Corporate Governance - The Key to Success Or Failure

Corporate Governance is the system determining the direction and performance of corporations. It consists of the interaction of: • the shareholders as owners, acting mainly at the annual general shareholders' meetings; • the Board of Directors, acting on behalf of the shareholders at Board meetings, led by the Chairman; and • the Executive Management, in charge of operational management, led by the CEO.

Dealing with Corporate Governance the central question is in whose interest does the company have to be run, if anybody's. In the past all kinds of concepts were said to be of importance here: Shareholder-Value, Stakeholder-Value, Workers' interests, community issues etc. Implementing one or more of those concepts means putting the company's fate at the mercy of lobbyists.

For greater clarity it is helpful to identify the true purpose of each company: the one and only purpose is to serve the needs and requirements of the company's customers. To constantly and improvingly serve the benefits of the customers is the only way for each company to stay competitive and alive. In other words, the company has to operate in a market-driven way. Without this distinct focus on customer-oriented performance it is useless to discuss anything from shareholder-value to workers' interests because the company will simply have no future.

Corporate Governance has to make sure that the corporation is run well, and it is run well as long as all corporate strategies, structures and decision-making processes serve the sole purpose of benefiting the customers and thus enhance the corporation's own market position. Only when this is consistently achieved and maintained will the company generate value for investors and other stakeholders.
Corporate Governance as the key management system of any company has to ensure long-term corporate health and fitness as well as the necessary dynamics in development, change and growth thereby maintaining corporate performance.

This means that all elements and individuals of the Corporate Governance System are facing significant challenges and therefore have to comply with the highest standards of professionalism, competence and leadership.

Any compromise in the capacity and quality of Corporate Governance jeopardises the existence of the company and is detrimental to the interests of all stakeholders.
Empirical analyses show there is a significant correlation between the quality of Corporate Governance of a given company and its performance in terms of bottom-line results, innovation rate, market share, time to market, employees' and customers' satisfaction to mention just a few important ones.
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Hence good Governance seems to be the only possible insurance against mismanagement and corporate disasters or failures. Mismanagement always stems from human deficiencies, be they incapability, fraud, individual ambitions, conflicts of interest etc. As soon as the real purpose of the company gets out of the sight of management, risks grow to become seriously critical. So the Governance System has to make sure that erroneous developments are addressed at an early stage and corrected immediately.

In the hierarchy of the three constituencies mentioned above the Board of Directors is of the utmost importance because it defines the strategic direction of the company, supervises, controls, hires and dismisses the Executive Board Members, is in charge of proper financial structures and issues the Annual Report. Overall, it is the Board of Directors' responsibility to ensure the implementation and maintenance of a top-notch, state-of-the-art Corporate Governance System.

Professionalising Corporate Governance therefore means making sure the work of and between the constituencies is executed professionally. In the past much attention has been paid to the requirements, development and performance issues of Executive Management.

There is quite a long tradition of analysing and discussing the requirements of top executive management positions. Many "managements buy" approaches have tried to contribute to this discussion and identify recipes for better management. In essence, Management "denotes function but also the people who discharge it. It denotes social position and rank but also a discipline and field of study" *(Drucker, Management - Tasks, Responsibilities, Practices, New York, 1973).*

Business Management consequently means all the processes needed to transform natural resources into demanded products and services. Business Management is thus a profession and Executive Managers are professionals doing their job by complying with market needs and employing state-of-the-art tools.

Professional Business Management consists of the following important elements:
• Marketing
• Human Resource Management
• Social Responsibility
• Transparency in Planning, Budgeting, Reporting
• Corporate Culture

The Corporate Culture represents the value system and mindset of the organisation influencing the conduct of all employees. It is of primary importance in business management that the executives first know what to do and from there come to a conclusion on how to do it.

