

Governance and Management

The Perennial Debate

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Research report by



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1. History

The debate on corporate governance is not recent. One of the earliest recorded studies dates back to 1932. In *The Modern Corporation and Private Property*, Berle and Means referred to the shift of control when a company's ownership gets dispersed. The need to create and activate structures and processes by which the investors and owners can ensure appropriate governance and management came in to focus.

In May 1991, the Conservative Government of the United Kingdom appointed "The Cadbury Committee" to address "...the financial aspects of corporate governance". The Committee was setup in the wake of a series of corporate scandals and failures during the late eighties and the early nineties - Ferranti International PLC, Colorol Group, Pollypeck International PLC, Bank of Credit and Commerce International (BCCI) and Maxwell Communication Corporation, to name a few. These failures were popularly attributed to weak governance systems, lax Board oversight, and the concentration of control in the hands of a single top executive.

The Cadbury Committee's report is embodied in "Code of Best Practices", an important document in the ongoing debate on governance. According to Cadbury, the emergence of global markets and pressure for Board accountability and performance are the driving forces behind today's worldwide interest in governance. While the publication of Turnbull Guidance in September 1999 gave further impetus to the corporate reformation movement, it was the US corporate turmoil symbolized by Enron in early years of the current century that sent the regulators scurrying to establish governance practices and guidelines in the Western world. The rest of the world was quick to follow.

2. What is Governance?

Governance" – a word derived from the French *gouvernance* – was first used in English by Chaucer and refers to the exercise of authority and control. The Cadbury Committee defined it, as "... the system by which companies are directed and controlled..." through the systems and processes. The OECD (Report on Corporate Governance, 1999) describes governance as involving "...a set of relationships between a company's management, its Board, its shareholders and other stakeholders..." Most definitions agree that governance deals with how organizations are structured and managed to lead to effective performance in achieving desired outcomes and satisfaction of stakeholders.

3. Why Governance?

There is convincing empirical evidence that good governance is the key to good organizational performance. A paper by Harvard and Wharton business professors entitled "Corporate Governance and Equity Prices"¹ analyzed 1,500 US companies and ranked them based on 24 corporate governance provisions.² Those companies with the lowest rankings were less profitable and had lower sales growth. Moreover, the returns on these companies lagged far behind those of higher ranked firms. In its 'Global Investor Opinion Survey' of over 200 institutional investors first undertaken in 2000 and updated in 2002, McKinsey found that 80% of the respondents would pay a premium for well-governed companies.

The roots of most corporate failures can be traced to bad governance. "Enron Board's worst failure", governance experts say, "was to overlook the dual role of the Company's CFO who reaped \$30m by simultaneously running limited partnerships that did business with Enron. This should have been a red flag to the Board. Having your CFO on both sides of a transaction reflected badly on the judgment of management."

The Enron collapse is also an example of misleading financial reporting. Enron concealed huge losses by creating illusions that a third party was contractually obliged to pay the amount of any losses. However, the third party was an entity in which Enron had a substantial economic stake. Arthur Andersen had lucrative consulting contracts with Enron and were only too pleased to let the Enron management have their way.

As organizations, particularly not-for-profits, take on more and more community responsibilities, the task of the Board becomes increasingly complex. To deal with expanding responsibilities, and the more complex operating environment, Boards must focus on what is important during the limited time they get together. The framework must address both conformance and performance. An effective governance system with balanced focus on compliance and results is quite difficult to develop and implement, yet critical to ensure that the Board meets its accountabilities.

4. Governance and Management

The line that separates governance from management is very fine. There is almost unanimous view among management experts that governance is in the domain of the Board (of governors/ directors/trustees) while execution is in the domain of management.

¹ Paul A. Gompers, (Harvard Business School), Joy L. Ishii (Harvard University), Andrew Metrick, (The Wharton School), February 2003

² Includes US corporate charter/bylaws provisions plus coverage under certain state takeover laws. (See Attachment 2 for a listing)

The Board is the strategic engine of every organization. It defines the mission, shapes the organization and steers it into the future. The Board sets corporate objectives, approves policies governing day-to-day operations, and oversees the implementation of those policies through the management. The Board is responsible for the organization's long-term success or failure.

