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Challenges and Consequences

The complexities of governing even a relatively small institution in the modern world are immense, and it is frighteningly easy for an organisation to go downhill quickly if standards of governance slip. The case of Ardwick Green shows how it can happen.¹

Ardwick Green

Ardwick Green is a Manchester-based charity providing grief counselling services to children who have recently lost a relative, especially in circumstances such as illness or suicide, or who have been victims of domestic abuse. It has a special focus on children living in deprived areas in Greater Manchester. As such, it provides vital service that cannot be easily replicated. Both the NHS and education system provide child mental health services, but these are heavily overstretched and oversubscribed. The charity has a staff of about twenty-five people.

In 2011, Ardwick Green underwent significant financial difficulties caused in part by a reduction in sources of funding. The board at the time was made up of contacts of the CEO of the charity. The independent directors were all very caring people and passionate about the services provided by the charity.

However, they were slow to recognise the challenges facing the organisation. This was due in part to a lack of understanding and challenge of the financial information being provided to them, in part to and a lack of involvement with the organisation outside of board meetings, meaning the directors were not fully engaged with the organisation and did not really know what
was going on inside it. The result was an overspend in the financial year and a reduction in reserves to below £20,000. The situation was sufficiently grave that the vital services provided by the charity were under immediate threat.

In order to address the issues, a new CEO was put in place and new board members were recruited. Two of the trustees from the original board also continued in their role on the new board; it was deemed important that at least some people with experience of the organisation were retained. In order to identify the skills required on the new board, a skills review was undertaken across the board and the entire organisation. Trustees from appropriate backgrounds were recruited in to address gaps in areas such as business development, HR and marketing. The new trustees were also recruited from a variety of different sources and were subjected to a rigorous application process. Finally, all trustees were subject to a formal induction process to ensure that they understood their responsibilities and the organisation itself.

The new board contracted a new accounting service with the immediate goal of producing management accounts that were accurate and easier for trustees to understand. The board also recognised the need for much more direct links between the board members and staff to ensure that the board understood what was happening in the organisation on a day-to-day basis.

The new CEO and board reviewed services, funding streams and expenditure. Staff were directly involved and kept informed throughout the process. Despite the fact that wages were frozen and all staff lost essential car allowances as a result of the difficulties, the staff team remained committed to helping the new CEO and board with the review whilst maintaining high professional standards when providing the charity’s services.

Following the review, with the help of a charitable organisation that links business people with charities, the CEO and board established a new mission statement and three-year business plan with strategic objectives. Targeted performance measures were established, and performance was monitored regularly by the board. The new board also identified that more active links with local businesses were needed in order to diversify funding streams, and the chair successfully applied for a grant to fund a business development worker for one year.

The accountant who produces the management accounts now attends every board meeting, and trustees have direct contact with staff members on a regular basis. Each staff team provides reports directly to the board on a regular basis. The board also established a service user panel to ensure that the board was getting direct input from service users when reviewing services and considering future service requirements.
As a result of the changes, the financial resilience of the charity has materially improved and the impact of the work undertaken by the charity (measured using outcome-based methodologies) has materially increased (Fig. 2.1). The case of Ardwick Green shows clearly how board failures can bring an institution to the brink of collapse, but equally, it shows how swift preventive action by a strong board can rescue an institution and put it back on a sound footing. Sadly, this doesn’t always happen. Not every story has a happy ending. As noted in Chap. 1, the list of scandals, failures, disasters and collapses is seemingly endless, and, every time, it is people inside and outside the organisation who suffer the damage.

Rather than compiling a grim list of failures, let us take two examples and look at them in turn. In particular, we should note the role of the board in the failure, and the consequences for people and society.

### The Impact of Failure

In 2008, the Healthcare Commission (an ancestor of today’s Care Quality Commission) investigated the high mortality rate at Stafford Hospital, run by the Mid-Staffordshire NHS Foundation Trust. Exactly how many unnecessary deaths occurred during the period 2005–08 is still a matter of dispute, but some press reports put the figure as high as 1200. The chairman of the Trust, Toni Brisby, resigned and the chief executive was suspended and ultimately left his post. A subsequent public inquiry in 2013 made the point that the Trust’s independent directors (known in this case as governors) had failed
in their duties during the period when the deaths occurred. It is worth quoting from the report at length (the italics are ours, for emphasis).

The governors of a FT [Foundation Trust] theoretically play an important role in its oversight. Their power to dismiss the chair and non-executive directors potentially gives them considerable scope to influence the running of the organisation. It is clear from the experience of the Trust’s governors, and from meetings the Inquiry had with governors at a number of other FTs of varying sizes that, in practice, there are numerous challenges facing them:

Weakness of mandate: Apart from any governors nominated by local representative bodies, an FT’s public governors are elected by a membership which is grouped into constituencies in a variety of ways. The membership is by definition a self-selecting group and is not necessarily representative of the community from which it is drawn… While this may be inevitable under this type of structure, and has value in enabling local conditions and needs to be recognised, it is important that governors are accountable not just to the immediate membership but to the public at large…

Potential lack of authority and experience: Governors are a disparate group from a wide variety of backgrounds. While they are a valuable source of information about local views, they are unlikely to be able to assess fully the competence of the board or effectively monitor its performance unless they have adequate support, for which they are currently almost entirely dependent on the board itself. Pursuant to the obligation of FTs to provide appropriate training, steps need to be taken to enhance governors’ independence and ability to bring to light and challenge deficiencies in the services provided by FTs….

There appears to be a lack of clarity and consistency around what the governors’ role is and how it is to be performed. The Inquiry has encountered a wide range of practice, from a role not far removed from a hospital visitor, to something almost approaching the challenge expected to be undertaken by non-executive directors. Much seems to depend on the leadership given by the organisations’ chairs and chief executives.²

In other words, the scandal happened in part, the report says, because the governors were not able to adequately carry out their duties and had no idea of what was going on inside the organisation for which they were responsible.