"Every failure is a failure of a manager; people manage, rather than "forces" or "facts". The "vision", "dedication" and "integrity" of managers determine whether there is management or mismanagement" *(Drucker, 1973).*

It becomes obvious that having a strong, dedicated, motivated and innovative team of professional leaders in place is the single most important competitive advantage of any corporation. However, executive teams of that nature and calibre are not given by fate but are rather the result of intense and relentless endeavours of those who are in charge, namely the Board of Directors.
The Board of Directors is the crucial part of the corporate structure. It is the link between the people who provide capital (the shareholders) and the people who use that capital to create value (the executive management). This means that the Board is the overlap between the small powerful group that runs the company and, in most cases, a huge, diffuse and relatively powerless group that simply wishes to see the company run well.

After World War II, the industrialised world went through a period of weak Boards which were marginalised in their function and power with executive bodies taking ultimate responsibility and power. By tradition and long habit, few if any Boards and their directors have ever (except in a few cases of acute crises) fully lived up to their legal obligations. This may more often have been through ignorance rather than through wilful negligence. Such low standards have, however, become the accepted norm, tolerated by shareholders and not discouraged by strong-willed CEOs.
All too often it was easy for the Chairman, in many cases simultaneously the CEO, to dominate a Board which by its sheer size (30 to 40) and composition (members of nobility, retired politicians, major clients, bankers, friends of the chairman) was not much more than a quarterly luncheon club fulfilling an essentially decorative role.

The Board's primary role is to monitor the Executive Management on behalf of the shareholders. The Board of Directors has the following key functions:
• focus on the ongoing prosperity of the company; and
• promotion of the company's best interests and long-term health.

The core and indispensable functions and responsibilities of the Board of Directors are therefore:
• to define and implement the corporate management structure in the form of a written, agreed document containing standing orders and procedural rules, transparently describing the tasks

and responsibilities of the Board and the Executive Management;
- to provide advice and counselling to top management;
- to select, guide, and regularly evaluate and, when necessary, to dismiss the principle senior executives;
- to determine management's compensation;
- to review succession planning;
- to supervise Executive Management and ensure it complies with the law, statutes, regulations and resolutions of the Board;
- to review the corporate development by analysing the corporate figures furnished by controlling with additional audits executed whenever deemed necessary by the Board;
- to preview and analyse budgets, plans and strategies and to set the agenda for future development; and
- to regularly evaluate the Board's performance and each Board member's contribution.

It is advisable that Boards be organised in some or all of the following committees:
- Nominating/HR: selects candidates for the Board and the Executive Management; approves important HR policies.
- Compensation: sets executive pay and Board compensation.
- Audit: reviews reports of outside audit, internal audit and oversees accounting procedures.
- Finance: monitors allocations of the company's funds and reviews the capital needs and allocations of the company.
- Executive: approves important decisions between full Board meetings.

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Working along these lines requires the independence and professional format of the Board and its members. The only value they are committed to is the corporate health and prosperity. They have to do everything to support this, which is what they are selected and paid for and that is what they have to be evaluated against. Good Corporate Governance boils down to ensuring efficient, high quality checks and balances within the company.

If we claim that strong, professional, high calibre Executive Management is to be put in charge it is at least as important and urgent to have an equally strong, professionally competent, high calibre and independent Board of Directors in place. With weak Boards, Executive Management acts without proper control, which means running high risks. On the other hand, a strong Board of Directors with a weak Executive Management will automatically be involved in day-to-day management to a large extent, which in turn jeopardises the key functions of the Board of Directors, namely the strategic as well as control and organisational functions. It is becoming obvious that top quality governance can only be achieved and maintained by forming top quality teams on either side, in other words the Board of Directors and the Executive Board.

Forming Boards of such quality and calibre initially requires the identification of the ideal skill and competence profile of the Board as an organisational body. Only after this has been done does it make sense to nominate individuals in line with the given criteria and requirements. Nominations of Board members and in particular the Chairman are some of the most important decisions in the life of a corporation, along with nominations of members of the Executive Board, especially the CEO.

