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Corporate governance is at a crossroads today. There are pulls and pressures from different directions. On the one hand legislations such as Sarbanes Oxley are taking the micky out of the business. On the other hand self-regulation has not worked. Most investors agree with the views of Elliot Spitzer, US's crusader against corporate fraudsters, that honour code among CEOs has not worked. Boards have not done their duty of oversight and self regulation has been a failure. So what is the choice before us? Hence the theme for the 7th International Conference for Corporate Governance Making Corporate Governance Work Through STARR – Selection, Training, Appraisal, Remuneration and Retirement of Directors – the five key areas to improve corporate governance.

We need to look at the selection processes. How do we recruit directors? What are our criteria? Do we realise the importance of diversity? Have we broadened our gene pool? Of course the key is training. Corporations are getting exposed to a multitude of complex range of problems. Legal and corporate frameworks are changing every day. Companies operating internationally are exposed to global problems – human rights abuse, poverty, AIDS, climate change. There is a huge revolution brewing. The revolution is about ethics and CSR. Both require moral courage. How do you acquire moral courage? How do we install the software of moral courage? Training is the only way to help us install this software and make it work.

Yet, directors are getting little training to handle these new challenges. Surveys have indicated that 62% of Non-Executive Independent directors of listed companies have received no training for their roles. Indeed directors sneer at the very suggestion of training. Training providers have confided that they have to call director training programmes as director development. If they termed it as training none would join.

We should have a system of effectiveness of our selection and training processes. We, therefore, need to develop appraisal systems to monitor effectiveness of the board – the CEO, directors and the chairman.

The purpose of focusing on STARR – Selection, Training, Appraisal, Remuneration & Retirement of Directors in this conference is to bring home the point that companies that destroyed shareholder values had all boxes ticked. They had a full complement of independent directors. But these directors did not ask the right questions at the right time. Asking questions is also a skill. One needs training for that. More importantly, the significant issue is not whether you have an independent director but whether the director is of an independent mind.

The issue of role and effectiveness of non-executive directors was first taken up by Derek Higgs in the report he submitted to DTI in January 2003. He talked about four attributes of Non-executive directors: integrity and high ethical standards; sound judgement; the ability and willingness to challenge and probe; and strong interpersonal skills. You cannot create an independent director simply by issuing a decree. This is a matter for developing, transmitting and internalising the training software that will help him/her exercise an independent mind. Derek Higgs also made recommendation about remuneration. This reads:

“The remuneration of non-executive director should be sufficient to attract and fairly compensate high quality individuals and the level of remuneration appropriate for any particular non-executive director's role should reflect the likely workload, scale and complexity of the business and the responsibility involved”.

This has led to a lot of confusion and non-executive directors today are drawing almost as much salary as the executive directors thus defeating the whole purpose of appointing outside directors. The remuneration has far more repercussions. It is creating a great divide in the

corporations. Never before in corporate history has the differential between the highest and the lowest paid person been higher.

Retirement is equally an important issue. Unless you retire directors you cannot induct young blood which is so necessary to revitalise corporations.

This volume contains papers contributed by distinguished corporate governance experts for the 7th International Conference in Corporate Governance. I am grateful to these authors for their brilliant contributions. The focus is on issues how boards can improve the quality of corporate governance by improving policies of selection, training, appraisal, recruitment and retirement. The contributors discuss both the compliance and competitive issues. There is a preponderance of emphasis on competitive issues such as CSR, sustainability and triple bottom line because it is these areas that will help the boards to use corporate governance as an instrument for creation of sustainable wealth that could create happiness for all. I hope you enjoy reading these contributions as much as I did as triggers for self-improvement. Enjoy the conference.

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Building Tomorrow's Boards

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Business has changed as never before. Technology and globalisation have changed the way we work. The greatest change however is in public expectations of the business. The obsession with bottom line profit and shareholder value looks tired and no longer provides the stimuli for leadership, motivation, innovation or brand equity. Stakeholders are questioning the very purpose of the corporation. Building brands and not profits has become the focal point of the corporate agenda.

