Corporate Governance

At its core, as I explain later, Corporate Governance is about accountability and values; this means that it is inextricably linked with the management of people. It is your people who:

- Implement the systems, policies, and processes that underpin effective/good corporate governance,
- Monitor the day-to-day operation of those same systems, policies and procedures, and;
- Accept day-to-day accountability for corporate governance in your organisation.

Corporate Governance, or to be more accurate failures in corporate governance, has been much in the news in recent years. Failures at NHS Trusts and on the part of financial institutions are frequently quoted examples of such failures, but we should remember that organisations such as these, unlike Enron, are subject to strict regulation by regulatory bodies such as the Care Quality Commission[1], the Financial Conduct Authority[2] and the Prudential Regulation Authority[3]. This suggests to me that whilst the organisations concerned may well have failed in their corporate governance obligations, so to have the regulators. It also suggests that, in common with corporate values, you cannot simply impose effective corporate governance. You can of course impose the systems and processes and you can also impose legislation and regulation, but unless the principles of good corporate governance and an organisation's values are fully aligned then good corporate governance will never become fully embedded in an organisation.

So what is Corporate Governance? Broadly speaking, it means the processes, relations and systems by which organisations are controlled and directed; corporate governance should not be confused with management. An organisation's governance arrangements must identify the distribution of accountability, rights and responsibilities among the different stakeholders in the organisation. These stakeholders may include, among others, the Board of Directors, managers, Government Departments, shareholders, creditors, auditors and regulators. An organisation's governance structure should include the rules and procedures for making decisions in corporate affairs. Corporate governance includes the processes through which organisations' aims, objectives and values are set and pursued in the context of the social, regulatory and market environment in which they operate. Corporate governance processes and systems include monitoring the actions, policies and decisions of organisations and their agents, in which category I include their suppliers. Corporate governance is therefore about what the board of an organisation does and how it sets the **values** of the organisation.

In the UK, the generally accepted 'Gold' standard on corporate governance is provided by the UK Corporate Governance Code[4]. The first version of the UK Corporate Governance Code was produced in 1992 by the Cadbury Committee and it still.(paragraph 2.5) provides the classic definition of the context of the Code:

> *"Corporate governance is the system by which companies are directed and controlled. Boards of directors are responsible for the governance of their companies. The shareholders' role in governance is to appoint the directors and the auditors and to satisfy themselves that*

[1] http://www.cqc.org.uk
[2] http://www.fca.org.uk
[3] http://www.bankofengland.co.uk/pra
[4] https://www.frc.org.uk/Our-Work/Codes-Standards/Corporate-governance.aspx

an appropriate governance structure is in place. The responsibilities of the board include setting the company's strategic aims, providing the leadership to put them into effect, supervising the management of the business and reporting to shareholders on their stewardship. The board's actions are subject to laws, regulations and the shareholders in general meeting."

I have no issues with the broad principles in the Code, but I do have concerns regarding its limited scope and restrictive wording. The shareholders' role is limited to satisfying themselves that there is an appropriate governance structure in place. For my part, I would like to see 'effective' inserted in the wording; corporate governance structures and systems can be appropriate, but that does not of itself mean that they are effective.

If we accept the general principles set out in the Code then why should it not be more generally applicable? The Code applies principally to 'listed' companies and primarily to 'Premium' listed companies, which I think is unnecessarily restrictive. There are around 8,350 UK registered companies with a turnover of £100M or more, there are only around 2,450 'listed' companies. Many commercial organisations, some of very considerable size, no longer seek a stock market listing and are thus, with some exceptions, not in scope of the Code. There are many other organisations with very substantial revenues that also fall outside the scope of the code.

Such organisations include:

- Charities,
- Educational institutions (Academies, City Technology Colleges, Universities, etcetera),
- Government Executive Agencies/Trading Funds,
- Local Authorities and;
- NHS Trusts.

Most of these organisations are subject to some form of regulatory framework, but many of the regulators have a remit that is restricted to either financial, or professional standards. Both of these have a role to play and I am not suggesting that they can be replaced by or, in some way, subsumed into the Code; I simply believe that having a single, common, standard for Corporate Governance in the UK is a good idea for all organisations and their stakeholders. Corporate governance should not be confused with professional ethics, regulation and standards, which I believe should be subordinate to a single, universal Code of Corporate Governance..