The second example is the charity Kids Company, which ceased operations in 2015. Kids Company derived most of its funding from the Department for Education. Civil servants began to express concern over how the charity was spending the grant money it received, and rumours also began to circulate about sexual misconduct in the charity’s offices. Although the allegations were never proven, they caused a loss of fundraising revenue from other sources and increased the financial pressure. The DfE then decided to pull the plug,
and in 2015 the grant was withdrawn. It then emerged that the charity had no financial reserves and was on the verge of collapse. The government agreed to provide a tranche of emergency funding on the condition that both the founder and CEO, Camilla Batmangelidjh, and the chairman, Alan Yentob, stepped down. Kids Company was then wound up.

The parliamentary commission of inquiry into Kids Company had harsh words for its trustees, its independent directors. Had they done their duty, the charity would have managed its finances in a prudent manner, accumulating reserves and spending its grant responsibly. Again, it is worth quoting the commission’s report at length (again, the italics are ours).

*Primary responsibility for Kids Company’s collapse rests with the charity’s Trustees.* Whether these allegations prove true or malicious, if the Trustees had not allowed the charity’s weak financial position to persist for so long, Kids Company would not have been so vulnerable to the impact of the allegations. The Board failed to protect the interests of the charity and its beneficiaries, despite its statutory responsibility to do so. Trustees repeatedly ignored auditors’ clear warnings about Kids Company’s precarious finances. This negligent financial management rendered the charity incapable of surviving any variance in its funding stream; when allegations of sexual misconduct emerged in July 2015 and threatened to impede fundraising, the charity was obliged to close immediately.

The Charity Commission’s guidance requires Trustees to ‘make decisions solely in the charity’s interests, so they shouldn’t allow their judgement to be swayed by personal prejudices or dominant personalities’. *Kids Company’s Board of Trustees lacked the experience* of youth services or psychotherapy necessary to interrogate the decisions of the Founder-Chief Executive. *This approach left the Trustees unable to defend the reputation of Kids Company and thus to discharge a prime obligation of the good governance and leadership of any organisation.* It is essential that Trustees of all charities ensure that some members of the Board have experience of the area relevant to the charity’s activities, in addition to the necessary skills, and that *all Trustees have the appropriate attitude towards responsible governance.*

The collapse of Kids Company, like so many other scandals in public, private and third sectors, was eminently avoidable. But the board lacked the experience and knowledge to do their job, and were in effect not competent to govern the charity. To put it another way, they lacked the knowledge to be independent thinkers and ask the questions that needed to be asked about how the charity was being run. Without good governance, without proper oversight and scrutiny, the defects in management at Kids Company went undetected and the charity’s collapse became inevitable.
The impacts of both these cases were considerable. The death toll at Stafford Hospital was appalling; twelve hundred lives lost, twelve hundred grieving families left to wonder what had happened and why. The reputation of the NHS itself was severely tarnished. The failure of Kids Company put employees out of work and meant that children who depended on the charity were left unsupported. Each case was a tragedy. But perhaps the most appalling thing of all is that these tragedies were created by human incompetence.

The first step to resolving the crisis of governance is to understand clearly the challenges institutions face and be realistic about their problems. Too many organisations fail, or come to the brink of failure, because through either ignorance or wilful blindness, independent directors put their heads in the sand and fail to see what is really going on around them. We need to be clear about the problems we face.

And, as we have already said, the challenges of governance are complex and difficult, and the pressures on independent directors are increasing. Some of the problems they face are generic. In the course of our research, many of the same issues cropped up over and over again in every sector: lack of resources, strategic challenges, coping with uncertainty and managing relationships with the executive team came up time after time. But every sector also has its own particular challenges, depending on the nature of the activity in which organisations engage, the risks they face and levels of resources.

Specific Governance Challenges by Sector

Business

Business is of course a very broad category indeed, and encompasses everything from small and medium-sized enterprises (SMEs) to global giants, but all face similar problems and challenges in governance.

In the corporate world generally, there are two types of risk: business risk, which will only affect the company itself, and industry risk, or risks faced by the entire sector. Business risks include issues such as:

- loss of key clients or contracts
- getting pricing strategy wrong and losing sales and profits
- failure of quality control systems
- failure of financial or information systems and data breaches
• loss of key personnel, either members of the management team or technical staff whose skills will be difficult and expensive to replace
• changes to organisation and restructuring, which can produce uncertainty be damaging to culture and morale
• the challenge of meeting customer expectations, especially when those expectations are prone to fluctuation and change

And finally, there is the age-old problem of corruption and malfeasance by employees or other stakeholders.

Industry risks include issues such as the continuing impact of globalisation and how it is changing the landscape of many industries. Retailing, for example, has been transformed by the rise of online platforms such as Amazon and Alibaba. The impact on high street retailing has been massive, and that impact is now beginning to spread to shopping malls. Coupled with globalisation, technological changes can render a company’s existing products or services obsolete, or at least provided competition from unexpected directions, as Uber and Airbnb have done in the taxi and hotel markets.

Geopolitical events can affect companies in other ways. We have already mentioned Brexit, but in addition there are issues such as the introduction or reduction of trade barriers; some parts of the world are negotiating free trade deals, while others are erecting protective walls. At time of writing, a proposed free trade deal between the European Union and the South American trading block Mercosur is under threat thanks to Brazil’s failure to deal with the problem of deforestation in the Amazon, which could have an impact on the global climate. Fluctuations in exchange rates, which are often linked to political events, can cost a company heavily if it is trading or sourcing material and components from overseas. Changes in law and regulation can restrict the company’s activities or force it to develop new strategies for compliance. And finally, of course, there is always the threat of competition.

Despite the SARS outbreak in 2003 and despite repeated warnings from the World Health Organization and other scientific bodies, the risk of a global pandemic had pretty much disappeared off the radar screens of most companies. Despite the obvious risks to the health of employees and to global supply chains—and, as it turned out, to the ability of many businesses to stay open at all—most firms ignored the issue and very few had a disaster plan in place to cope. Having been caught flat-footed by the rapid spread of the pandemic, many businesses argued that this was a ‘black swan’ event that they could not have been prepared for. In fact, like most so-called black swan events, the pandemic had long been foretold, but businesses preferred to think of plagues
as something that belonged to history, impossible in the modern day. This particular form of wilful blindness has come back to haunt them.