In order to be able to cope with the given tasks and challenges the Board of Directors should have the following skills represented by its members:
- Broad general management experience gained holding P + L responsibility
- International experience
- Knowledge and experience in the business model of the company
- In-depth know-how regarding finance, controlling, balance sheet management, corporate finance
- Market orientation i.e. total control of up-to-date marketing mix instruments
- Know-how regarding up-to-date instruments in strategising, expertise in international alliance management
- Human Resources

When combined these profiles should form a Board of expressed skills, professional stature and high credibility. Most criteria for election to the Board involve convincing credentials in one of these areas.

Personal qualities like reliability, integrity, loyalty, charisma, communication skills and, last but not least, being an example of high moral and interpersonal standards are in addition to this.

Another important criterion is the independence of Board Members, meaning independence from each other and from the corporation on the Board of which they are serving. The credibility of the Board depends on the entire absence of any conflict of interest of its members.

Since the corporate culture in any organisation develops top-down it involves an example that is lived by the chairman, his or her Board colleagues, the CEO and his or her colleagues, and this determines the conduct throughout the organisation. The chairman has to be the guardian of corporate moral and ethics and must initiate immediate corrective steps if things start to go out off track.

For the maintenance of quality, professionalism and credibility at Board level, the Board should issue a code of conduct for the body and its members.
This code of conduct should commit the members in the following ways:

- full attendance at meetings;
- thorough preparation for meetings;
- active participation in Board meetings and open communication with Board members;
- active involvement in follow-up and follow-through actions to the results of meetings;
- absolute loyalty to the corporation;
- strict confidentiality regarding all Board matters; and
- the avoidance of any conflicts of interest.

This code is to be accepted and signed by each member and to thereby form an important element of Board members' evaluation. In the case of non-compliance with the code the Board member has to resign.

It is the Chairman's key task to make the Board work in a consistent, trustworthy, credible and efficient way. The Board's efficiency, quality of work and overall performance is by and large contingent on the way the Chairman carries out his duties. He has to generate an atmosphere of mutual respect and trust within the Board and between the Board and the Executive Management. He also has to be an example of the very moral and professional values he wants to see throughout the organisation. He has to emphasise and build on the strengths of the Board members and the members of Executive Management. He must make sure that the co-operation with employees' representatives is constructive and in the interest of the company.

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To fulfil his challenging tasks, the Chairman needs to be an individual of high personal and professional stature. Ideally, he is an ex-CEO of an important corporation and has also already served on Boards so he knows how they function. He should be somewhat detached from operative management, i.e. passed beyond it, in order not to feel tempted to interfere with executive management's areas too often.

The Chairman definitely has to offer enough available time and should be supported by adequate infrastructure within the company in the form of a Chairman's office.

In summary, we could say that based on today's experiences and existing trends an ideal system has to respect the core elements set out below.

In structuring this system, we should keep in mind that its quality and performance depends on the quality, skills, ethical standards and professional commitment of human beings.

If we apply the necessary criteria consistently, we will be able to develop the desired corporate governance which, in turn, leads to the desired corporate culture and performance.
Demands for more effective Boards involves a call for more effective governance, thereby improving corporate performance:

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- strict separation of the Board from Executive Management;
- non-transferable and non-withdrawable competencies of the Board:
  - organisation of the corporate management structure;
  - organisation of accounting and financial systems;
  - nomination and dismissal of Executive Management;
  - laying down of the corporate vision, approval of strategies;
  - giving Executive Management supervision and direction; and
  - defining standing orders and procedural rules between the Board and Executive Management;
- code of conduct for the Board;
- election of top personalities to the Board based on clear criteria (professionalism, track record);
- periodical review of the Board's performance / Board Members' contributions;
- a hierarchy of constituencies
  - the Board's top responsibility; and
  - Executive Management is in charge of operations along agreed strategic lines; and
- a balance of power and quality between Board and Executive Management.

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