Do we really need the current proliferation of codes of (Corporate) governance? Do charities, local authorities, NHS Trusts, schools, voluntary organisations, and the rest, really need their own (entity-specific) codes of governance? I think not; I believe that, with minor amendments, the UK Corporate Governance Code could be universally adopted.

My general proposition is that all organisations with revenues in excess of £100M should be in scope of the Code; the £100M figure is entirely arbitrary, but seems to me a sensible threshold. I have deliberately chosen revenues/turnover because of its simplicity and relative transparency. I also propose that all organisations be encouraged/permitted to voluntarily subscribe to the broad principles of the Code. I accept that such a move would involve some work on the part of the likes of the Charities Commission, Financial Conduct Authority, and Government

Departments, but I believe that it would be well worthwhile. In her recent book (Good Company)[5] Laurie Bassie stated:

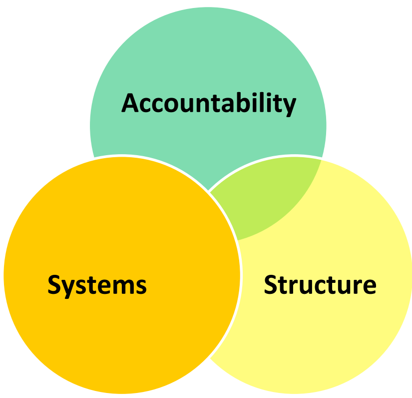
> "Many companies during the past decade have launched disparate initiatives such as becoming an employer of choice, reducing carbon footprints and beefing up compliance efforts. But firms that aim to succeed in sustainable ways must move to become good companies through and through."

If we substitute 'organisation' for 'company', or 'firm' then I think that this paragraph becomes relevant to all manner of organisations. In the same way, we can take paragraph 25 of the original (Cadbury Committee) UK Corporate Governance Code (see above) and with a very few alterations, it takes on a much wider scope:

> *Corporate governance is the system by which organisations are directed and controlled. Boards of directors, governors and trustees are responsible for the governance of their organisations. The shareholders'/stakeholders' role in governance is to appoint the directors, governors, trustees and the auditors and to satisfy themselves that an appropriate governance structure is in place. The responsibilities of the directors/governors/trustees include setting the organisation's strategic aims, providing the leadership to put them into effect, supervising the management of the organisation and reporting to shareholders/stakeholders on their stewardship. The actions of the directors, governors and trustees are subject to laws, regulations and ultimately the stakeholders.*

Corporate governance is inextricably linked with accountability and values. Without the clearly defined distribution of accountability, corporate governance structures and systems, no matter how well designed, are missing an essential ingredient. To use the analogy of Adair's[6] interlinking three circles, all three elements of Accountability, structures and systems need to be present if an organisation is to have effective corporate governance. If any one element is missing, or incomplete then the other two elements are left incomplete.

A Model for Corporate Governance



I firmly believe that for effective corporate governance organisations need a clear set of values and it is arguable that corporate governance must be 'values based' if it is to become fully embedded in the organisation's culture. Effective/good corporate governance and a clear set of values are integral to being a 'good' organisation and, as Laurie Bassi has demonstrated, being a

[5] Bassie L, Frauenheim A, McMurrer D, with Costello L (2011). Good Company, Business Success in the Worthiness Era. Published by Berrett-Koehler Publishers Inc.
[6] http://www.johnadair.co.uk

good company/organisation is good for business. Being 'good', provided it is also accompanied by consistency and transparency, will have a number of significant benefits:

- ✓ It will enhance your organisation's reputation generally,
- ✓ It will give consumers, customers, suppliers and potential investors confidence,
- ✓ It will help establish/enhance your reputation as 'An Employer of Choice',
- ✓ It will, to a degree, enable you to differentiate (positively) your organisation from others, and;
- ✓ It will facilitate increased engagement, loyalty and trust on the part of your people.

In my experience, there is a tendency to conjoin corporate governance with audit/compliance and risk management. I consider this inappropriate as it attempts to combine the strategic (corporate governance) with the operational (audit and risk management), which is not intended in any way to diminish the importance of the likes of audit, internal controls and risk management. They are essential elements of the framework that underpins effective corporate governance; they provide some of the checks, balances and monitoring needed to facilitate good corporate governance.