How these risks present themselves depends on the company, its size, its products and services, and its customer base. No company is immune to them, and no independent director is immune either. One of the most high-profile casualties of recent years was Sir Richard Broadbent, chairman of the board of Tesco, who was forced to resign in 2014 after a financial accounting scandal which saw a £420 million black hole open up in the company’s accounts and several executives facing criminal charges. The Tesco case is reminiscent of the fall of Dutch supermarket group Royal Ahold, which had expanded rapidly in the late 1990s. Accounting ‘irregularities’ at several of its overseas subsidiaries caused the company’s collapse in 2003.

Royal Ahold is an example of a board that failed to exercise oversight. The CEO, Cees van der Hoeven, was given a free hand to do whatever he wished, and the board merely nodded along. The collapse of Lehman Brothers in 2008 was another case of the board failing to scrutinise the actions of the chief executive, Richard Fuld; famously, only two of the independent directors on Lehman’s board had previous banking experience.

Too often, independent directors remain silent when they should speak. A study by management consultants McKinsey & Company found that more than 60% of non-executive directors make no comment on corporate strategy papers and simply nod them through. The same study also found a strong link between board engagement and corporate performance; that is, companies where the board had a culture of scrutiny and challenge by independent directors tended to show superior financial results. Sometimes directors see the problems but feel constraints and are unwilling to speak up; sometimes they come under pressure from shareholders and feel unable to resist (indicating they are not sufficiently independent; and sometimes, as in the cases of Tesco, Royal Ahold and Lehman Brothers, the board seemed to have no idea what was going on.

When boards fail to meet the challenges they face, the consequences can be severe. Corporate scandals and collapses destroy value on a massive scale. They reduce shareholder value, which in turn has knock-on effects such as reducing the income flowing into pension funds, and this in turn has downstream consequences for pensioners, now and in the future. In the aftermath of the Deepwater Horizon disaster in 2010 and the ensuing oil spill in the Gulf of Mexico, there were concerns that BP might collapse under the weight of costs to clean up the spill and fines imposed by the US government. Had this happened, British pensioners could have been in serious trouble. Every major
pension fund was invested in BP, and some funds may not have survived the loss of these large investments.

One of the myths about business failures is that the only people who suffer are fat-cat shareholders. Nothing could be further from the truth. Corporate breakdowns cost all of us. When companies collapse, they stop paying taxes, meaning government has less revenue to spend on vital social services, health services, defence and policing and so on. Society as a whole becomes less secure. Collapses also cost us directly, too. The UK government spent £45 billion to bail out Royal Bank of Scotland in 2008, and taxpayers are still paying for this.

Failures also lead to job losses, sometimes on a very large scale. The Retail Gazette estimates that 164,100 retail jobs will have been lost by the end of 2019, while another report predicts a staggering 900,000 retail job losses by 2025. Some of the people who lose their jobs will find work in other sectors; many may not. When jobs are lost, families lose their income, meaning they may be unable to pay mortgages or rent, or even put food on the table. Children may find their educational prospects are stunted and they can no longer get into the university of their choice, or even go to university at all. Futures are lost, hopes and dreams die, and families are condemned to poverty. The consequences could have been mitigated, if only the directors had done their job and governed the company well.

Charities

We have already touched on some of the challenges facing the charities sector. The competition for resources continues to dominate the thinking of many charity boards and managers. Overall giving by individuals in the UK rose slightly last year, but the Charities Aid Foundation warns that fewer people are making donations; those that do donate are giving more, but this well may eventually run dry. Many charities are heavily reliant on contract income from other sources, usually government or from grants by foundations. The latter have also increased in value, but at the same time the demand for income has increased even faster, in part because of severe cuts to local government funding over the past decade.

Charities also have to guard their reputations closely. The public hold charities to a higher standard of account than businesses, and expect them to be cleaner than clean. The Oxfam scandal in 2018 damaged many other unrelated charities as well, and may be one of the reasons why fewer people are now making donations. As for Oxfam itself, the decline in donations hurt
not only the charity but, by extension, the people in developing countries who desperately need its services. Oxfam’s ability to carry out its mission has been impaired.

Charities also struggle to attract staff and volunteers. Low wages are an issue for a former, finding time in their already pressured lives deters the latter. And the inability to attract high-calibre staff means charities are often lacking in vital areas such digital skills—at a time when digital delivery is becoming increasingly important—and professional, competent management.

All of these things mean that charities are struggling to meet the challenges that face them, at a time when their services have never been more badly needed. Overstretched and underfunded, local authorities and the health service are increasingly relying on charities to deliver services for them, from nurses and care coordinators funded by the Heart Foundation to charities taking over local libraries. If charities collapse, then many of the services on which society depends could collapse with them. We saw above, with the cases of Ardwick Green and Kids Company, how damaging these collapses can be.

Are charity boards up to the challenge? Our research suggests that many charity trustees are pessimistic. Only 74% of trustees we surveyed rated their own organisation as good or excellent for board competence; over 20% were concerned that there was no effective overall strategy, and 33% believed the board was risk averse. Over 20% felt that there was no long-term strategy. Among the failings we found were lack of evaluation or monitoring of board performance, lack of data with which to analyse performance, and lack of commercial acumen and experience on the part of board members, meaning they were unable to act as effective independent advisors.

Higher Education

As noted, the introduction of tuition fees in the UK has put universities under pressure to deliver value for money and provide high-quality education. With fees at £9250 per annum and living expenses to pay on top of this, many students will end up with a debt of £50,000 or more by the time they finish their
undergraduate degree. Unsurprisingly, they want something for their money, and are becoming more vocal about asking for it.

The Augar Review, which recommended a reduction in fees to £7250, sent shockwaves through university councils. Twenty per cent of universities already face financial difficulties, and if the Augar Review’s proposals are accepted, the financial pressures will increase considerably. Brexit also poses an unquantifiable threat to research funding—most universities derived at least some of their research funding from EU programmes—and research staff, especially if UK governments continue the policy of restricting free movement from Europe.