There is no universally accepted point where governance ends and management begins. It varies with the organizational characteristics. It is up to each Board to establish a distinct point of delegation applicable to its own organization. It is important for the organization to articulate clearly where they are heading and why, and relate their objectives to appropriate governance structures, especially tailoring what they do to their uniqueness and the societal values they attempt to uphold.

In corporations, the owners (shareholders) delegate the rights to make decisions to the CEO who is expected to act in their best interests. So ownership is clearly separated from control. To define and control the actions of managers, owners establish a system of governance through the Board of Directors.

The Board's accountability to the organization's stakeholders³ is operationalized through governance. It is the link between management and stakeholders and is potentially the most effective instrument for good governance.

The simplest difference between governance and management is:

- The governance framework is responsible to ensure through oversight of management that appropriate management systems are in place.
- Management is responsible to establish and maintain policies and procedures that would contribute to the orderly and efficient conduct of the organization's business

Clear understanding and demarcation between governance and management is critical to the long-term success of the organization. The Board has to establish policy and the management has to implement it. Problems do arise when the responsibilities of the Board and management are not defined. Maximizing the performance of an organization requires an effective partnership between the Board and management to guide both strategy and performance.

³ There is a subtle difference between "stakeholder" and "shareholder". In this paper, however, both are used interchangeably. In the CGIAR context, the term stakeholder is generally used to include NARS, Farmers' Organizations, NGOs, ARIs, IARCs, Donor Community, Private Sector, Regional organizations and the CGIAR system.

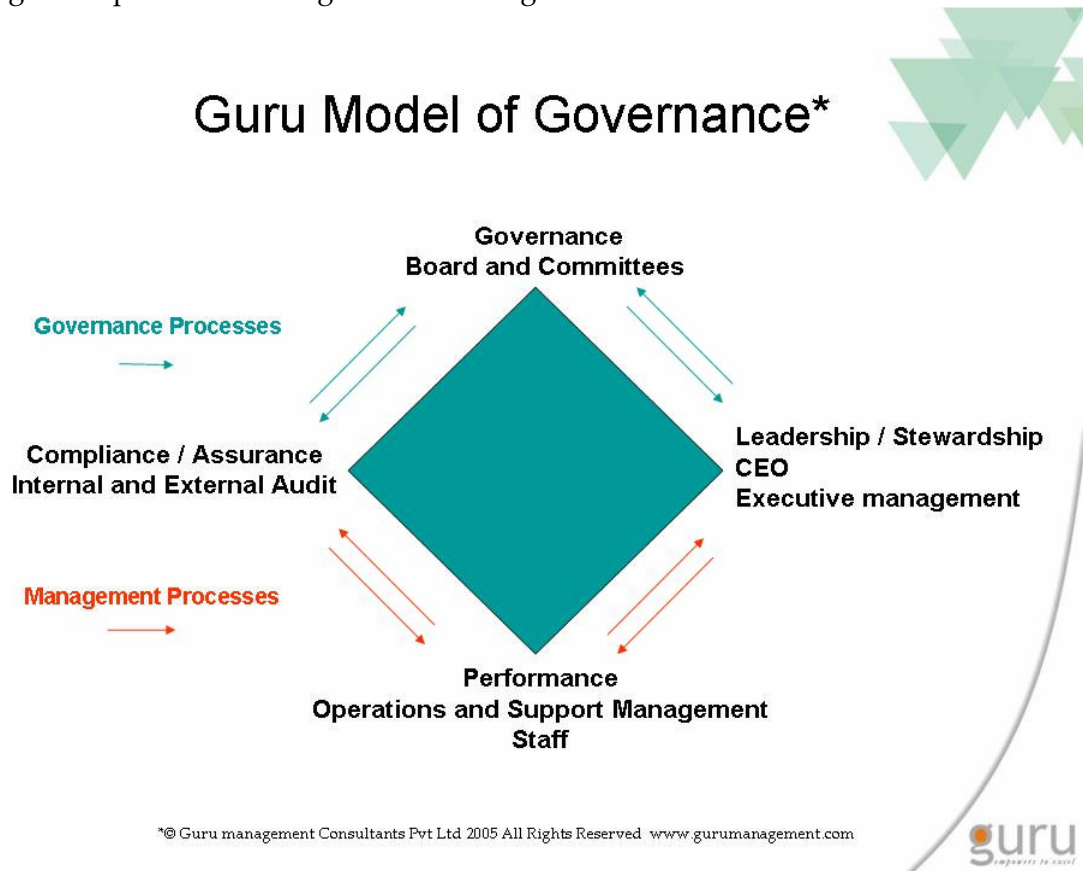
Effective governance therefore includes:

