they now get more airtime in the culture space

than some of the very specific regulatory areas. One participant also noted that they believed that financial services regulators, including the PRA, were taking a more robust and engaged approach to corporate culture as they believe it could have an effect on the systemic nature of the entire banking system in the UK, if there was a poor cultural outcome at a major financial institution.

However, it is important to note that it is not just financial services where regulators are putting an increased focus on corporate culture. For premium listed firms, the Financial Reporting Council's 2018 version of the UK Corporate Governance Code puts far greater emphasis on the roles and responsibilities of company directors regarding corporate culture.

The Code makes clear that a company's culture should promote integrity and openness, value diversity, and be responsive to the views of shareholders and wider stakeholders. Section 1 of the Code, Principle B, 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".

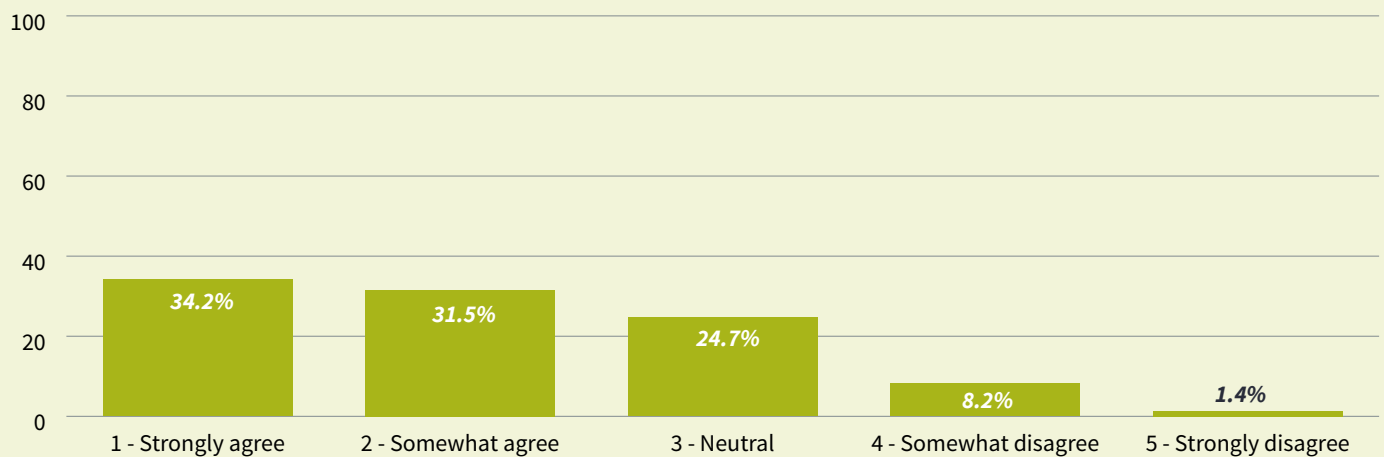
Provision 2 states: "The board should assess and monitor culture. Where it is not satisfied that policy, practices or behaviour throughout the business are aligned with the company's purpose, values and strategy, it should seek assurance that management has taken corrective action. The annual report should explain the board's activities and any action taken".

Internal audit is one assurance provider that could and should be providing reports to the audit committee and board on corporate culture and supporting company directors to meet these new requirements.

When we asked senior internal audit executives if they believed that the UK Corporate Governance Code should be further strengthened regarding corporate culture, a majority of 65.7% believed that it should be strengthened, with only 9.6% saying it should not.

### Please indicate to what extent you agree or disagree with the following statement:

I believe that the Financial Reporting Council's UK Corporate Governance Code should be further strengthened to highlight the responsibility of the board to promote, monitor, and assess the desired corporate culture, and if required to seek assurance that management has taken corrective action



A similar trend towards a greater focus on corporate culture can also be observed in the governance codes across other sectors.

The latest version of the NCVO Charity Governance Code<sup>7</sup> puts greater emphasis on integrity, values, and culture. It goes on to state that charities should monitor and measure how well they are doing on equality, diversity, and inclusion.

Similarly, the National Housing Federation Code of

Governance 2020<sup>8</sup> states in Principle 1.4:

“Culture: the board regularly considers and defines the culture and behaviours that will best enable the organisation to deliver its mission and values.

(1) The board leads by example and promotes the culture of the organisation.

(2) The board seeks regular assurance that its desired culture and behaviours are being enacted in practice in alignment with its mission and values”.

*“I was stunned by the fact that both the Financial Conduct Authority and Prudential Regulation Authority have demanded 100% of all cultural work that the internal audit team does, that is so different to everything else we do, so there is a keen interest from them and they will come and discuss those items in more detail than some of the other larger items.”*

*Former Chief Audit Executive of a large bank*

7. Charity Governance Code

8. Code of Governance 2020, National Housing Federation



## Questions for internal audit

- Does the organisation, including the internal audit function, have an open, constructive, and cooperative relationship with relevant regulators in regard corporate culture?
- How is the organisation meeting the requirements of regulators in regard to monitoring and assessing the corporate culture?
- How is the organisation complying with any requirements of relevant corporate governance codes in regard to corporate culture?

## What risks have the most impact on corporate culture?



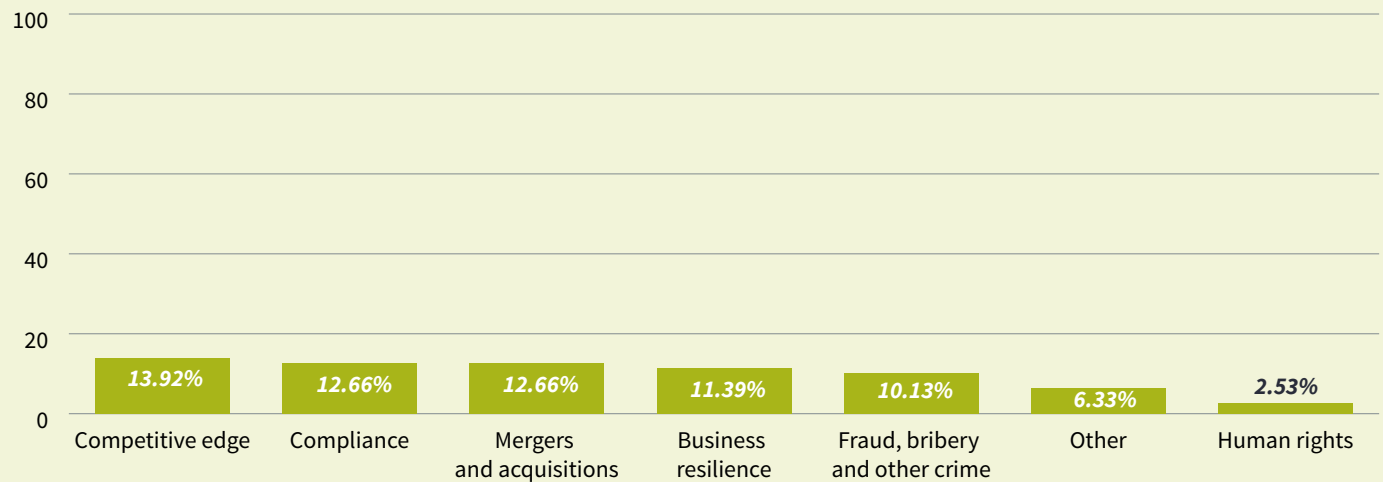
**Corporate culture is not just a risk in its own right, but it has a significant impact on a broad range of other risks, and vice versa with other key risks having a big impact on the corporate culture.**

As one might expect, human resources, talent management, recruitment and retention risk was identified by respondents to our survey as the number one risk that has the most impact on the corporate culture, with 64.5% of survey respondents voting it a top three risk. This was followed by 34.1% citing inclusion, equality, and diversity risk, followed by 31.6% of respondents who cited health, safety and staff well-being as being a top three risk to impact on corporate culture.

However, there were several additional business-critical risks that were also identified as having a significant impact on the corporate culture. This included corporate governance (30.3%), ethics (27.8%), reputation (22.7%), and regulatory and legal (19%), along with a number of others shown in the graph on the next page.