Pensions are another major challenge for universities. The Universities Superannuation Scheme, the pension fund for academic staff, is badly under-funded with a deficit of £6 billion and proposed changes to the pension scheme have been poorly handled; in 2018, more than 42,000 academic staff went on strike to protest the changes. Further strikes followed in 2019.

Research funding is another critical issue; there are fewer sources for funding than formerly, and much of this funding is being invested in a handful of elite universities, leaving the rest to go begging. More generally, we found that university councils lack the capacity to cope with change, that they lack international focus at a time when international competition in higher education is increasing, and that they are not adjusting to the challenges of the digital world.

Now, the cracks are beginning to show. Many universities are declining in the world rankings, meaning they will find it harder to recruit foreign students. Some UK universities are already struggling, and some have already been forced to merge. More mergers may well follow in the next few years, and outright failure or collapse of some struggling institutions is a distinct possibility. Cost cuts mean there is a threat to the quality of education that students receive, and also to the support that vulnerable students—for example, those with disabilities or struggling with mental health—receive while they are on campus. The purpose of higher education is to allow people to develop and realise their full potential, and to make a contribution to society. Failure to deliver high-quality education to those who want it is a broken promise, not only to students but to society itself.

Yet, despite the formidable challenges faced by universities, we found a remarkable degree of complacency on the part of independent directors. Too often, university councils appear to be in denial about the problems they face, or simply do not recognise that the problems exist. There is a worrying lack of engagement. Most councils meet six times or fewer per year, and most meetings last no more than three hours. Eighty-two per cent of council members
spend twenty days or fewer per year attending to their duties. Thirty-five per cent currently have no other independent director role, meaning they lack experience of the post. Forty-two per cent never visit faculties or colleges of their university to meet staff and students. Too many council members are not engaging with their organisations, and as with businesses, this is bound to have an effect on board performance.

In part, as one interviewee commented, this may be down to the culture of universities themselves. University councils tend to be large, as they are required to represent a wide range of stakeholders including staff, students, the university senate and so on, and this can make them unwieldy. The majority of council members are part of the university. ‘That creates a culture of stewardship, a culture of “we’re all in it together”, and that can be very good’, the interviewee said. On the other hand, independent members of the council can easily get drawn into that culture and lose their independence.

Some council members did express concerns. We found that over 35% thought their council was risk averse, and 25% felt they lacked enough data to adequately monitor performance. Another 28% believed that the views of the independent directors are not aligned with those of the vice-chancellor.

Other concerns expressed included lack of shared vision and purpose, lack of an effective chair, not enough attention to strategy, insufficient adherence to codes of governance and lack of opportunities to challenge the vice-chancellor and his objectives. Ten per cent doubted whether the contributions they made at council meetings were effective. And yet, council members themselves seem to take a remarkably *laissez-faire* approach to their role.

| Key Challenges in Higher Education |
|------------------------------------|
| Providing value for money and maintaining quality |
| Capability to cope with the pace of change |
| The Augar Review and the prospect of reduced student fees |
| Pension fund deficits |
| Concentration of research funding in a small number of universities |
| Student loan book |
| Lack of international focus |
| Adapting to a digital world |
| Loss of overseas students, especially from East Asia, in the aftermath of the pandemic |

**Health Care**

As we noted in the previous chapter, the very broad mandate of the NHS makes governance difficult, to say the least. More than 20% of the trustees we surveyed said they believed effective governance was impossible. It is not only
the vast size of the NHS itself that complicates governance, but the complexity within it. Individual NHS Trusts can employ up to 20,000 people across multiple sites with income of more than £1 billion, but that is only the beginning. As our interviewees explained, delivering health care in any given locality involves interaction between GPs and several different trusts including perhaps an ambulance trust, a hospital trust, a community health trust and a mental health trust, as well as local authorities and other stakeholders who are not part of the NHS. ‘There is a particular governance challenge in overseeing a set of activities that are very dependent on other institutions and other public services over which you have no control’, said one.

Other interviewees spoke of constant interference in the workings of the board by outside agencies including regulators such as NHS Improvement, the Department for Health and even cabinet ministers. One former chair reported that regulators had insisted on controlling some appointments to the board, and described how a minister of state intervened to insist the Trust purchase specific kinds of equipment. NHS Improvement had also insisted the board establish more committees, adding significantly to the workload of overworked and underpaid independent directors.

Government funding for the NHS has increased, but the demands on the service have increased still faster, thanks in part to an ageing population with more complex health care needs. Much progress has been made in fighting illnesses such as heart disease and some forms of cancer, but in their place have come ‘new’ diseases such as obesity and dementia.

Although preventive health could play a much larger role in combating lifestyle diseases like obesity, in practice the NHS has little alternative but to commit the bulk of its resources to treatment rather than prevention and research. The squeeze on resources means that care quality is sometimes endangered. A culture of targets enforced by government has also changed the nature of health care delivery, not always in positive ways.

Staffing issues are also becoming an increasing problem. There is a chronic shortage of GPs in many parts of the UK, and also a shortage of nurses; the latter has been exacerbated by the difficulty in recruiting nurses from overseas following the Brexit referendum. According to *The Times*, one in ten diagnostic posts in cancer treatment is vacant, and staff are also having to make do with outdated equipment; as a result, cancer survival rates are lower than in most other developed countries.¹² Brexit has also contributed to staff shortages in care homes, and more generally there is an acute shortage of care home beds with many private providers struggling to survive financially. Funding by local authorities has reduced by 50% over the past ten years due to central government cuts in expenditure. All this, of course, is happening at a time
when a rising population of elderly people is putting more and more strain on the care system. According to Age UK the number of older people who do not have access to the care and support they need is now over 1.4 million. There have been a number of inquiries and reports, but so far the government has failed to come forward with a plan for social care, despite the fact that the predicted social care funding gap by 2025 is £3.56 billion.