One of the greatest hindrances in developing boards is the corporate allergy and apathy to the word training when applied to directors. Training is important for staff but not directors. A belief has gained currency in corporate boards that once you step into the boardroom you no longer need any training. You can call it development or better self-assessment but certainly not training. It is essentially because of this that despite so many codes and statutes for improving corporate practices the situation on the ground is still far from satisfactory.

In an interview to Wall Street Journal, Eliot Spitzer, New York's crusader against corporate fraudsters said: "The honour code among CEOs, did not work. Board oversight did not work. Self-regulation is a failure."

Yet you cannot change corporate behaviour simply by issuing edicts. This has to come from inside. Changing behaviour is not easy. The regulation simply forces us to build firewalls to prevent detection. It encourages focus on building manuals on HNGC (How Not to Get Caught), not really how to improve corporate governance.

This is a tragedy because while humans do not like change, they do have great potential to improve once they get down to it in a determined manner. Determination comes through realisation that there is a need. Realisation that a problem exists itself provides 90% of the solution. Our greatest challenge, therefore, is to make boards realise that lack of director training is a problem.

In his report on non executive directors Derek Higgs defined the following four attributes for the directors: integrity and high ethical standards; sound judgement; the ability and willingness to challenge and probe; and strong interpersonal skills.

The question is how are they to be inculcated? Obviously we don't all come installed with this software. So how are we to learn without proper training? More importantly how are the directors going to cope with the wrenching change they experience every day? These changes have shaken the very fundamentals of business and the fundamentals even of corporate governance. Compliance to regulation is no longer the key nor is the old style competitiveness because the criteria for competitiveness itself have changed.

We are witnessing the death of shareholder value as a competitive differentiator. Various booms and busts have shown that shares have no intrinsic value. They move like shuttle cocks swept by market winds. Many CEOs are swept away by the alarming share price changes as a consequence of some small piece of news about their own company or a competitor. Corporate governance failures today pose a much bigger threat in destroying corporate value than ever before. Billions are wiped out from the stock within days.

Standards of corporate governance have changed vastly due to the migration of public value. The issue of statutory compliance is no longer as important as ethics and social responsibility of the business. Shareholder value as a concept has lost the plot because of the interdependence of the world brought about by globalisation and connectivity. It is no longer a dominant business driver and is getting increasingly discredited.

Shareholder value on its own is regarded as an immoral concept because it demeans the purpose of business as a selfish pursuit to earn profit for its owners with no obligation to other stakeholders whose contribution is greater than the owners. It is also a demotivator. The fierce competitiveness of today's business requires not only hands but hearts and minds to beat the competition. Who will stick his/her neck out or put his/her heart to be passionate in making money for others? It negates the effort to build a loyal customer base. Corporations are nurtured to defy laws, bend the rules, explore the vulnerable and build firewalls in pursuit of HNGC.

In his well researched article in this volume on "Independent Directors – Key to Good Governance" Mr P K Banerjee of ICFAI draws attention to the 21 Century expectations of the corporations. He says: "20th century has seen lot of misuse of power, greed, lust and above all one-upmanship. The collapse of giant corporation like Enron, World Com, Arthur Anderson have rewritten the rules of corporate history in the ink of greed, self conceit and fraud, forgetting that power is only legitimate when it is used for general good of the society at large. So called captains of the industry has forgotten that a real leader should have the confidence to admit limitations and failures and work with others to achieve shared long term goals; a confident leader works with others to shape a pattern of power and working values that can be effective in the long run".

All this has changed. Boards of tomorrow will not focus on shareholder value but corporate value as a whole focusing on contribution by each stakeholder. They will be transparent and accountable, environmentally sensitive, socially proactive, aspiring for long term sustainable growth through an ethical approach. Sustainability has become a big issue. There is a growing recognition that this is my planet and I must keep it out of harm's way for my children. There is an increasing concern for societal values, poverty, equity, work life balance, volunteering and community service.

The fundamental precept of tomorrow's board will be built on turning failures into virtues. Boards would realise the power that is unleashed by the moral courage in admitting mistakes. It creates ability to deal with failures and use them as learning opportunities.