*This suggests that when internal audit functions are auditing some of these business-critical risk areas as part of their audit plans, it would be useful to incorporate and integrate into these audits, an examination of the potential impact some of these risks may be having, or could have, on the overall organisational culture. As well as examine the impact of the organisational culture itself on these business-critical risk areas.*

## Please select the top three risks that you think have the most impact on corporate culture within your organisation



In particular, when auditing human resources, talent management, recruitment and retention risk, internal audit should look at whether the recruitment process aligns to the expectations set by the board in relation to the culture, including equality, diversity, and inclusion considerations. Additionally, examine whether development plans and performance management processes align to the values and organisational cultural expectations. It can take many years to embed or change the culture of an organisation and over this time many people will have been recruited and even more subject to performance review. It is fundamental that the recruitment process is fully aligned to the expectations for the corporate culture and there should be a review of the success of the process. Failure to do this properly can undermine the success of the expectations being met and stymie progress.



## Questions for internal audit

- Is culture a part of every audit engagement? Particularly the audits of those business-critical risks with the greatest impact and interdependency with the corporate culture?
- Is the internal audit function assessing how business-critical risks could be impacting the corporate culture and vice versa?

*“It is also just as important to have a robust, confidential exit survey process in place, to help you determine if your organisation’s culture may be contributing to the loss of talent in your organisation. The phrase ‘people don’t leave bad jobs they leave bad managers’ does have a strong grain of truth in it and is supported by research.”*

*Vyla Rollins, Executive Director, Leadership Institute, London Business School*



## How to tackle culture audits: standalone, integrated, or continuous audits?



**When it comes to auditing culture, the clear message that came from our roundtable discussions with senior internal audit executives is that there is no one size fits all approach. Each organisation and internal audit function should customise their approach based on their individual circumstances. Not least because culture is a broadly defined term, therefore each organisation and their internal audit function will think about it differently and manage it differently.**

This was reflected in our survey results, with 37% saying they integrate aspects of culture into their standard audits, 5% said they were doing a standalone culture audit, and 18% said they were doing both.

A number of the participants at our roundtable discussions observed that as well as internal audit carrying out its own work in the culture space where appropriate, internal audit also has an even more important role in assessing how well first and second line business functions are doing at assessing, measuring, and monitoring culture. For example, this might involve reviewing how well the HR or risk management function is doing in monitoring, assessing, and embedding corporate culture.

Other participants, including those from financial services, observed that they tend to mainly focus on 'risk culture' and that this is integrated into standard audits.

The overall view of the senior internal audit executives we spoke to is that corporate culture should be integrated into all audits, particularly those audits of business-critical risks with the most interdependency with corporate culture, such as HR, talent management and recruitment and retention risk; inclusion, equality and diversity risk; and health and safety risk.

One approach is to also adopt continuous auditing on corporate culture. Internal audit should consider cultural aspects every day in every interaction and audit engagement that takes place. Internal audit has multiple interactions across the organisation every day and should therefore be able to use these engagements to gauge the health of the corporate culture, and highlight areas where the espoused culture is not being appropriately adhered to. Internal audit must use its ears and eyes to play close attention to the culture and behaviours it sees in front of it every day.

Some of the senior internal audit executives we spoke to could also see the value on occasion and where appropriate, in carrying out a standalone audit on corporate culture, to undertake more of a deep dive into some of the cultural and behavioural issues and to gain deeper understanding and insight.

A good example of this approach was the 'culture review' that was undertaken by the internal audit function at the Government of Ireland's Department of Public Expenditure and Reform. A case study of this work is included at the end of this report.

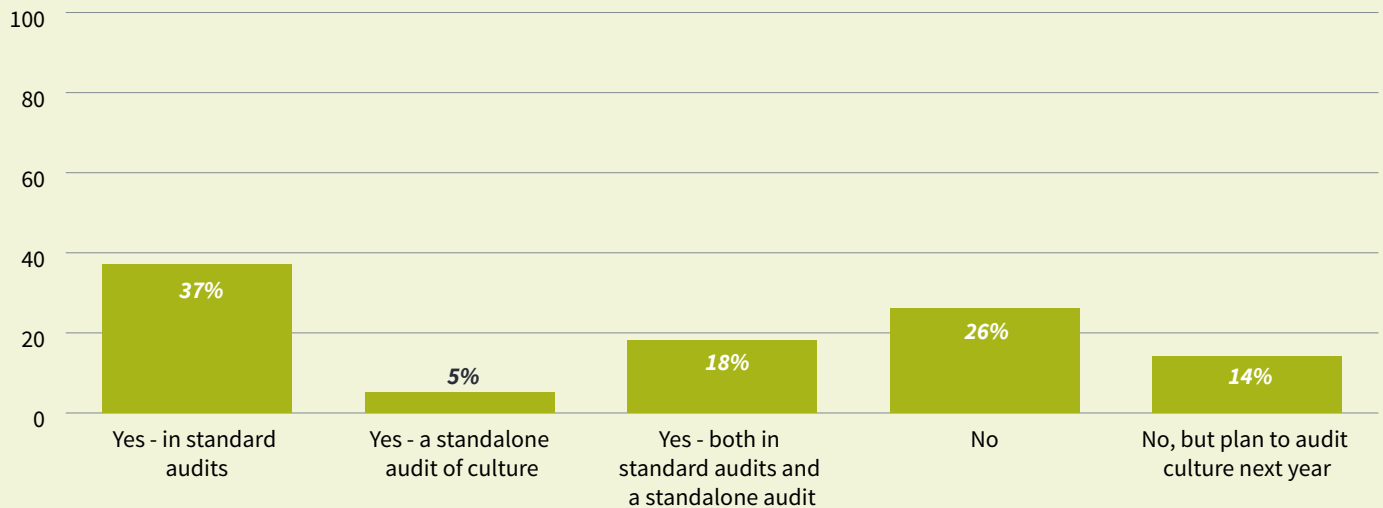


*“I’ve done culture audits for a range of clients, they can be both standalone or integrated. The thing that is important is getting the question right, what is it that we want to know? The most powerful thing is the employee survey, but I have a problem with it, in that most of them are standard, they only measure one aspect of culture, which is employee experience, which is problematic as it is from a management perspective. If you truly want to know employee experience of culture then you should be thinking of asking the question slightly differently. So, for example, how do our values show up at work?”*

*Kami Nuttall, Founder and CEO, Culture Lab Consultancy*



## Does your audit plan include any aspect of culture either integrated into aspects of your standard audits or as a standalone audit of culture?



## Connecting the dots: the importance of cross-organisation collaboration



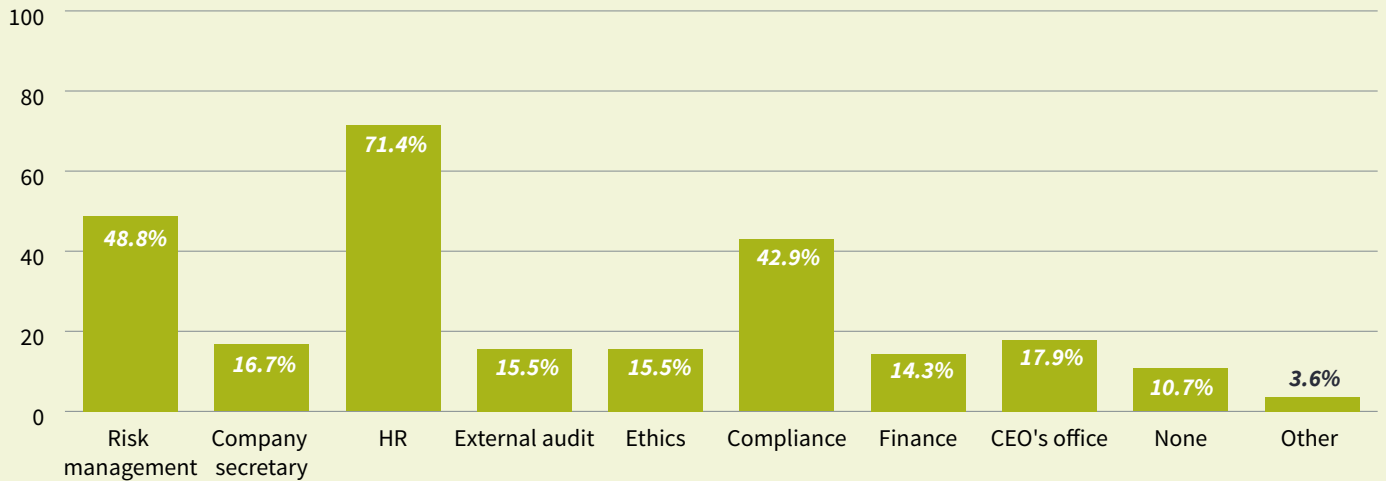
Our research has found that internal audit functions collaborate with a vast array of relevant business functions in their work in auditing corporate culture and this is very encouraging. As you might expect, the top business function internal audit collaborates with when assessing the culture is HR, with 71.4% of survey respondents selecting this as an option. This was followed by risk management (48.8%), compliance (42.9%), and the company secretary (16.7%).