Past lack of investment in the NHS is also coming home to roost. Respondents to our research programme speak of problems such as deteriorations in the fabric and infrastructure of hospitals, and failure to invest in new technologies. These problems, along with staff shortages, are contributing to a deteriorating quality of service generally. Long waiting lists and frequent cancellations for many hospital procedures are evidence that many NHS Trusts are failing to cope with patient demand. Data from the Estates Returns Information Collection (ERIC) in 2018–19 shows that there is a backlog of maintenance in NHS Trusts of £6.5 billion, of which £3.4 billion represents issues that are ‘high risk to patients and staff’. Even attempts to modernise and improve service are running into problems. In 2018 the North West London Clinical Commissioning Group (CCG) came under fire for spending £66 million on fees to management consultants, who providing a modernisation plan which would cost £1.3 billion to implement, at a time when the CCG already had a large deficit.13

Our survey found high levels of pessimism amongst trustees. Over 40% felt that government influence over how NHS Trusts are managed was very strong, and the clear inference is that they felt this interference was hampering board effectiveness. Perhaps related to this, 76% felt their boards were too focused on short-term pressures, and 30% felt their board was insufficiently innovative. We found that 30% felt their board was risk averse.

We also found evidence of a real lack of engagement in some trusts. Forty per cent of those we surveyed failed to bring access to their own networks and resources to the board, and 48% failed to engage in relationship-building activities which might link the trusts more closely with its stakeholders and the outside world; 18% lacked commercial experience or acumen. Thirty per cent stated that when the organisation runs into difficulties, they do not step forward to help. Surprisingly, 10% said they felt unable to make an effective contribution to the board. We suspect the real figure may be far higher, and once again, this lack of engagement can only be damaging to the performance of the NHS. We strongly suspect that we have seen some of the consequences of this lack of engagement during the pandemic crisis, particularly around
issues like lack of equipment and PPE. When the crisis is over, an inquest into these issues will be necessary, and that inquest must extend to include the role of boards.

Key Challenges in Health Care

- Too broad a mandate for the NHS
- Balancing achieving quality against limited resources
- Ageing population
- Delivering against targets
- Demands of modern-day diseases and lifestyle issues, for example, obesity, dementia
- Coordination with local authority services, for example, care homes for the elderly
- Funding innovation in life sciences

Sport

The picture in sporting bodies is more dismal still. Despite various attempts by governments and other bodies to stimulate a growth in interest in sport among the public, including the ‘legacy’ of the 2012 Olympics, sports governing bodies report a picture similar to that in charities (and many of these organisations are charities) including declining levels of funding, heavy reliance on government funding and lottery grants, and increasing competition between sports for declining levels of resource. Even sports which perform well in terms of competitions or medals won can have their funding capriciously cut.

We referred to some of the problems in sporting organisations in Chap. 1, including the ongoing corruption saga at FIFA, problems around doping in a number of sports and the sexual abuse scandals in youth football. The case of cycling is worth considering in more detail. Allegations of doping among cyclists have been around for a long time, but cycling in the UK seemed to be an exception to the rule. The all-conquering cycling teams at the Beijing and London Olympics and the extraordinary feats of Team Sky, who won the Tour de France with Bradley Wiggins and Chris Frome, seemed to show that cycling was a clean and well-governed sport.

Since then, allegations of poor medical record-keeping have dogged Team Sky, while the UK cycling team has been the subject of repeated allegations of verbal abuse and bullying, especially of disabled and female riders. Cycling remains a popular sport in Britain, but the fallout from these scandals is a real
threat to its future, precisely at a time when more people should be taking up cycling, both for health reasons and to reduce the number of cars on the road.

Serious problems of governance can be found all across the sports sector. Our research found problems with lack of accountability, unclear governance and lack of skills and experience to sort out the mess. The survey results in this sector make for grim reading. Far too many directors and trustees responded to our questions by saying, ‘don’t know’.

In part, according to some interviewees, this is because of a confusion over the nature and purpose of sporting organisations. At times they can be called upon to act like a business, but many, especially the smaller ones, are organised as charities. Some spoke of a lack of diversity, and of board’s recruiting directors ‘who they think will give them a less challenging time’. Some people become directors of sporting organisations because they are passionate about the sport, but that too can compromise independence. ‘If you’re a fan of the sport, you really need to be able to separate yourself from that in order to provide check and challenge’, said one interviewee.

Engagement levels are often poor. Ninety-two per cent of those were surveyed said they had board meetings six times a year or fewer, and 73% reported meetings lasting four hours or fewer. Forty-six per cent devoted less than ten days a year to their role as independent director. Nineteen per cent reported that their board does not have a ‘strategy day’, leaving an open question as to how strategy is made in these boards—is there a formal strategy at all?—and outside experts are rarely invited to board meetings to give advice. Ten per cent of chief executives were reported to have little dialogue with their boards, meaning communication between boards and executive teams in such cases is low, and 14% reported that they do not get enough information to assess performance or make effective decisions.

What makes this worse is that there is clear evidence of a lack of experience for the role, and of trustees and directors being appointed on an ad hoc basis. Sixty-two per cent of respondents had less than three years’ experience in their role, and half had no other similar board position, meaning their experience is limited in the extreme. Only 26% were selected through a formal process conducted by a nominations committee, and 68% reported that they did not think the process of recruitment was extensive. More than 10% had no induction training.
What emerges, then, is a picture of inexperienced and untrained directors making decisions based on inadequate information, without enough discussion or debate to explore the issues thoroughly. Without effective governance, the door is open for scandals to continue to happen.

We could go on; there are clear challenges for governance in many other sectors too, government, further education and the police to name just a few. But the examples given above show the nature of the crisis in governance. On the one hand there are common problems such as lack of engagement by directors, lack of knowledge of how to govern, achieving targets with increasingly limited resources and so on.

But on the other hand, every sector also has its specific challenges. Businesses are—usually—better resourced than organisations in the public and third sectors, but businesses have to deal with a complex and changing business landscape, balancing the need to make a profit with the need to meet the demands of stakeholders. Charities, on the other hand, have to carry out their missions while operating on wafer-thin margins, sometimes unable to attract the best talent because salaries are so low, and always they must jealously guard their reputation, which are often their only real asset. Higher education needs to shake itself out of its rut and realise that here too, the landscape is changing; tuition fees, technological advances and growing international competition all pose a threat. NHS Trusts, locked into the complex mosaic of the medical and social care system, need to rethink how they can best deliver care, for example, concentrating more on preventive medicine and less on treatment. Sport organisation needs to become more professionally managed and, especially, more transparent and better governed if they are to attract more people to participate in sports and avoid further scandals. An understanding of the nature of these specific challenges and the skill and experience to deal with them are among the things every independent director needs.

