



Lignum Vitae - "Tree of life"

The Risk & Regulatory Forum (TRRF)

A LOOK AT SOME OF THE ISSUES AND COMPLEXITIES OF IMPLEMENTING GOOD CORPORATE GOVERNANCE PRACTICES.

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The growing emphasis on corporate governance and its importance to the viability of an organization operating in today's global economy, will be the driving force to effect the necessary changes in how business enterprises respond to the need for greater accountability and transparency in the management of their organizations. Corporate governance is not new to most large organizations. Public listed companies and companies operating within the financial services sector are required to adhere to corporate governance guidelines that are issued by the Regulators. In its simplest form, corporate governance practices may have been implemented in other organizations, however, the quality of governance and the extent to which it is monitored and enforced may have relegated it to a lesser corporate framework.

Corporate governance may be described as the system by which business corporations are directed and controlled. Good corporate governance practices places the responsibility of the governance of the organization with the Board of Directors. The thrust for increased adoption of good corporate governance principles and practice is not only in response to the role it has played in the demise of public conglomerates both locally and internationally but is also being considered due to the benefits that will accrue to both the company and the country as a whole as a result of our changing environment and how business is conducted.

Globalization and people's access to information has increased the expectations of stakeholders who are now demanding greater accountability and transparency. This is evident in the promotion of corporate governance in commonwealth countries by the Commonwealth Association for Corporate Governance (CACG). In Jamaica, The Private Sector Organization of Jamaica (PSOJ) is leading the process to increase awareness of effective corporate governance in both public and private sector organizations and to establish best business practice corporate governance guidelines for Jamaica.

The guidelines being promulgated are neither mandatory nor prescriptive and are designed to be flexible and responsive to new developments. It is an accepted fact that there are differences in business enterprise, the industry in which they operate their ownership structure and their markets among other factors. It is also accepted that all the policies and practices may not be relevant or suitable to some businesses enterprises. However, there are certain issues that are common to all businesses and the policies could be modified to ensure adherence to the guidelines.



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In evaluating and monitoring whether good corporate governance practice is being implemented, the following highlight some of the issues that may arise and should be considered:

The requirement for independent/non-executive directors

Best practice governance principles recommend non executive directors in the composition of the Board. The non executive directors should be independent and should be able to and be prepared, where necessary to express disagreement with colleagues on the board and to bring independent judgment to bear on issues identified without the fear of being maligned or dismissed.

Independence may be seen to be achieved where there is no relationship to the organization and its management that would interfere with the exercise of the director's autonomy from the organization and its management. This also means that the personal interests of a director, or persons closely associated with the director, must not take precedence over those of the corporation and its shareholders.

Boards comprising solely executive directors may need to reassess their composition in light of these factors.

How do we retain and attract the right directors?

According to the CACG Guidelines on Corporate Governance, "New directors should be familiarized with the corporation's operations, senior management and its business environment and be inducted in terms of their fiduciary duties and responsibilities as well as in respect of the board's expectations. If new directors have no board experience, they should receive training in their unaccustomed responsibility which carries with it significant personal liabilities."

The increased scrutiny of the duties and responsibilities of directors will require directors to pay closer attention to understanding their role and their ability to add value to an organization. This increases their reputational risk and may result in directors turning down offers to sit on corporate boards. Directors may also demand additional compensation for the additional time that will be required to execute their duties effectively. Therefore director remuneration will have to be given more consideration in light of these factors.



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How are directors performance evaluated and who will perform the evaluation?

While the boards of most companies are evaluated as a whole by regulators or external parties, there may be a need for a formal process in place to independently assess the performance of individual directors in accordance with the guidelines. This will be a challenge for some companies due to the composition of the board and the sensitivity of the issues involved. The primary purpose of these so-called boardroom "health checks" is to assess whether the board has the right mix of proficient directors whose source of inspiration and advice will add value and should not be seen as a process to single out individuals for public humiliation.

Organizations which have implemented corporate governance practice have overcome this in a number of ways by using external auditors, the peer review process (by fellow directors), non-executive directors to perform individual evaluations. This may be new to some organization and directors who have served the companies for a number of years may not gladly "buy in" to such a process.

Directors with significant influence/dominant - how will this be addressed?

In our society, situations where directors are appointed to a board at the instigation of a party with a substantial interest in the corporation are not unheard of. Efforts to reform such practice will certainly be challenging where the directors' dominance and influence results in the organization being operated according to their dictates. The situation is compounded if the director has controlling interest in the organization. Such situations, as seen in the Parmalat case, could be detrimental to the long term survival of any organization.

Documentation and evaluation of the governance practice. Will this have to be monitored by an external party?

To be effective, the system of corporate governance should be clearly documented and effectively communicated to the appropriate internal and external stakeholders. A properly documented corporate governance framework will define amongst other things, the role of management(day-to-day management and execution of strategic plans and programs) versus the functions of the board(responsible for oversight);define independence of directors and outline the composition of the board; the size of the board and the process for the selection of directors; ethics and conflicts of interest; succession planning; mandate of the board and each committee; and evaluation of the board, committees of the board, individual directors and senior management.

The ability to effectively monitor and evaluate good corporate governance practice is largely dependent on the level of documentation in place. The level of documentation may vary depending on the organization and will be a challenging process for some



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organization due to their practice over the years of not documenting certain issues including adequate notes on minutes of meetings together with supporting board papers. This will be even more difficult if there is requirements to have external parties evaluate the process.

Board appointments; are these in line with all aspects of the best practice?

According to the CACG Guidelines on Corporate Governance, “The board should be composed of people of integrity who can bring a blend of knowledge, skills, objectivity, experience and commitment to the board which should be led by a capable Chairman who brings out the best in each director. Crucial to this, is having a proper director selection process to avoid the propensity for “cronyism” and “tokenism”. The selection process must be managed by asking what skills are needed on the board to add value to the processes of the board in the context of the business of the corporation. Consequently, the composition of the board should be planned with strategic considerations and objectives of the corporation in mind.” This guideline will impact the existing corporate culture of some companies and questions as to the availability of willing participants will in no doubt arise.

The implementation of good corporate governance practices will in no doubt give rise to some sensitive and complex issues that each organization will have to face. These issues may require significant changes to how business is currently organized and managed and may also challenge their commitment to the process.

Notwithstanding the foregoing, adoption and adherence to the guidelines recommended will be relevant to the long term survival of the organization. Let us not allow the challenges of implementation that will be faced in the short term to stifle the long term benefits that will be created for not just the organization but the country as a whole. It is also important that effective, prudent and ethical management is not sacrificed for increased profits, and regulation does not become a hindrance to the ability of organizations to operate efficiently and profitably in order to remain viable.

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