THEME PAPER

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Corporate Governance Perspectives & Sustainability Challenges

Reassessing Governance and Sustainability

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Over 100 Heads of State and Government attended this year's Earth Summit in Rio to review progress since the UN Conference on Environment and Development that was held in Rio in 1992. During the intervening 20 years new challenges have arisen as development has intensified pressure on the environment and the time is ripe for business leaders to consider their own contributions to sustainable business growth.

It is also 20 years since the publication of what has become known as the 'Cadbury Report', the first of what has become a steady flow of reports on corporate governance. The reports have led to codes of practice in many parts of the world, some new legislation and significant growth in the number of advisers, consultants, academics and other experts who claim an expertise in corporate governance.

The Institute of Director's 2012 global convention planned for October 10-12th of this year in London embraces the 12th International Conference on Corporate Governance and the 3rd Global Convention on Sustainability. The convention presents an opportunity for participants to take stock of what has been achieved in the arenas of governance and sustainability and discuss next steps which business leaders can take.

In many countries directors and particularly CEOs are under intense pressure and media scrutiny. When errors of conduct and crises of confidence arise they and Governments are expected to act quickly and decisively. Coping with crises and uncertainty is a global challenge for those with governance responsibilities, whether operating in a country where corruption and malpractice is widespread or in the unexpected spotlight of a Parliamentary enquiry or criminal investigation.

Responses can range from the pragmatic, such as reviewing crisis communications arrangements, to the more strategic, such as establishing a vision for an organisation's role in the green economy, responsible behaviour and growing sustainably. Business leaders may need to better engage with stakeholders and consider what new governance, risk management and reporting arrangements need to be put in place.

Approaching the London convention one senses that more than pious statements about appropriate conduct and ostensible observance of codes of practice may be required. Business leaders need to find ways of making things happen. This can require changes of behaviour, especially by those in the front line who are interacting with stakeholders such as customers and members of the public.

More than 'box ticking' is required. While an association between what corporate governance codes would consider 'good governance' and company performance is evident, it is not always clear that the latter is a consequence of the former. Maybe good boards and management teams are endeavouring to get their governance 'right' just as they try to do the 'right thing' when designing, pricing and selling their products and services and building relationships with various groups of stakeholders.

The 'Cadbury Report' does not feature in the index of the author's 1993 book 'Creating Excellence in the Boardroom'. The omission was not because of a lack of interest in governance, but because the book's focus was upon the conduct of boards and the behaviour of directors in building successful companies. Its premise was that it is the qualities of directors and the quality of their decisions and implementation that determine business development rather than board and corporate structures.

What directors do in relation to strategic challenges and opportunities continues to be more important than the few moments they periodically devote to checking they have met the requirements of a governance checklist. Corporate failures continue to occur - irrespective of whether or not the organisations concerned have complied with governance codes – where mistaken or inappropriate strategies have been pursued.

Despite elaborate risk management procedures, much expenditure on professional advice from leading professional firms, and recruiting 'A team' directors from the ranks of 'the great and the good' some boards continue to act in a blinkered way, behave like lemmings and take stupid decisions. It is remarkable that there have not been more legal cases against directors when simple questions such as how loans might be repaid in the event of a property bubble bursting have not been asked.

In relation to the London convention's twin themes of governance and sustainability, one could conclude that in the short-term certain companies and banks and financial institutions in many countries are much less sustainable than the world's environment and climate. More widespread failures of financial institutions have only been prevented by Government bailouts and collective action. The latter has extended to the whole of the Euro-zone in the case of the support of Spanish Banks.

One could argue that the risks of corporate failure and systemic collapse have grown as the number of governance codes has increased and more organisations have sought to observe them. In place of unified boardroom teams endeavouring to keep their wits about them while building global businesses, one now finds 'independent directors' keeping their eyes on executive director colleagues and an army of checkers examining just about everything except the 'killer' factors that are often missing from board assurance frameworks with their long list of risks and mitigating actions.