### Key Challenges in Sports Governance

- Lack of resources
- Dependence on lottery/public funding
- Competition for declining resources
- Lack of accountability
- Unclear governance at lower levels in sport
- Lack of appropriate skills and competencies
- Rebuilding grassroots sports and sports participation in particular after the coronavirus pandemic

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But where do they turn for help? How are they to understand what their duties are and what phrases like ‘independence’ and ‘engaged stewardship’ actually mean? The usual starting point is the codes of governance, which exist in every sector. These codes stress the role of the independent director in ensuring good governance. Increasingly, too, they make directors personally responsible for the organisations they serve. Financial penalties and legal sanctions can now be handed out if directors, governors and trustees are deemed to have failed in their duties. NEDonBoard, the professional organisation of non-executive directors in the UK, summarises the position as follows:

Directors may bring about personal liability, both criminal and civil regarding their omissions or acts in their manner of directing the organisation. Any individual can potentially be fined according to summary conviction and/or be sent to prison for as long as six months. Also, a director may be held negligent where he or she may be personally liable for a certain transaction or business contract concerning an additional third party.14

Thus far, instances of independent directors being punished are fairly few and far between. In the UK, Angela Burns was fined and banned from acting as a non-executive director in 2018 for ‘failing to act with integrity’ at two mutual societies, while overseas, Malaysian regulators banned the directors of Golden PLUS and delisted the company from the stock exchange for accounting irregularities.15 The Charities Commission in the UK has banned a number of people from acting as trustees, usually because of financial irregularities in their personal or professional life, and in 2016 the Commission banned all trustees of the Anatolia People’s Cultural Centre for financial irregularities and suspected links between some members of the organisation and terrorist groups.16

There are other examples of directors being banned, usually where criminality has also been proven, but on the whole the threat of punishment has remained just that, a threat. However, we should not assume this will always continue to be the case. In most countries, governments and the public alike are demanding more accountability from boards. Independent directors who fail to discharge their duties should expect to be sanctioned in some way.

This means in turn that independent directors need to know what is going on inside their organisations, and this is true whether that organisation is a
charity, a university, an NHS Trust or a business. Ignorance is not considered an excuse. In the case of the Anatolia People’s Cultural Centre, the Charities Commission concluded that most of the trustees did not know about either the financial problems or the potential connection with terrorism, and therefore were guilty of neglect. Independent directors often rely heavily—too heavily, we believe—on the executive team to provide them with information. In the previous chapter, we noted complaints by university governors that they do not have sufficient information to do their job. To a large extent, though, the onus is on governors themselves, to make sure they get the information they need and can understand it.

In the final chapter of this book, we argue that the role of the regulator should be reviewed. In particular, regulators should be given greater powers to intervene before disasters happen, not merely step in to clear up the mess and hand out punishments afterwards.

Be that as it may, most codes of governance limit themselves to explaining the purpose of governance and the role of the independent director. We provide two examples here, the Principles of Corporate Governance promulgated by the Financial Reporting Council and reviewed in July 2018, and for contrast, the Principles of Charity Governance issued by the Charities Commission. Other codes tend to look very much the same, with similar structures and principles.

**Principles of Corporate Governance**

*Financial Reporting Council, July 2018*

- A successful company is led by an effective and entrepreneurial board, whose role is to promote the long-term sustainable success of the company, generating value for shareholders and contributing to wider society.
- The board should establish the company’s purpose, values and strategy, and satisfy itself that these and its culture are aligned. All directors must act with integrity, lead by example and promote the desired culture.
- The board should ensure that the necessary resources are in place for the company to meet its objectives and measure performance against them. The board should also establish a framework of prudent and effective controls, which enable risk to be assessed and managed.
- In order for the company to meet its responsibilities to shareholders and stakeholders, the board should ensure effective engagement with, and encourage participation from, these parties.
- The board should ensure that workforce policies and practices are consistent with the company’s values and support its long-term sustainable success. The workforce should be able to raise any matters of concern.
Principles of Charity Governance

Charities Commission of England and Wales, 2018

Principle
The board is clear about the charity's aims and ensures that these are being delivered effectively and sustainably.

Rationale

- Charities exist to fulfil their charitable purposes. Trustees have a responsibility to understand the environment in which the charity is operating and to lead the charity in fulfilling its purposes as effectively as possible with the resources available. To do otherwise would be failing beneficiaries, funders and supporters.
- The board's core role is a focus on strategy, performance and assurance.

Key outcomes

- The board has a shared understanding of and commitment to the charity's purposes and can articulate these clearly.
- The board can demonstrate that the charity is effective in achieving its charitable purposes and agreed outcomes.

Recommended practice

Determining organisational purpose

- The board periodically reviews the organisation’s charitable purposes, and the external environment in which it works, to make sure that the charity and its purposes stay relevant and valid.
- The board leads the development of, and agrees, a strategy that aims to achieve the organisation's charitable purposes and is clear about the desired outputs, outcomes and impacts.

Achieving the purpose

- All trustees can explain the charity's public benefit.
- The board evaluates the charity’s impact by measuring and assessing results, outputs and outcomes.

Analysing the external environment and planning for sustainability

- The board regularly reviews the sustainability of its income sources and business models and their impact on achieving charitable purposes in the short, medium and longer term.
- Trustees consider the benefits and risks of partnership working, merger or dissolution if other organisations are fulfilling similar charitable purposes more effectively and/or if the charity's viability is uncertain.
- The board recognises its broader responsibilities towards communities, stakeholders, wider society and the environment, and acts on them in a manner consistent with the charity's purposes, values and available resources.
To repeat, these codes tell us what the independent director should do, but they do not tell us how to do it. Statements like ‘the board recognises its broader responsibilities’ are useful reminders that boards and directors need to consider all their stakeholders, not just the few that are deemed most important or that make the most noise. But what does that responsibility look like in real life? What is it that boards and directors actually do, in order to govern their organisations well and make a positive impact on society?