Board meetings will be occasions for discussing failures and learning from them. Directors will be skilled to ask questions and be encouraged to do so. Transparency will be the order of the day. There will be rewards for admitting failures so these could serve as models for learning and improvement. Annual reports would faithfully track both success and failure. There will be no effort in egging the profits and sweeping the losses under the carpet. Failing CEOs will not face sacking. There will be a requirement that they serve the company to clear the mess. After all having burnt their fingers earlier they have a better chance to set things right than someone who is starting without experience.

Annual reports will quantify the degree of environmental damage in production processes. Creation of wealth will be counted in terms of all three parameters: financial, social and environmental capital. Graphs will not only show the quarter earnings and other financial ratios but also the differential between the lowest and the highest paid person in the organisation. Customers and suppliers will be invited to board meetings to make presentations of their feedback of company's efforts towards triple bottom line. Representatives from office and shop floor employees would also address board meetings.

Boards will be accessible and self-critical groups. They would regularly appraise each other and review the performance of CEO and Chairman marking them out of 10 to ensure 360 degree feedback.

Boards of tomorrow will not confine themselves in air conditioned boardrooms but will spend time on shop floors and plants with service and sales engineers to get the feel of business on the ground. As Mark Goyder Director of Tomorrow's Company says "The unscripted appearance of an independent director at one of the plait's premises to sit in on some meetings and take a bowl canteen of soup with a random group of employees would be unsurprising: as a result when employees had serious doubts about the ethics of a new directive from on high, they would know that in extremis they could e-mail or phone a board

member without fear of reprisal because openness always won over hierarchy.” Mark Goyder describes how new independent directors are to be initiated:

“You are a new independent director on two boards. Company A does things in style. You dine well with your fellow directors. The board meeting the next day is dispatched efficiently by the chairman. There is a general feeling things are going well. And the CEO and the FD seems to be competent people. You are relatively new. You feel proportionately able to ask one, may be two, questions.

Before you get near the board meeting at company B you have had several stages of induction. The chairman explains that your role is not simply to oversee the current reports of performance in the business, but to identify risks and opportunities and hold the business to account against its original purpose and values.

You visit the operations, take lunch in the staff canteen with a mixed group of employees. You meet one of the NGOs that opposed the company. You learn about the major business risks. You meet some major investors. Your induction covers your own ethical position, and how to deal with potential conflicts of interest. You are shown how the company’s business principles are communicated to every employee in the world. The company secretary explains that you always have the right of independent access to information. You discuss your own professional development towards achieving chartered director status.

At the end of the induction, you hope that can describe yourself as an independent director: you would not longer describe yourself as ‘non-executive’. And, you ask yourself, how in limited time do you keep your finger on the pulse?”

The intangibles will be the biggest business drivers for tomorrow’s boards. The main focus will be on corporate ethics and CSR. These will become the most powerful factors for both brand creation and destruction. Transparency will become a competitive differentiator. A MORI survey among corporate communications directors of FTSE 100 companies showed that 93% believed that publishing non financial information enhanced a company’s reputation and made for better management decisions. A model based on a Fortune/Management Today of most admired 500 US and 250 UK companies showed a direct correlation between reputation and financial outcomes – share price and credit rating. The survey suggested that reputation on average accounted for 27% of the FTSE 250 companies market capitalisation. A US study published in February 2004 indicated damaged reputation can take up upto to 4 years to be restored.

Tomorrow’s boards will not take CSR as a box ticking exercise driven by external pressures or a PR exercise. They will understand the value of embedding it in the business practices. One of the key tasks of tomorrow’s boards would be to develop reputation management systems to monitor reputation. CSR will act as insurance against bad news. In tomorrow’s business bad news will hit companies much harder than today; like tornados tearing apart the guts of the business and shattering the market confidence. CSR will provide the survival kit.

The best armour, of course, of tomorrow’s boards will be their commitment to training and learning. This will be the largest single factor that would set tomorrow’s boards apart from today’s boards. Boards will be exposed regularly to self-development programmes to keep themselves abreast of the changes and prepare themselves before the competitors do. They will analyse risks and opportunities faster than the competition and would understand the value of developing their intangible assets. Boards of tomorrow will be the true learning organisations. These boards will be composed of directors who, using words of Mahatma Gandhi, will live as if they were going to die tomorrow and learn as if they were going to live forever.