*We believe that internal audit, as the third line, with its helicopter view of the entire business operation, is in a strong position to foster greater cooperation, collaboration,*

*and communication across the various business functions in regard to corporate culture.*

Internal audit can help to ensure there is a joined-up approach, connect the dots and support organisations to more effectively assess, monitor, and embed their organisational culture.

## Which other business functions do you collaborate with when assessing culture?



## Questions for internal audit

- How is the internal audit function helping to encourage and facilitate a joined-up approach in the monitoring and assessment of corporate culture?
- In supporting a joined-up approach, is the internal audit function meeting with and engaging all the relevant other business functions it should be in effectively auditing the corporate culture? Are there other business functions worth engaging on this topic?
- When meeting with other business functions is corporate culture a discussion item on the agenda?

# What proxies and methods should you use to audit behaviours and culture?



Corporate culture can be measured using a whole range of quantitative and qualitative measures. To support their work internal audit functions use a range of proxies and methods to audit behaviours and culture. The fact is internal audit has access to a considerable amount of data at its fingertips, both from its own audit work and from across other parts of the organisation. This data can be harnessed to provide fascinating insights and trends regarding corporate culture.

## Proxies

In the survey research we conducted of senior internal audit executives, the number one proxy used for internal audit's work on corporate culture is staff surveys, with 73% of survey respondents selecting this option. This was followed by whistleblowing activity (69.7%), governance structures (64%), values statements and their incorporation into recruitment and performance management (60.7%), HR grievance data and exit interviews (56.2%), management of customer complaints (49.4%), and pay, reward, and incentive structures (44.9%).

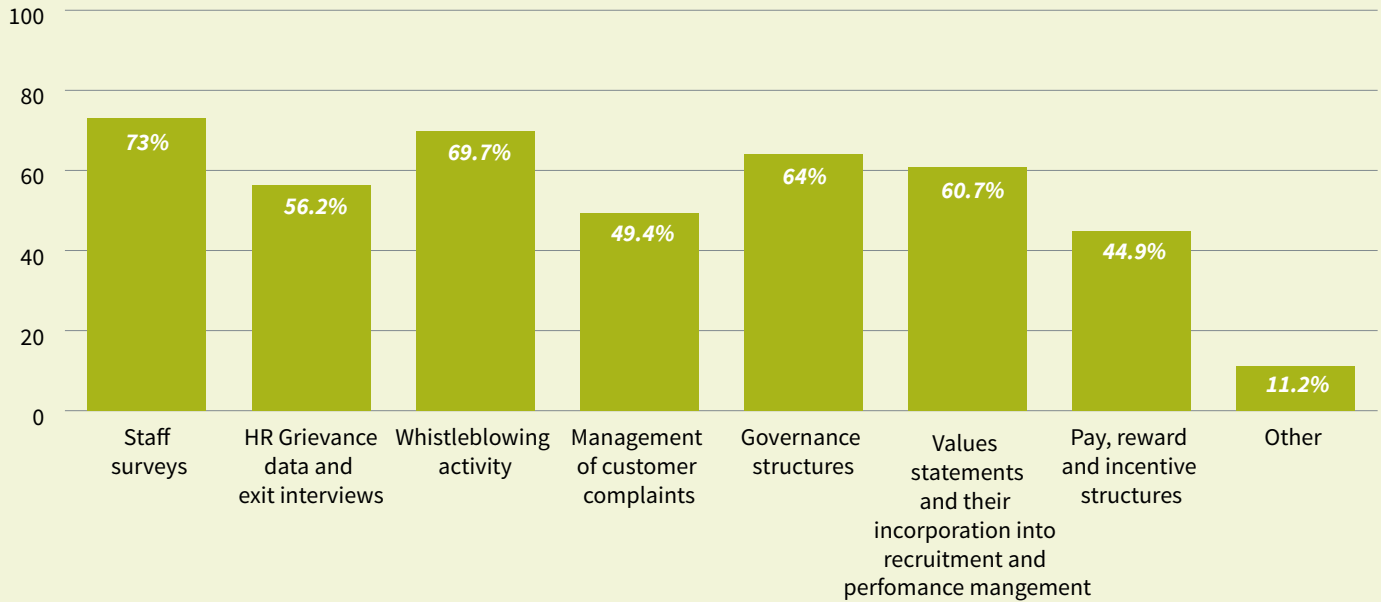
This range of proxies was broadly reflected in the roundtable discussions that we conducted with senior internal audit executives. Many reported using staff surveys conducted by the HR function. However, some participants did voice scepticism around their use and validity, including raising some concerns. Specific concerns raised included that many of these surveys are 'canned' or 'off the shelf' and often only measure one aspect of culture, the employee experience, which is often framed

from a management perspective. Another significant concern was that these surveys are sometimes used to help determine performance-related remuneration of management. With a risk that management might try to influence or manipulate what their staff say in these surveys.

Therefore, if internal audit decides to use the staff survey as a proxy to support their culture audits, they should do so with a degree of professional scepticism. This should include assessing how the survey is carried out, including the integrity of the process and the results, and whether the survey is asking the right questions.

If internal audit does have concerns, then they should take appropriate action. This should include speaking to HR, senior management, and the audit committee. As well as flagging these issues and ensuring they are documented in their culture audit reports, this should also include following-up on any recommended remedial actions.

## Which of the following do you use as proxies for auditing culture?



## Methods

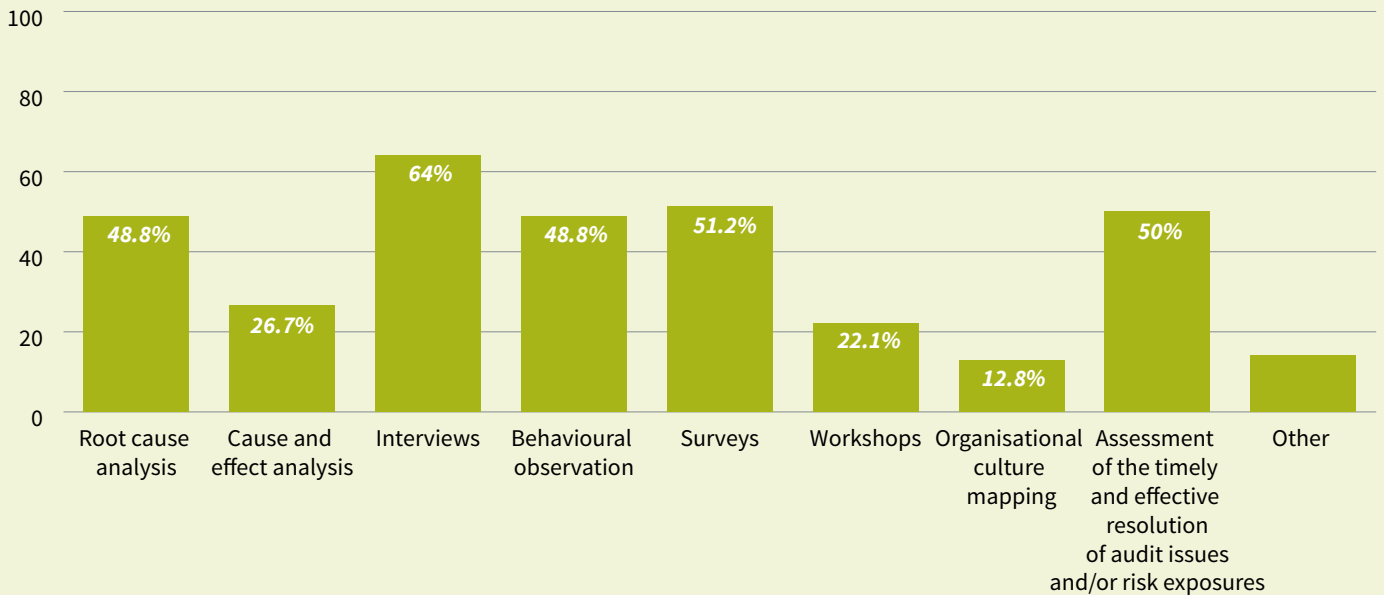
Our survey found that the top method used for auditing culture was interviews, with 64% of survey respondents selecting this option. This was followed by surveys (51.2%), assessment of the timely and effective resolution of audit issues and/or risk exposures (50%), behavioural observation (48.8%), root cause analysis (48.8%), cause and effect analysis (26.7%), workshops (22.1%), and organisational culture mapping (12.8%).