**Making Positive Impact**

**Thinking Strategically**

For a start, they need to think more strategically. All independent directors are responsible for the strategic direction of the organisation. They do not implement strategy, but they work with the executive team to decide the organisation’s direction of travel. One of their particular responsibilities is to ensure that the organisation’s strategy is aligned with its stated mission. Indeed, one of our interviewees went so far as to say that this was the board’s primary mission; all other activities were subordinate to that.

This sounds simple, but in the complex and fast-changing world we inhabit, keeping strategy aligned with the mission is seldom easy. Economic uncertainties are everywhere. At time of writing the American and European economies are beginning to slow, and there is concern that another global recession may not be far away. If this happens, private and public spending may be squeezed still further. Consumer demand will lessen, but demand for some key public services may well increase. On top of this, there are new political uncertainties as old trading blocs break down and protectionism is on the increase. Brexit represents a massive political risk for the UK economy and society, but it is not the only one.

And there are other risks that we seldom think about. So fixated are we on economic and political risks that we seldom stop to think about other, more deep-rooted changes that are going on around us. Technology is tearing up the rules of the game. The rise of robotics and artificial intelligence is changing the landscape in which we operate, and the nature of organisations themselves. But how many boards are fully aware of these changes, and have a strategy for dealing with them? The Harvey Nash/LBS report we cited in Chap. 1 suggests that while many companies are indeed aware of the challenges and confronting them head on, there is a long tail of companies that
are engaging with these challenges only a half-hearted fashion, or not at all. Our own research at Henley confirms the same picture in the public and third sectors.

This must change. Independent directors must attempt to understand these trends and the range of possibilities the future could hold. When the organisation’s strategy is no longer fit for purpose, the independent directors must be prepared to say so. They must also be able to argue the case for a new strategy, one that will meet the organisation’s needs, and back up their case with evidence.

**Fiscal Responsibility**

When a corporation or a charity collapses, it is often because it has run out of money. This should not happen, but it does, with alarming regularity.

Scrutinising the organisation’s finances and making sure that money is being used well, effectively and for its proper purpose has always been one of the duties of an independent director. Today, the pressure on finances is increasing in many sectors. Businesses are cutting costs and squeezing budgets, increasing the pressure to do more with less. The financial pressures on the National Health Service will be familiar to anyone who reads the British press. ‘The big debate for most boards’, said one person we interviewed, ‘is whether the financial targets they have been asked to deliver are achievable, and whether the board is able to sign up to them.’

In charities and sports organisations too, we found a common pattern of lack of financial resources, meaning that these organisations struggle to meet their existing remit on a daily basis, let alone expand or take advantage of new opportunities.

Independent directors do not intervene in the running of the organisation, and they do not manage its finances. What they must do, however, is ensure that those resources are used as efficiently as possible. That means supporting the executive team with advice on issues such as financial strategy, but also scrutinising accounts and ensuring money is used wisely and well; and checking for any signs of malfeasance.

Most organisations will have a finance and audit committee as a sub-committee of the board of directors—in many sectors this is a legal requirement—and this committee has front-line responsibility for examining and approving budgets and spending plans. But responsibility does not end there. All independent directors must be aware of the organisation’s financial position and must be prepared to scrutinise the accounts—even if they have
already been approved by the finance committee—and to Questions whether those accounts give a true picture. We cannot stress the importance of this too strongly. Lack of financial literacy and ignorance of financial management on the part of the board has been the downfall of more than one organisation.

People Matter

We are all familiar with the clichéd slogan, ‘people are our greatest asset’. In this case, the cliché is very often true. People determine the culture of the organisation, and culture in turn shapes the leadership’s ability to get things done. A strong enabling culture leads to innovation and quality of service, but a weak or toxic culture can drag any institution down. We can see evidence of weak culture in many organisational failures: Lehman Brothers, Kids Company and Stafford Hospital among them.

Many of the organisations we surveyed cited lack of human resources as being a challenge of equal magnitude to the lack of financial resources. Charities in particular struggle to recruit people with the skills and experience needed to manage in complex environments (they also struggle to recruit trustees with the right skills and experience). Even in the biggest and best-funded charities, salaries tend to be lower than in the private sector, and this is a particular problem when recruiting to senior management positions.

The same problem can be found in health care. One of our interviewees spoke of a hospital he had visited where there was a permanent vacancy rate of 20% among nursing staff. Staff shortages mean increasing pressure on existing staff, forcing them to work longer shifts with potential consequences for the quality of their work. The physical and mental health of staff can suffer as well.

Independent directors who neglect the culture of the organisation and are not aware of the stresses that staff undergo are putting the organisation and themselves at risk. They must be on top of these issues, and they must also consider the changing nature of work itself and how this will impact on their workforce. Much has been written about Generation Z and changing work patterns, and it is quite clear that younger people have different expectations of work, and working hours in particular. Artificial intelligence is threatening to be a game-changer in many sectors. Service delivery in sectors such as health care is increasingly being delivered online, which means organisations need to think differently about whom they employ and what skills they seek.

Here again the challenge for the independent director is to not merely accept the status quo—‘this is how we’ve always done things’—but help the
rest of the board and the executive team to imagine a different future. As work changes, so organisations will change too, and the independent director will play a vital role in making a successful transition to new models and modes of working.

Coaches and Referees

‘I’m not just there to give orders to my chief executive’, said one interviewee, ‘I am there to advise her as well.’ A good board of directors provides specialist skills and expertise in a variety of areas relevant to the organisation’s needs. The composition of the board (which we will discuss more fully later in the book) needs to reflect the particular challenges that face the organisation. These could include areas like digital skills, experience of operating internationally, expertise in sectors such as law, property management, personnel development and training, intellectual property and patents, and many others. Any of these areas of high priority need to be reflected in the composition of the board with independent directors recruited for the experience they bring.