With so many codes, so much regulation and legislation, and so many different systems in place there is a tendency for people to assume someone somewhere is covering all the bases. When the sheer number of requirements is too large for any one person to master more than particular areas there is a danger that certain risks will fall between the cracks or not be addressed as a whole. People do not want to appear ignorant or naïve at a board meeting and sometimes obvious questions are not asked.

After twenty years of corporate governance the core work of the Institute of Directors to help directors to become more competent and boards to be more effective has never been more important. One need to revisit the basics of governance and ensure that directors understand the distinction between direction and management, are properly prepared for their roles, and are able to distinguish between successful and unsuccessful approaches to sustainability and other challenges faced by boards.

Directors need to understand that much has altered over the last twenty years in relation to the context within which boards operate. Change is not new. Previous and 'pre-governance' generations of directors also faced major changes such as those caused by information and communications technologies, flight and antibiotics. Boards need to track external developments, anticipate their impacts and initiate appropriate actions to address challenges and exploit opportunities.

Among changes that many boards have tracked are more demanding customers, greater concern with the environment and a growing willingness of individuals and motivated groups to use the internet and social media to challenge much larger organisations. Major corporations that have attracted intense criticism and been under the spotlight found themselves unexpectedly vulnerable. A reputation, image or brand that has been built up over a long period can be quickly lost when responses are inadequate, insensitive or perceived as excessively defensive.

When younger people want to make a difference and have more control over their lives and customers have more options than before, corporate boards can no longer take allegiance for granted. Relationships with employees, customers, suppliers, business partners and local communities have to be mutually beneficial. To engage and secure interest and commitment organisations need to be turned into causes. Top-down approaches to 'command and control' may no longer work.

Fresh thinking is needed in many corporate boardrooms. Effective governance involves the challenging of assumptions, expectations and prevailing practices. When the boardroom agenda is already long and there are pressing matters to deal with, certain activities are sometimes taken for granted. This is especially so if other companies appear to be undertaking them and when senior members of the management team champion them. Yet focused scrutiny might reveal serious deficiencies and uncover more affordable and flexible alternatives.

A five-year investigation led by the author has found that many companies adopt approaches to transforming performance that are expensive, time consuming and disruptive in comparison with quicker and more affordable options. The findings set out in two new reports *Talent Management 2* and *Transforming Public Services* suggest that while an area such as change, talent or knowledge management may be too important to leave to executives, director involvement and questioning should be appropriate, balanced and strategic.

There is much that independent directors and their senior executive colleagues should challenge. For example, many companies commission expensive culture change programmes, even though different parts of an organisation may need different cultures, relationships may need to be built with people from a great many cultures, and the form of organisation and culture required in future years may be uncertain.

If a culture change to secure certain behaviours and prevent others is being sought the chances are it is unnecessary even if it could be achieved. Changing performance support and remuneration incentives to help and motivate people to do what is desired and prevent or discourage what one is seeking to prevent may well achieve the results required and other benefits in a small fraction of the time and at much less cost.

Many changes are resisted because people do not feel that they are in their best interests. Blatantly seeking to squeeze more out of people without any compensating benefit is unlikely to engage. In contrast, by making it easier and less stressful for people to excel at difficult jobs, performance support can yield advantages for both people and organisations. It is often quickly adopted without the need for ‘corporate communications’ and ‘management of change’ programmes.

In this and other areas one sees many directors engaged in groupthink, behaving like lemmings, and following fashions and fads. The challenge provided by independent directors who have the capacity to think for themselves rather than run with the herd can be invaluable. Why are environmental and sustainability issues being seen by some boards as challenges rather than viewed as opportunities?

Getting the right balance between factors such as change and continuity is especially important. Unnecessary changes can be stressful and disruptive of important relationships. Boards should only change what needs to be changed and ensure that people understand why change is needed and are equipped to bring it about.

Sometimes it requires courage not to make certain changes when other organisations are undertaking them. Some boards have been saved from the consequences of poor decisions by a reluctance of people to implement them. Marconi was not so fortunate and brought to its knees when its policy of outbidding others to invest in internet related businesses at inflated prices was driven through the organisation by a determined chairman and CEO.