Our roundtable discussions with senior internal audit executives revealed that they deploy the full range of these methods in their corporate culture audit engagements. Many of the senior internal audit executives we spoke to saw the value in using quantitative surveys. Often these surveys were used as a first stage of the process to help provide context, shape the scope of the audit and to identify key areas to do more of a deep-dive exploration.

However, the senior internal audit executives also emphasised the importance and value of undertaking qualitative analysis and research, with a strong emphasis on the need to use one-to-one interviews and focus groups as a way of listening to people and getting richer insights. Internal auditors should also observe behaviours every time they undertake an audit engagement and in the meetings they attend as part of their work, incorporating and observing behaviours in everything they do, using a continuous auditing approach. In conducting focus groups, a number of senior internal audit executives harnessed external expertise to run these.

Some even co-sourced or outsourced their culture audits to help ensure their independence.

## What methods do you use to audit behaviours and culture?



*“The team who are behavioural specialists will start off with a survey, to get an indication of how many people return it. Our assumption is the higher the proportion of people that return it, the more likely it is that there may be issues in that particular area of the business. Because people are looking to speak to somebody. They will then go in and do a series of one-to-one interviews, and then possibly roundtable discussions. In the survey there is free/open commentary and that is relatively rich pickings. Once you’ve got that rich data, people sat in a room trying to draw data together and make a map and look at the risks coming out of it. Looking at things that might happen if there isn’t an intervention in the near future.”*

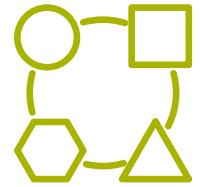
*Former Chief Audit Executive of a large bank*



## Questions for internal audit

- When using proxy data, like staff engagement surveys, have you assessed the integrity and validity of the data being used and the process used to gather it, applying an appropriate level of professional scepticism?
- Is the internal audit function using the full suite of proxies and methods available to audit corporate culture, or are you becoming over-reliant on just a few?
- Is there an appropriate balance between both quantitative and qualitative research methods?

# What skills and competencies are required when auditing corporate culture?



Internal auditors need a broad range of skills and competencies to audit corporate culture, and this was largely reflected in our survey results. The top five skills and competencies needed to audit corporate culture cited by respondents were professional judgement (74.4%), soft/interpersonal skills (69.5%), use of experienced/senior internal auditors to lead the work (63.4%), enhanced communication skills to deliver unpalatable findings (45.1%), and influence and negotiation skills (42.7%). Other skills and competencies that were cited as important included training from specialists on qualitative methods and survey design (34.1%), and the use of organisational psychologists within the internal audit function (12.2%).

In addition to this more tangible list of skills and competencies, Richard Chambers, former President and CEO of the Global IIA and now the Senior Internal Audit Advisor of AuditBoard often shares a story that is pertinent to the skills internal auditors need when auditing culture. Chambers had given a lecture to an audience of senior board chairs in India on internal audit's role in auditing culture. At the conclusion of his remarks, one of the distinguished Chairman of a major Indian company rose and observed: "I agree that internal auditors should audit culture. But you must expand the senses you use as you undertake these audits. Internal auditors typically rely on their sense of sound and sight. When auditing culture, you must also leverage your sense of smell." While he was clearly using a metaphor, the board chairman highlighted just how different the skills need to be when auditing culture.

In fact this is partly why some of the more mature internal audit functions now employ organisational psychologists and behavioural risk experts within their teams, to do much of their audit work on corporate culture. This is particularly common within many of the large banks and financial institutions, as part of their internal audit function's response, evolution, and increased focus on culture following the financial crisis of 2008.

However, even for smaller internal audit functions, it is likely that even if you don't employ dedicated specialists, members of your internal audit team will need the skills and knowledge required to audit corporate culture. This doesn't necessarily mean that all internal auditors will be required to be subject matter experts on corporate culture, but they will need to have a sound grasp of knowledge and an understanding of the issues.

In this sense corporate culture audits should be tackled no differently than audits for other key areas of the business. If internal auditors are required to audit the financial, information technology, sales or marketing areas of the business, then one would expect these auditors to have a certain level of expertise and knowledge.

If internal audit functions are therefore looking to undertake corporate culture related audit engagements, then they should ensure that members of their team have sufficient skills, knowledge, and expertise to be 'culture auditors', or if required undertake upskilling and training in this area<sup>9</sup>. This should also include an in-depth understanding of the organisation, particularly around mission, purpose, objectives, and values. Ensuring they have strong commercial knowledge, as well as people knowledge.

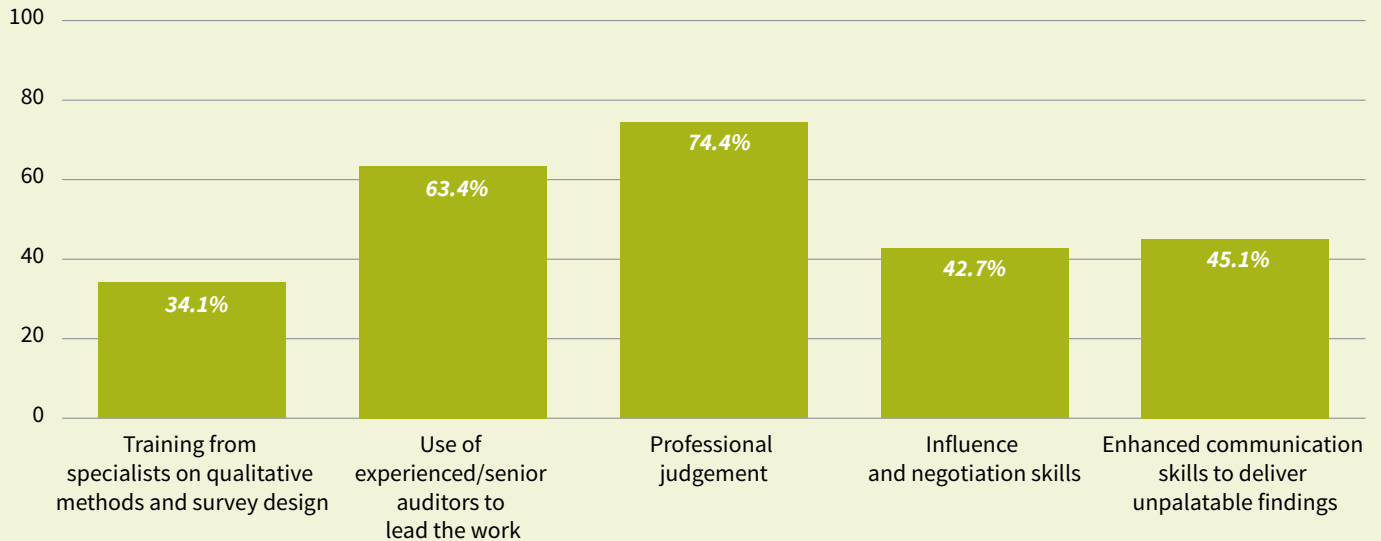
*“This area is all about the skills of the future and the need to up-skill internal auditors on a range of topics. Culture is one of those. You’re not going to be expert, but you need a reasonable grasp.”*

*Anthony Kennedy, Audit Director – Finance, Culture, People & Property,  
Lloyds Banking Group*