We can take strategy as an example. The executive team is also responsible for strategy, but the executives need the collaboration of independent directors to make strategy work. The executive team often—usually—face considerable short-term pressures and immediate demands on their time. In the words of management guru Henry Mintzberg, they are involved in ‘firefighting’, and have little time to consider the long term. Freed from the pressures of day-to-day management, independent directors can concentrate on the long term and ensure that the organisation has a strong strategy and continues to follow it.

As well as working with the executive team, however, independent directors must also scrutinise their actions and hold them to account, acting simultaneously as coaches and referees. One of our interviewees described a situation in which the executive team were discovered to be concealing evidence of poor performance from the board. Clearly, in this case, the board needed to call the executives out and demand a full and truthful account.

The problem is that boards are often ill-equipped to do so. In particular, they lack diversity. There are no enough directors from different backgrounds or with different mindsets to ensure a diverse range of views and experiences. Too many boards of directors look the same; even worse, too many of them think the same.
Society and Community

In many sectors, private and public, stakeholders have become more active and more vocal. These groups can range from students protesting about tuition fees, to activists demonstrating against fracking or new airport runways, to community groups demanding to have say in local health care provision or protesting against the closure of community hospitals. Groups such as Occupy and Extinction Rebellion have had a huge impact on public opinion, and social media has made it much easier for such groups to organise and become active.

The independent director can also provide a valuable sounding board and conduit for relationships with stakeholders. The challenge for directors is to see both points of view. They are stewards of the organisation and have a duty and responsibility to it, but they also have a duty to stakeholders. When stakeholders come forward with their own agenda, independent directors need to stop and listen, and if they feel that the stakeholders have a point and may be right, or partly right, then they have a moral duty to represent that viewpoint to the board.

This is particularly true of concerns raised by employees, with the Financial Reporting Council’s Code of Corporate Governance advising that companies should have directors with particular responsibility for employee engagement. In some countries such as Germany, employee representation is already built into the corporate governance structure, with employee representatives serving on boards. Here, NHS Foundation Trusts also have staff trustees, and some charities have followed this example.

However, the responsibility of the independent director also extends more widely, to communities and to society itself. Given the financial and operational pressures many organisations face, then can be forgotten. Charities, for example, need to constantly remind themselves that their duty is to serve the community, not perpetuate themselves. Businesses could usefully do the same. Reminding the board and the organisation as a whole that the mission is not about ‘us’ but about ‘them’, the stakeholders we serve, is one of the most important duties of an independent director, and cannot be neglected. Enshrining that point of view in board culture is one of the key components of the idea of ‘engaged stewardship’ (see Chap. 3)
Risk and Reward

We saw earlier how many independent directors believe their boards to be risk-averse. We also saw cases where board took little account of risk or did not understand the risks, and crashed. Perhaps it is the memory of what happened in these cases that makes directors averse to risk, or perhaps it is the fear of sanctions by regulators; either way, this is a real problem. Running an organisation requires a certain level of risk, and too little risk can be just as dangerous as too much.

Different sectors have different perceptions of risk; in the NHS, patient safety is a primary risk, while universities face a significant risk if they fail to provide high-quality education. In the commercial sectors, risk can include things like market risk but also health and safety to both employees and customers.

There is also the issue of risk to reputation. The public tolerance of risk is low, and even a single incident can cause a major scandal, as the sandwich chain Pret a Manger discovered when a mislabelled food item caused the death of a customer. Tolerance for health and safety risk is also declining, with initiatives such as ‘zero harm’ spreading from the steel industry into other sectors as well. Also, new kinds of risk are emerging. The introduction of the General Data Protection Regulation (GDPR) has both highlighted the risks that organisations face when using data, and increased risk levels by ramping up penalties for those that fail to comply or experience data breaches.

Independent directors must scrutinise their organisations closely, partly to protect themselves and their own reputations, but also because they have a duty of care. They are responsible for the organisation, and if things go wrong and harm is done, then blame will be laid squarely at their door. They are responsible for ensuring that their organisation is compliant; to take GDPR again as an example, they must ensure that any data breaches are reported and investigated. More widely, they need to ensure that organisation is managing risks proactively and correctly. They should look at the broader environment and try to identify risks that the organisation might not be aware of, or which it is insufficiently prepared for. Once they have identified these emerging risks, they must bring these to the attention of the board and press for action to be taken.

Another example where risk enters the picture is takeovers and mergers. These are not just a corporate phenomenon; charities and sports organisations merge and acquire each other too, and we have seen several mergers of universities including the University of Manchester and University of Manchester Institute of Science and Technology (UMIST) in 2004, and the more recent merger of the University of Wales with Wales Trinity St David and Swansea Metropolitan University. Here
the challenge for independent directors is to ensure that due diligence is properly carried out and risks assessed.

Sometimes in cases of merger or acquisition, the takeover is the pet project of the CEO and the executive team. They may have staked quite a lot of their own reputation on this project, and are determined to make it happen. But if the independent directors believe the risks are too great, then again, they have a duty to make their views known. Conflict between the executives and the independent directors is always unfortunate, and can be damaging. In such cases, the directors must weigh up whether the damage caused by the conflict will be exceeded or outweighed by allowing an unwise takeover to proceed.

**What Must Be Done**

Who ensures that all these tasks are carried out? Who checks to see whether the organisation has a clear strategy, and the financial and human resources to carry it out? Who is the guardian of the organisation's values and culture? Who understands the risks the organisation faces, and identifies these risks and ensures appropriate action is taken?

The answer in every case is the independent directors, who are the true stewards of the organisation. They must have the experience, the skills and above all the truly independent cast of mind to guide the organisation in the right directions. The task that faces us now—all of us, government, institutions, society—is to ensure that every organisation has these stewards, these independent directors, to watch over them.

In Part II of this book we will talk in more detail about the kinds of skills and experience that are needed in order to make a positive impact. First, though, we will examine the concepts of ‘independence’ and ‘engaged stewardship’. What do these words really mean? As we will show in the next two chapters, they are not rules that can be written down in a code of conduct. They are an attitude, a cast of mind that needs to be cultivated and a culture that must be zealously guarded and protected.

**Notes**

1. Thanks to Nada Kakabadse for contributing this study. Ardwick Green is not the real name of the charity.
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