Recognising developments and opportunities in the context in which one is operating is one thing, but reacting appropriately is another. Flexibility and speed of reaction can be critical. In a dynamic situation what may need to change is an organisation’s approach to change in order to adapt more quickly and with much less effort and without the collateral damage that can result from general corporate-wide initiatives.

Many directors should spend more time reflecting upon what they can do to help people to cope. The right support arrangements can be personalised and enable people to handle uncertainty and quickly change direction. They can also impact directly upon behaviours independently of corporate cultures, structures and processes, and allow bespoke responses to the requirements of individual customers.

Far too often corporate organisations are getting in the way of what is required. When people in the front-line and customers can be helped to help themselves directors should challenge why so much effort is being devoted to changing organisations rather than eliminating areas no longer required. When so much is uncertain and difficult to predict, they could also question why so much time is devoted to multi-year plans as opposed to equipping an organisation to learn, evolve and adapt.

When considering governance arrangements and sustainability strategies boards need to take account of the changing nature of the entities for which they are responsible. Companies are networks of relationships embracing all those who collaborate to deliver value sought by customers, including the customers themselves. Performance support can be critical for ensuring that people are able to quickly access whatever they need to deliver and/or obtain desired outcomes whenever a requirement arises and wherever they are, including when on the move.

Many business leaders could also rethink their own roles. For example, are they are getting the right balance between providing top-down leadership and giving bottom-up support. Some boards appear cocooned by C-suite senior executives and the world of the boardroom when their members would benefit from more direct contact with customers and those in the front-line charged with addressing their needs.

To outsiders some directors appear more concerned with the ‘walking overheads’ that make up the senior management teams of their organisations than they are with customers and front-line staff. Preparing a cadre of future leaders may seem more important than helping today’s people to excel at key jobs, handle difficult issues and remain current and vital. Time is spent discussing expensive coaching arrangements for the few rather than adopting affordable ways of providing people across the organisation, business and channel partners, customers and users with 24/7 support.

Agility, affordability and speed of reaction are increasingly important. There is little point boards commissioning multiple initiatives when priorities and requirements may change long before they achieve any positive results. Much better to adopt more affordable approaches such as putting the right performance support arrangements in place to allow new offerings to be quickly launched new policies to be easily implemented, and multiple objectives to be simultaneously achieved on a global basis.

Once customers, users and front-line staff are properly supported expensive and protracted corporate restructurings may no longer be required. Letting different areas of an organisation organically evolve may be a cheaper and more sensible option when the future is uncertain. The siren voices of powerful vested interests for whom restructuring and culture and change management represent good business should be ignored when success is affordable with existing people and cultures.

As vested interests abound and many people have services to sell it is not always easy for business leaders to decide upon from whom to take advice. When major corporations are implicated in governance scandals, damage the environment or make large losses or significant write-offs, one often finds leading professional firms and major consulting firms among their advisers. Smart directors recognise that counsel is given by particular individuals. The best among them have a nose for whom to trust.

The most valuable lessons can sometimes be learned from those who have found themselves in a hole and yet managed to find a way out. Discussing issues with ones peers and exchanging thoughts with others who face similar problems can be invaluable, particularly if they are willing to ‘tell it as it is’. This is where networking and sharing experiences at gatherings like the IOD’s global conventions can help.

This brings us back to the essential importance of directors and the value of challenge and contending viewpoints when boardroom decisions are made. A ‘rubber stamp’ board can result in an organisation sleep walking to disaster. A thoughtful and reflective board that is open to new ideas and willing to learn from others, questions assumptions and proposals, and has the courage to try better alternatives can be the best guarantee of continued survival and relevance in uncertain times.

Further Information

The reports *Talent Management 2* and *Transforming Public Services* on a quicker and more affordable route to high performance organisations are published by Policy Publications and can be obtained from www.policypublications.com

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