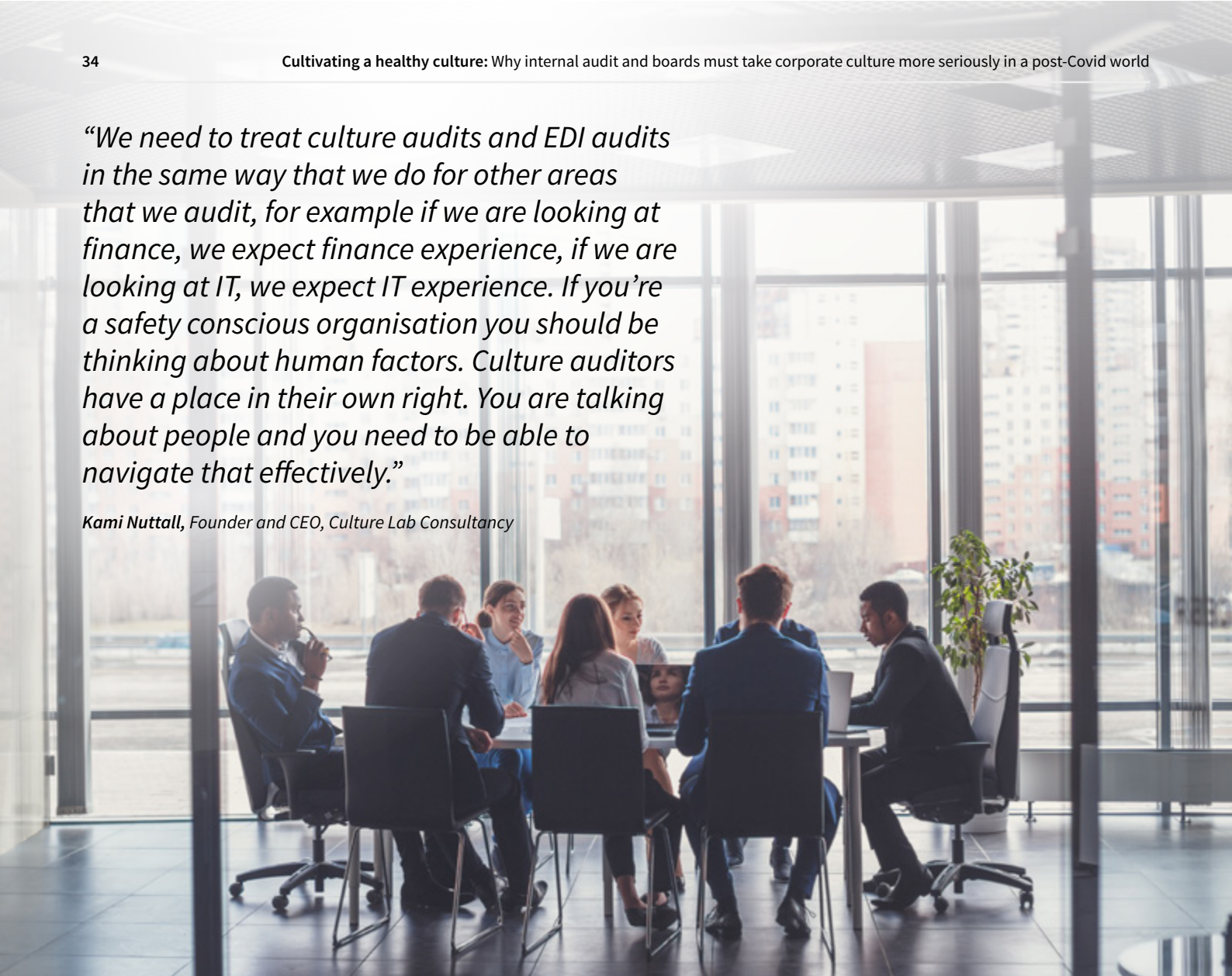


### What skills and competencies does internal audit need to audit culture?



*“We need to treat culture audits and EDI audits in the same way that we do for other areas that we audit, for example if we are looking at finance, we expect finance experience, if we are looking at IT, we expect IT experience. If you’re a safety conscious organisation you should be thinking about human factors. Culture auditors have a place in their own right. You are talking about people and you need to be able to navigate that effectively.”*

*Kami Nuttall, Founder and CEO, Culture Lab Consultancy*



## Questions for internal audit

- Does the internal audit function have the appropriate skills, knowledge, and competencies to effectively audit corporate culture, in the same way that it does for other business-critical risk areas?
- Do members of the internal audit function need additional training to effectively audit corporate culture?
- Would the internal audit function benefit from employing organisational psychologists/behavioural experts in auditing corporate culture (this might involve the use of a guest auditor seconding someone from another business function e.g. HR)?
- Has the internal audit function considered co-sourcing or outsourcing options when auditing corporate culture?

# Working with cultural risk management frameworks to support culture audits



The use of cultural risk management frameworks can be a useful tool to support internal audit's culture audit work. A number of senior internal audit executives that participated in our roundtable discussions reported using them.

## Financial Services Culture Board Framework

In financial services a number of internal audit functions cite using the Financial Services Culture Board's (formerly the Banking Standards Board) cultural risk management framework<sup>10</sup>, based on nine key attributes. This helps internal audit to link their culture work and observations to a commonly used industry standard and a reference point to use the same language and terminology. The nine attributes include: shared purpose, honesty, competence, reliability, responsiveness, personal/organisational resilience, accountability, openness, and respect.

There is no reason why internal audit functions outside of financial services couldn't also use, adapt the framework, or indeed use it as the basis to develop their own framework based on their own organisation's espoused values and behaviours.

## Financial Services Culture Board Framework



The Institute of Risk Management (IRM) have produced a 'Risk Culture Framework' and accompanying practical guidance<sup>11</sup>, to help risk managers better understand risk culture within an organisation. There is no reason why internal audit functions could not use the framework and associated guidance to help inform their work on both risk culture and the wider organisational culture and behaviours.

## IRM Risk Culture Framework



*“We have eight company behaviours defined that everyone should be aware of. What we have done in internal audit is to set up a cultural assessment framework, based on these eight behaviours, looking at each one from the perspective of risk and potential red flags, that could be warning signs of cultural issues within certain teams. Now introduced into every audit, we do an assessment using this framework of these eight red flags. We decided rather than do a standalone audit on culture, we would do it as a small part of every audit that we undertake. So, we now assess things like pressure to deliver, trust, tolerance of breaches, as part of every audit, then give ratings against it. This is the first year we have done it, and six months in, there are some interesting results. We have found positives as well as negatives.”*

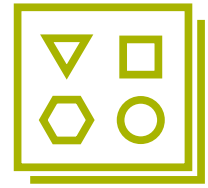
*Chief Audit Executive of an aerospace company*

*“We thought it would be helpful to peg our culture audits to an industry standard. So, we give insights on culture against the BSB/Financial Services Culture Board’s nine attributes. So, we’ve got a reference point that we use the same language and wording. Honesty, Accountability, Openness, Competence, Reliability, Shared purpose, Respect, Resilience, Responsiveness. All terms we reference against.”*

*Anthony Kennedy, Audit Director  
– Finance, Culture, People & Property,  
Lloyds Banking Group*



# The importance of equality, diversity, and inclusion to corporate culture

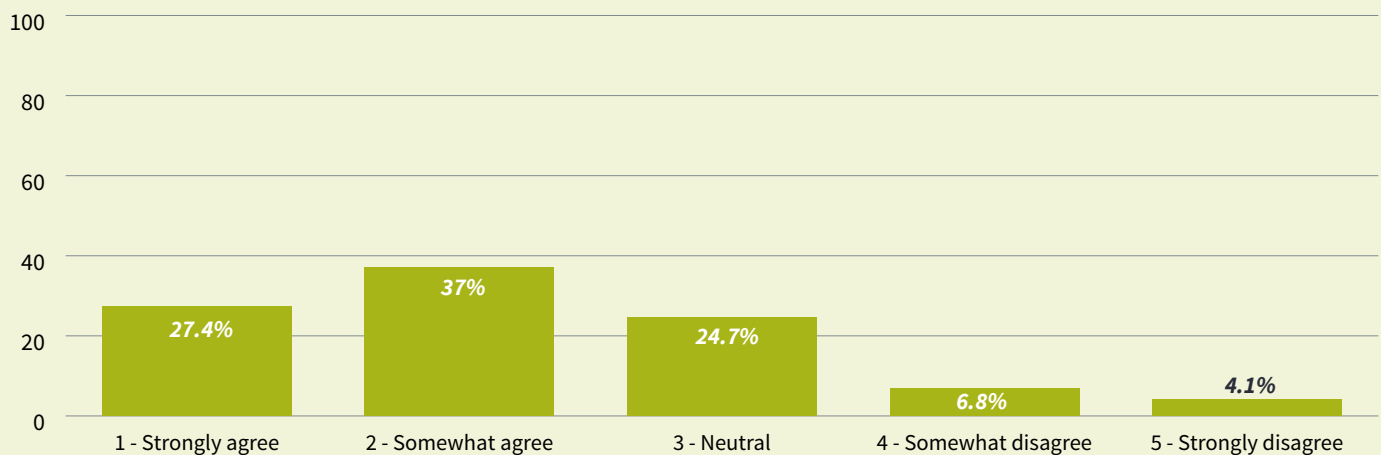


It is becoming increasingly important for organisations to ensure that their cultures help to champion and embed the equality, diversity, and inclusion agenda. Indeed, equality, diversity, and inclusion is cited by 34.1% of respondents to our survey as a top three risk that impacts the corporate culture.