There is also a pronounced tendency in many organisations to view corporate governance and associated activities (e.g. audit and risk management) from a purely financial perspective. The financial perspective is clearly important, but if you accept the premise that people are potentially an organisation's greatest liability, I contend that, in matters of corporate governance, an organisation's people (Human capital) are of equal importance to financial matters.

Although the Board's role is pivotal, corporate governance is not the sole responsibility of the Board. It is the responsibility of everyone employed by an organisation. There is a proverb:

> '*For want of a nail the shoe was lost; For want of a shoe the horse was lost;*
> *For want of a horse the battle was lost; For the failure of battle the kingdom was lost;*
> *All for the want of a horse-shoe nail.*'

The proverb has been attributed to a number of people, not least William Shakespeare, but for me its importance lies in the interpretation. It describes a situation in which a failure to anticipate or correct some initially apparently minor problem leads progressively through increasingly critical stages to a disastrous outcome. It follows that although corporate governance and accountability are seen primarily as matters for, the responsibility of. the board and executive management, they are actually matters for and the responsibility of all employees. This cannot happen without clarity, consistency and transparency. For me, effective corporate governance is inextricably linked with an organisation's culture, its values and its people.

Effective/good corporate governance needs to be embedded in an organisation. As legislation and regulation change, so must an organisation's corporate governance systems, processes and structure. However, if an organisation's approach to corporate governance is values-based and is an integral part of its culture then such changes will be adaptive/evolutionary in nature, rather than requiring revolutionary change. This is one of the principal reasons that I prefer the UK's incremental (Comply, or explain) approach to that adopted by some other jurisdictions, most notably perhaps the USA with the Sarbanes-Oxley Act 2002[7] and the Dodd-Frank Wall Street Reform and Consumer Protection Act 2010.[8]

[7] http://www.sec.gov/spotlight/sarbanes-oxley.htm

[8] http://www.sec.gov/spotlight/dodd-frank.shtml

Let us put aside, for the moment, the Board and consider corporate governance at a more fundamental, but equally important, level. I accept that corporate governance is essentially strategic, but looking back at my proposed model sound/effective corporate governance needs to be underpinned by the actions of all your people, especially your people managers. Do you fully consider and take account of corporate governance and your organisation's values when undertaking for example:

- Performance reviews,
- Recruitment & Selection, and;
- Pay reviews?

You may be wondering what relevance these have to corporate governance, so let me provide some examples:

i. Performance reviews are an element of Performance Management, which includes Learning & Development, and Organisation Design & Effectiveness. The objective-setting that should be an integral part of the performance review process is not just about operational objectives, it is also about organisational objectives/values and the behaviours that underpin the successful achievement, maintenance, and promotion of those objectives and values,

ii. When you are engaged in recruitment and selection, apart from looking for people with the appropriate experience and skill-set, you are/should be also looking for people with the right values, people who will promote and support your organisation's values and, inter alia, your organisation's approach to corporate governance, and;

iii. Pay reviews, or more accurately, pay structures, should be focussed on promoting the long-term success of your organisation, rather than short-term benefits/gains. Structures that encourage the pursuit of short-term gain can encourage, in effect approve, inappropriate risk-taking behaviours that are inconsistent with good corporate governance.

Assuming that both your approach to corporate governance and your values are explicit and transparent then all of your people will be aware of them and will have an expectation that their managers will honour them and apply them in all matters pertaining to the management of people. The same holds true for the people that you are trying to attract through your recruitment and selection activities. There is probably a detailed reference to your corporate values on your website and there is almost certainly a reference to corporate governance on the same website. Unfortunately perhaps, there is also a vast amount of information available on the internet and if that information is not consistent with the values that your organisation espouses then you have a significant problem.

For more reading on this topic, I suggest both 'Corporate Governance and Accountability'[9] and 'Corporate Governance – Principles, Policies, and Practices'[10]. If the opportunity should arise, I recommend attending one, or more, of the events/meetings of the All Party Parliamentary Corporate Governance Group (APPCGG)[11]. I have been fortunate enough to attend a number of the Group's events and they are very informative and interesting.

[9] Solomon J. (2013) Corporate Governance and Accountability (4th Edition), published by John Wiley & Sons Ltd
[10] Tricker Bob (2012) Corporate Governance – Principles, Policies, and Practices (2nd Edition), publishedby Oxford University Press
[11] http://www.appcgg.co.uk/