FEATURE ARTICLE

Positive Corporate Governance: A New Stewardship Approach for the Next Era

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Origins

This year marks the 30th year since the issuance of the Cadbury Report in the U.K. in December 1992. This monu -mental document has, by any measure, heralded the genesis of modern corporate governance across the globe. The underpinning of Cadbury, particu -larly the "comply-or-explain" philosophy, has steered corporations in protecting investor interests, especially those of the shareholders.

Ten years on, the Sarbanes-Oxley Act (SOX) was enacted in the U.S. in July 2002. This legislation is now in its 20th year of existence. This is an even more significant landmark law that is mandatory for companies and affected entities to comply. In fact, the coverage of the Act has been deemed to be overwhelmingly comprehensive and all encompassing.

But has there been progress since the launch of the duo pivots of corporate governance? Cadbury-SOX was supposed to transform the landscape. Cadbury, in particular, has been the major influence in corporate gover - nance thinking in many Commonwealth localities, including India and many jurisdictions in Asia. SOX was deemed a powerful antidote for corporate impropriety in the businesses and the professions.

Has Regulation Moved the Needle?

Corporate governance has been placed under scrutiny with the ever increasing gamut of regulations. But we are not sure if it has actually changed for the better.

To be sure, these regulations were themselves quick-fix reactions. Cadbury came hot after the heels of several fiascos namely Bank of Credit and Commerce International, Maxwell Communications and Polly Peck. SOX was instigated by the infamous Enron debacle, together with a series of unfortunate incidents such as Adelphia Communications, Global Crossing, Tyco and WorldCom.

Cadbury-SOX may not be the be-all and end-all. But with the plethora of principles and legislations, one would have expected significant improvements in corporate governance practices, and certainly a reduction, if not eradication, of big scandals.

But scandals continued to happen. Even bigger ones.

Even with SOX, a succession of governance related catastrophes occurred during the U.S. financial crisis of 2008. The names involved are no less than reputable insurers like AIG, legendary investment bankers like Bear Sterns, Lehman Brothers and Merrill Lynch and supposedly rock-solid government-sponsored enterprises like Fannie Mae and Freddie Mac.

In Asia soon after, there were its own versions of "Enron" as seen in Satyam Computer Services of India in 2009 and also Olympus of Japan in 2011.

Just in the most recent few years, we are seeing mega-scandals in corporate governance all across the world, notably the Volkswagen outrage that began in 2015 and the Nissan ignominy that came to light in 2018 and is still unresolved.

Even more current in 2020 is Germany's Wirecard's fall from grace following a chain of accounting frauds. Then we witnessed financial falsifications by listed companies like China's Luckin Coffee. And the year saw the long-awaited imposition of fines for the famed Wells Fargo which was caught faking client accounts some four years back.

Has Governance Gone Awry?

Suddenly the world of corporate governance is in a serious dilemma.

Maybe it is time to go back to the examination room. Has the medicine been ineffective? Was the diagnosis wrong? Or was the treatment wrong? Maybe we had the wrong patient? Or the wrong doctor? Or was everything just wrong?

I think we had simply barked up the wrong tree.

We have probably framed the problem wrongly. It is not about the corporation, the systems, the regulations or the practices. It is about human nature.

No amount of codes and laws will suffice if the real problem is not recognized. All the exacting stringent requirements to catch the few culprits will only suffocate the vast majority of companies which are law abiding. And even for that, it has not been effective as history has shown.

Really, our whole approach, our whole underlying assumption for corporate governance needs a fundamental re-examination.

Back to Drawing Board

We have to go back to the original purpose of corporate governance. Having more directives for complying and more boxes for ticking certainly do not add up to enhancing the firm's worth. Hard controls and more rules will only add to the burden and distract from the core task of real governance.

Perhaps we should emphasize soft aspects which are more to encourage good culture, entrench good values and embed good practices.

Indeed one may even ask - is corporate governance actually a return of “red tape” in more palatable words? Has corporate governance evolved in ways that deviate from the intent?

Going the Positive Way

We can take a leaf from the book of an emergent branch of psychology called positive psychology. The focus is to draw out the fine points and virtues of humankind, and to treat each person as a talent who wants to give the best and have happiness.

We can view through a whole new lens of positive corporate governance.

The premise is that a person, whether director or manager, essentially desires to do good for the company. This is a departure from the traditional agency theory where there is a divergence of interest between the principal (shareholders) and agent (management).

Positive corporate governance is somewhat akin to the stewardship paradigm, the counterview of agency theory. Accordingly, directors or managers are like stewards who are entrusted with the resources and the resultant power of decision-making on the right usage.

Applying Stewardship

In positive corporate governance, the traditional antagonism gives way to synergism amongst the stakeholders. Tension becomes cohesion and the divergence of interests converts to convergence. The critical notion is confidence in people where the management and the board of directors work as unified partnerships of stewards for the collective well-being of all stakeholders, including share - holders.

How then do we put in place positive corporate governance based on stewardship?

The key idea is to have people viewed as stewards, each of whom will be entrusted to do their work. First is to reduce the rules. Keep only those that serve critical purposes. For example, these may include minimalistic guide - lines on director independence, director nomination and compensation and audit. Actually positive corporate governance is about what is not there rather than what is there. So reducing the voluminous rules will help.

Next, foster a culture of trust. Pay attention to competence and human development. Underscore the spirit rather than the letter of the law. For example, companies can conduct sharing and training sessions amongst the board and management. Industry and professional associations, such as director institutes or educational bodies, can be tapped to promote healthy agendas of corporate governance in the companies. These sessions can serve to foster the internalization of good governance rather than the convenient, often mindless, shortcut of rule compliance.

Have Faith in People

In the evolution of corporate governance throughout history, we had knee-jerk reactions. We then followed up by arm-twist solutions. This is not good enough. We need to work on the heart and mind. Appeal to rationality and emotionality and this can enhance the adoption and acceptance of good governance beyond just awareness. Center on the outcome and not the process; it's the results that we are interested in.

The traditional rational straw man of economics – homo economicus – who maximizes utility has been a paradigm that guided our business thinking for just too long. The current corporate governance regime based on self-interest has not worked. The pendulum has tilted too much to control at the expense of enlightenment.

Realistically, let's put it this way – the “Wolf of Wall Street” is going to come no matter what the laws or codes are. Let's now go a different path, an enlightened path. Let's restore the confidence in people. Let's give humanity a chance – try positive corporate governance with stewardship at its core. ■

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