It was therefore encouraging that 64.4% of respondents to our survey believed that the corporate culture supports the equality, diversity and inclusion campaigns, initiatives and practices that are in place at their organisation.

## Please indicate to what extent you agree or disagree with the following statement:

I believe that the corporate culture supports the inclusion, equality and diversity campaigns, initiatives and practices that are in place at my organisation



The emergence of the #MeToo and #BlackLivesMatter social movements have put even more pressure on organisations to ensure their corporate culture supports and underpins a more equal, diverse, and inclusive workplace. Furthermore, high-profile public scandals, linked to equality, diversity, and inclusion, such as the recent racism scandal at the Yorkshire County Cricket Club, have highlighted the consequences of an unhealthy corporate culture. This example also demonstrates how corporate culture and equality, diversity, and inclusion are in many respects two sides of the same coin and help to feed one another.

There is a strong business case for organisations to have a corporate culture that helps to underpin equality, diversity, and inclusion. According to a 2018 study by the Centre for Economics and Business Research, the economic cost of workplace discrimination to the UK economy is forecast to be £127bn. £123bn due to gender discrimination, £2.6bn due to BAME discrimination, and £2bn due to LGBT+ discrimination. On the other hand, the UK's most diverse workplaces are 12% more likely to financially outperform their industry average than the least diverse companies. Firms with the most developed diversity policies are 15% more likely to financially outperform those with less focus on diversity. This evidence suggests there is a significant financial dividend associated with corporate cultures that promote and embed equal, diverse, and inclusive workplaces.

However, increasingly within organisations it is as much about the fairness case for the corporate culture to underpin the equality, diversity, and inclusion agenda as it is the business case. This is being driven largely by the need to deliver on increased stakeholder expectations, including from the workforce, customers, and suppliers as well as the wider public.

Meanwhile, organisations are also facing increased regulatory requirements in regard

to EDI-related non-financial reporting, such as a greater focus on gender and ethnicity pay gap reporting.

*Internal audit has a key role to play in providing assurance that the corporate culture is supporting the equality, diversity, and inclusion agenda and vice versa.*

A chief audit executive we spoke to suggested that internal audit has an important role in providing assurance on the integrity of the equality, diversity, and inclusion information being reported to the board and externally.

As well as ensuring that the organisation has the right policy statements in place regarding equality, diversity and inclusion, internal audit also has an important role to play in ensuring organisations' practice what they preach in this space.

While there are strong interlinkages between EDI and corporate culture, and internal auditors can use EDI measures and data to assess the health of the corporate culture, the clear consensus in the roundtable discussions that we held with senior internal audit executives was that EDI is a deep topic in its own right, that needs its own space.



## Questions for internal audit

- Does the organisation, including the board, recognise and embrace the importance of equality, diversity, and inclusion as part of the corporate culture?
- Does the culture set by the board and cascaded through the organisation include equality, diversity, and inclusion?
- Has the integrity and validity of the EDI data the organisation is using been validated?
- Do you have the same level of comfort as to the accuracy of the EDI data, as you do the financial data?
- Has the workforce had EDI training? Is it updated on a regular basis?
- What is the second-line capability to provide EDI assurance?
- If the organisation has made public statements in regard to EDI, how is it living up to those statements and ensuring it is practicing what it preaches?
- Is the voice of the workforce regarding equality, diversity, and inclusion heard at board and senior management meetings?

# The importance of assessing and testing ‘psychological safety’ in auditing culture



Psychological safety is a belief that individuals will not be punished, alienated, humiliated, ignored, and/or silenced for voicing ideas, sharing hypotheses, thinking aloud, asking questions, sharing concerns, highlighting oversights or mistakes. More than that it can be described as a state of being in the moment. Does a person feel like a valued member of their team? If they speak-up will their manager listen to them and take them seriously? Fundamentally, do people feel comfortable being their true authentic self in the workplace?

*Assessing levels of psychological safety is therefore an important indicator when examining an organisation’s corporate culture and is linked to issues around equality, diversity, and inclusion, in terms of diversity of different ways of thinking. The right organisational culture and tone from the top can help to support higher levels of psychological safety.*

The most mature and advanced organisations, and their internal audit functions, are now incorporating and integrating assessment and monitoring of psychological safety into their work in auditing culture.

A chief audit executive we spoke to at our roundtable discussions said they now embed assessment of psychological safety in their surveys to help identify any psychological safety issues within teams. They will then compare the results of a particular team against the norm of everyone else. They have found that if the psychological safety scores are lower, it is more likely they’ll find behavioural risk issues.

Another chief audit executive said that they do try to cover psychological safety when carrying out their deep-dive culture audits, however that this tended to be done through one-to-one interviews and focus groups.

Other chief audit executives we spoke to said that there has been an increased focus and a shift in terms of psychological safety, with its assessment being integrated into HR’s employee engagement survey. This will then be used by the internal audit team to support them in auditing corporate culture.

One simple but effective tool used by one chief audit executive in assessing psychological safety was asking in each audit interview whether the auditee had been asked to do anything they felt uncomfortable with. In circumstances where the auditee says they have been asked to carry out things they didn’t feel comfortable doing, then internal audit should ask why they felt uncomfortable, for example was it because the thing they were asked to do felt inappropriate, compromised their integrity, or in breach of the organisation’s rules? Or was it because they hadn’t been sufficiently trained and so didn’t feel sufficiently competent to do the particular task they’d been asked to do?





## Questions for internal audit

- Does the organisation, including the board, recognise and embrace the importance of psychological safety?
- What are the first and second line functions doing to monitor and assess psychological safety e.g. is it now being assessed within the staff engagement survey?
- Is assessing psychological safety embedded into internal audit's own work on corporate culture?

## Harnessing data-analytics and technological innovation in auditing culture



**In the age of big data, and with many organisations harvesting and collecting a whole range of data that can be used in assessing the corporate culture, many internal audit functions are now harnessing the power of data-analytics and technological innovation when auditing this risk area. Indeed, we would argue that the use of data-analytics in auditing culture is both essential and non-negotiable if it is to be assessed effectively.**

One chief audit executive that we spoke to used data-analytics in their culture audits to help identify HR cultural issues as a general risk factor. They will then use this to decide which companies within the group that they may then wish to visit to undertake further audit work. This will involve looking at things like staff turnover, number of employment tribunals, number of whistleblowing calls, training take-up etc. The results of this data analysis help to form a general picture of how well the subsidiary company is operating and being run and if there are any red flags.

Other internal audit functions have created dashboards of live metrics that they monitor on an ongoing basis, based on eight or so key characteristics and sets of data that they have always collected.

Another chief audit executive described how their internal audit function collaborated with the first and second lines to join up a labyrinth of cultural insights from across the organisation. This included data from staff engagement surveys, results of investigations, the speak-up/whistleblowing helpline and customer complaints. Within the internal audit function they had also developed their own database of cultural observations from audits that they undertake.



## Questions for internal audit

- Is the internal audit function using data-analytics to help identify any corporate culture related red flags?
- Has the internal audit function developed a corporate culture dashboard of live metrics to support continuous monitoring?
- If the internal audit function is using data-analytics for its corporate culture work, is it using a broad enough range of data sources, to get a clear picture of any culture/behavioural related issues/red flags?

## Conclusion: spring into action



The Covid-19 pandemic has impacted the corporate culture of organisations in many shapes and forms. This is especially the case for those organisations where large numbers of their workforce have had to work remotely for a protracted period. This has created unique challenges for organisations to promote, embed, and sustain their cultures, and these challenges are likely to remain as many organisations look to move to hybrid working models longer term. There is a real risk of cultural erosion and decay over time, without new measures and processes put in place. Meaning that monitoring, measuring, and assessing the corporate culture has never been more important.

All of this is set against a backdrop of rising regulatory expectations regarding corporate culture. This is particularly the case for the financial services sector, but increasingly all sectors are now facing greater regulatory scrutiny in this area. Internal audit functions in a range of sectors should be prepared to expect regulators to demand far more in relation to corporate culture in the future. This is likely to involve regulators giving more airtime to corporate culture and requesting to review the work of internal audit in this area. Internal audit functions should therefore ensure that they have an open, constructive, and cooperative relationship with regulators in regard to corporate culture.



## Key takeaways

1. Having the right corporate culture, aligned to the organisation's purpose, values, strategy and vision for the future, is of fundamental importance to the success and long-term sustainability of organisations.
2. The corporate culture of an organisation also touches upon and interlinks with a wide range of business-critical risk areas, and from a risk culture perspective, can have a significant impact on the robustness of the risk management and internal control environment.
3. Boards, audit committees, and internal audit should therefore be taking corporate culture, and the risks associated with a weak, poor, or unhealthy culture, seriously.
4. Boards have a critical role to play in articulating, establishing, and embedding the corporate culture, ensuring it cascades down through the organisation. The right tone from the top is vital to achieving this.
5. The role of the chief executive officer is of particular importance in this respect. However, the entire board has a responsibility to ensure that corporate culture is promoted and embedded, as well as monitored, measured, and assessed on a regular basis, including seeking independent assurance.
6. Internal audit's role is to provide assurance that the first and second line business functions have done their jobs properly in regard to embedding, monitoring, and assessing the corporate culture.
7. Internal audit should carry out its own independent work to monitor, measure, and assess the corporate culture, reinforcing the assurance from the first and second lines.
8. Internal audit must adopt a pro-active (not reactive) approach to its work on corporate culture, and not wait for the board or the audit committee to come to you first, before doing something about it.
9. If internal audit functions have concerns about the organisational culture, they must be prepared to use their voice and speak to the board or audit committee. Equally, boards and audit committees should be empowered to seek the support of their internal audit functions in providing independent assurance in regard to the corporate culture.
10. It is important that internal audit functions have the sufficient skills, resources, and capabilities to audit corporate culture and behaviour effectively.
11. Corporate culture audit work should be tackled in the same way as the audit work of other areas of the business and 'culture auditors' should be expected to have a certain level of expertise and knowledge in this area.
12. Internal audit functions should consider whether members of the team need training to audit corporate culture, or whether they would gain value from outside expertise to support their work in this area. For example, many of the most mature internal audit functions have evolved their work in this area by employing dedicated organisational psychologists or behavioural risk specialists.

Internal audit functions should be mindful that corporate culture is not a standalone risk that should be tackled in a silo but has a significant impact on a vast array of other business-critical risks. Many of these risks can also have a big impact on the corporate culture itself. The most obvious one is human resources, talent management, recruitment, and retention risk. However, there are also strong interlinkages with equality, diversity, and inclusion risk; and health, safety, and well-being risk. When planning an audit of another business-critical risk area, internal audit should always consider whether there

would be value in examining the potential impacts these risks could be having on the overall organisational culture, and vice versa.

With a renewed focus on organisational culture only likely to grow in the years ahead, we urge more internal audit functions to now step up and play their part in monitoring, assessing, and providing independent assurance in this space. If they haven't done so already the first step should be having a conversation with the audit committee chair about the risks associated with corporate culture.



# Closing reflections: from the London Business School Leadership Institute



**Congratulations to the Chartered IIA for crafting a report that will help the leaders of organisations across the spectrum deepen their knowledge of the importance and impact of organisational culture. This report will help organisations define, think about, cultivate, and measure culture, as well as help to facilitate and accelerate action and understanding of how this can be done.**

We welcome the Chartered IIA's contribution to this important conversation by showcasing and drawing on a mix of research methods (case studies, surveys, empirical and longitudinal studies) to inform and support their conclusions. Not only does this research pose some impressive, interesting, and critical questions, but the analysis will undoubtedly facilitate learning. By also including some engaging and interesting case studies on culture measurement and cultivation, the Chartered IIA helps the reader to learn by seeing the activities and processes that have been used by well-known organisations to measure, promote, cultivate, and execute healthy cultures.

## Why culture matters

The Chartered IIA contribution to culture matters because the past decade has demonstrated over and over the critical role that culture plays in the face of unexpected change. When Covid-19 required organisations to completely shift how they operate and deliver services, for example, it highlighted once again the importance of strong culture to guide the organisation when existing processes and lines of authority are challenged.

When change happens, we can see how ineffective leadership can lead to the erosion of the factors that contribute to a healthy culture such as psychological safety, ethical behaviour, and appropriate employee engagement and management processes. Culture audits can spot early how mindset, behaviours, biases, judgements, and critical thinking (or a lack thereof) might be having a negative impact on organisational culture.

Now, more than ever, as the world moves towards a new state of operation, there is a window of opportunity for organisations to reflect on what “Culture 2.0” needs to look, feel, and operate like—especially given hybrid and remote working appears to be here to stay. In our view, this will involve rebuilding and re-defining what a healthy and vibrant culture should look like in that new world.

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*Now, more than ever, as the world moves towards a new state of operation, there is a window of opportunity for organisations to reflect on what “Culture 2.0” needs to look, feel, and operate like.*

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## The role of internal audit professionals in managing culture

We applaud the evidence demonstrating that internal audit functions are working with other functions in their organisations to tackle the measurement and cultivation of organisational culture in a collaborative, multi-functional way. We hope this collaborative process continues to be led by internal audit, but also works to facilitate true, equitable collaboration on this type of effort to feel like it is owned and led by all parties involved.

That collective sense of ownership of culture is critical for success to understand that organisations are more like “ecosystems” than “machines”, and that culture cultivation is a process and practice that needs to take place consistently, mindfully, and regularly, over time. We are encouraged to see that the results of this survey demonstrate a clear understanding of this principle, along with seeing the cultivation process as “systemic” – acknowledging that healthy cultures need multiple elements to be cultivated (processes, systems, values, mindsets, leadership, and management practices, to name a few).

### **Vyla Rollins**

Executive Director  
London Business School Leadership Institute

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*...audit professionals need to be engaged with the board on monitoring organisational culture.*

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Importantly, audit professionals demonstrate here their understanding that boards of directors, executive and non-executives alike, are ultimately responsible for the cultivation of healthy, strategically anchored cultures and that audit professionals need to be engaged with the board on monitoring organisational culture. For that reason, we hope that the results of this survey will continue to encourage the Chartered IIA to develop their profession-changing culture efforts. Internal auditors will need to work even more effectively and efficiently with the board and other organisation functions in the measurement, monitoring, and cultivation of organisational culture moving forward.

### **Professor Randall S. Peterson**

Academic Director  
London Business School Leadership Institute

Case study:

## Department of Public Expenditure and Reform, Government of Ireland 'Culture Review'



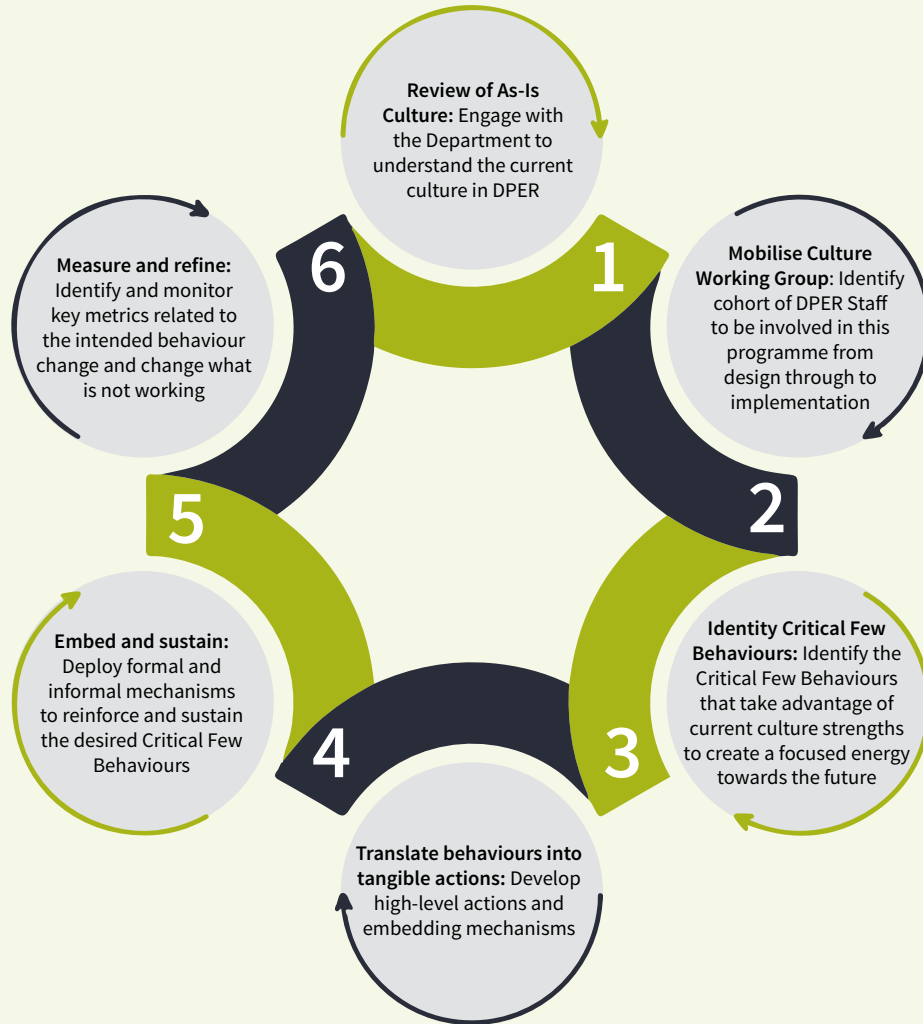
The Government of Ireland's Department of Public Expenditure and Reform (DPER) aims to be the best in class and a strong corporate culture is key to achieving this. To achieve their corporate goals, they recognise that ensuring that the corporate culture of the department is a positive one is an essential enabler of how the department works. The culture of the organisation was generally regarded as being strong already. However, to help build on this, Internal Audit, in partnership with the Human Resources Strategy Unit, undertook a standalone and holistic culture review as part of their 2020 Internal Audit Plan. This review aimed to gain insight into staff and external stakeholder perspectives on what it is like to work in, and with, the department, with the view of building on the existing strengths and identifying areas for improvement.

To lead and support the culture review, an internal project review team was established which consisted of members of the internal audit function and the human resources unit. A steering group was also established consisting of both internal and external members to help oversee the work. A professional services firm was appointed to provide subject matter expertise and independent oversight over the process.

The review defined culture as the "self-sustaining pattern of behaviour that determines how things are done". Because organisational cultures change slowly over time, the approach focussed on firstly understanding the current culture. By identifying the 'cultural traits' of the organisation, the review team identified a small number of key behaviours, known as the 'critical few behaviours', which align to DPER's strategic ambition and values and will help the department to evolve. By focussing on a small number of critical behaviours, the review team believe they can help ensure every person within the department can take action and contribute to a positive culture.

Below is a diagram that illustrates the approach the review team took to carry out the culture review and the specific steps taken.

## Approach to culture review



The culture review started in January 2020 with analysis of the ‘As-Is’ or current culture of the department. This involved undertaking a wide-ranging quantitative ‘Dive into culture survey’ supplemented with focus group discussions with staff, as well as interviews with external stakeholders.

Because of the onset of the Covid-19 pandemic, the work had to be paused in March 2020, but restarted again in January 2021. This provided a useful opportunity to reassess the effect, if any, of the pandemic on the cultural traits of DPER and consider how the culture had responded. From February 2021 onwards the identification of the critical behaviours took place, this included working with the Management Board in co-designing the key actions to embed the behaviours.

The ‘Critical Few Behaviours’ identified were:

- Seek opportunities to innovate and collaborate with colleagues
- Take pride in delivering on our goals and objectives
- Treat others with respect and value all contributions
- Speak up and welcome challenge

The identification of the behaviours was chosen to align with the department’s strategic ambitions and values, as well as build on the strengths and mitigate the challenges of the current culture, to help accelerate the delivery of the department’s strategy.

Having identified the Critical Few Behaviours, the focus going forwards has been to embed and role model these behaviours across the department.



## Case study:

# Lloyds Banking Group's approach to influencing culture and behaviours



Lloyds Banking Group's internal audit function is evolving its approach to assessing and providing insights on corporate culture and behaviour.

Their work on risk culture, and the wider organisational culture, stems from the Chartered Institute of Internal Auditors 'Internal Audit Financial Services Code of Practice' that was first published in 2013. The Code states that: "Internal audit should include within its scope the risk and control culture of the organisation. This should include assessing whether the processes (e.g. appraisal and remuneration), actions (e.g. decision making), 'tone from the top' and observed behaviours across the organisation are in line with the espoused values, ethics, risk appetite and policies of the organisation".

In accordance with the Code's guidance and to support the leadership to learn from the observations, it was crucial to share insights into behavioural patterns that are helping improve as well as those that are inhibiting effective risk management and control. To do this, they use the Financial Services Culture Board (FSCB) framework of the nine characteristics of effective culture (see chapter 13).

They initiated a culture programme within internal audit which encouraged auditors to adopt a mindset where culture is assessed as a tangible risk management asset. To enable internal audit colleagues to be confident and credible in gathering culture observations and discussing these with their stakeholders an extensive training and support programme was put in place.

Throughout the audit process, audit teams capture both helpful and inhibiting observations relating to Competence, Reliability, Responsiveness, Personal/Organisational Resilience, Accountability, Openness, Respect, Honesty, and Shared Purpose. The audit

team will discuss and agree all their gathered observations which is then saved in a culture workpaper within their audit tool on each individual audit file.

They will also gather information relating to leadership styles and tone from the top, how teams talk about the customer, what pressures the business is under and what is important for the teams and the business to get right.

The internal audit culture team collates and analyses all the data captured in the culture work papers to produce Culture Insight Reports. The Culture Insight Reports are produced on a six-monthly basis at a divisional level as well as at Group level.

The Culture Insights Reports are shared with relevant executive committees and audit committee to discuss internal audit insight and trends with key divisional and Group stakeholders. The reports do not contain actions, they contain recommendations for stakeholder consideration alongside other culture information from across the Group.

The internal audit culture team works with the Group culture team and divisional culture leads from both the first and second lines of business functions to join up cultural insights from across the organisation. This will include colleague engagement surveys, Financial Services Culture Board surveys, culture scope behavioural insights, divisional and group culture plans along with other data sources e.g., conduct investigation data, speak-up/whistleblowing, material events, and customer complaints.

The internal audit function can also capture behavioural observations through business monitoring from stakeholder meetings, and governance and committee meetings. They can use the information to include in the Culture Insights Reports.

## Appendix and useful resources

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1. UK Corporate Governance Code 2018, Financial Reporting Council, July 2018
  2. Creating Positive Culture, Financial Reporting Council, December 2021
  3. Auditing Risk Culture: A practical guide, The Institute of Internal Auditors Australia, July 2021
  4. Managing Culture: A good practice guide, The Institute of Internal Auditors Australia, December 2017
  5. Risk Culture Guide, Victorian Managed Insurance Authority, State of Victoria, July 2021
  6. Annual Review of Corporate Governance Reporting, Financial Reporting Council, November 2021
  7. An outcome-based approach to assessing organisational culture, The Financial Services Culture Board, January 2018
  8. IRM Risk Culture Framework, Institute of Risk Management, 2012
  9. Organisational Culture (technical guidance), Chartered Institute of Internal Auditors UK and Ireland, September 2020 (membership subscription required)
  10. Making culture part of your audit DNA (technical guidance), Chartered Institute of Internal Auditors UK and Ireland, September 2020 (membership subscription required)
  11. Auditing Culture – A Hard Look at the Soft Stuff, Global IIA, February 2016
  12. Time to rethink your company culture, London Business School, February 2021
  13. Boards Need To Get Serious About Managing Organizational Culture, London Business School, December 2019
  14. Looking in the Mirror: What About Internal Audit's Own Culture?, Internal Audit 360, February 2022
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## About the Chartered Institute of Internal Auditors

The Chartered Institute of Internal Auditors is the only professional body dedicated exclusively to training, supporting and representing internal auditors in the UK and Ireland.

We have 10,000 members in all sectors of the economy.

First established in 1948, we obtained our Royal Charter in 2010. Over 2,000 members are Chartered Internal Auditors and have earned the designation CMIIA. About 1,000 of our members hold the position of head of internal audit and the majority of FTSE 100 companies are represented among our membership.

Members are part of a global network of 200,000 members in 170 countries, all working to the same International Standards and Code of Ethics.

### Stay connected



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