- Defining roles clearly and ensuring that they are well understood by all concerned
- Constructive relationships and accountabilities based on those roles.

Ultimately, the Board is totally accountable to the stakeholders. If a particular area falls under management's responsibility, the Board cannot consider itself absolved of its responsibility to scrutinize and monitor the area. The Board shall always remain responsible for the overall stewardship of the organization and must be ready to proactively question, scrutinize and monitor the performance of management.

Guru Model of Governance⁴

The Guru Model of Governance defines and describes the links between governance and management processes amongst the following four critical teams:



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- The Board and its committees form the Governance Team. The Governance processes mostly involve the two groups: Compliance Team and the Leadership Team.
- The Leadership Team comprises of the CEO and the Executive Management. The Leadership Team is actively involved through governance processes with the Governance Team and through management processes with the Performance Team.
- The Compliance Team, comprising of the internal and external auditors, is actively involved in the governance processes with the Governance Team and through management processes with the Performance Team.
- The Performance Team comprises of staff members, operations and support management. This team is responsible for delivery and actively involves with the Leadership Team and the Compliance Team through management Processes.

5. Governance in the CGIAR System

CGIAR Centers have significant differences from other public and private sector enterprises. They have distinctive accountability requirements to the donors and to the community. They need to maintain autonomy and to protect and enhance scientific and academic freedom of staff. Increasing competition for resources has seen donor community looking closely at the way Centers are governed. DFID's funding strategy, for instance, insists on yearly Board statement on governance.

Senior managers and scientific community in CGIAR often fear the dilution of autonomy or power when governance issues are raised. The most important reason for putting governance arrangements of CGIAR Centers is that for the long term sustainability of the CGIAR Centers, retention and expansion of donor support is critical. To ensure this, they must not only operate and be governed effectively but should also be seen to be doing so. The key challenge is to devise governance structures that assure a well- run and managed center that respects the need for scientific independence and effectiveness.

One of the most common problems the CGIAR system faces is the lack of focus on strategic issues. Boards in the CGIAR system, comprising members with scientific background, tend to get over-involved in the intricacies of research agenda and its implementation. This often reduces the Board activities close to program management. Boards should avoid micro-managing operations and instead, provide guidance and oversight on direction and strategy.

CIMMYT – A case in point

CIMMYT's 5th EPMR squarely blamed the Center governance for most of its troubles. A very significant factor contributing to the turmoil CIMMYT has been undergoing is the breakdown in financial management, which reached a critical point in 2002. A look at the CIMMYT Board composition would show why. During the period 1998-2005, among 26 persons who served on the CIMMYT Board, there was not one member with specialized skills in the field of Finance. While the Center was going through the trauma of financial mis-management, the Board could only watch silently what was going on. According to the EPMR Panel, *"... Collectively, the Board, which carries ultimate responsibility for maintaining adequate internal controls, failed in its oversight role of the Centre's finances and management. The cost of this failure was borne not by the Board but by the staff and Programmes of the Centre..."*

The EPMR highlighted the System's heightened attention to Center governance as well as particular concerns with the performance of CIMMYT's Board in recent years.

The review also revealed an awkward fit between the accepted standards within the system for evaluating the governance function and the demands that CIMMYT's growing organizational complexity places on its Board.

According to the EPMR Panel, *"...It is no longer functional and may be counterproductive to make oversight of science and research a primary role or responsibility of the Board. While this is a responsibility that cannot be wholly relinquished by the Board, it can be managed more efficiently in other ways, for example, through CCERs, a higher level of Board engagement in the results of the EPMRs, and the use of task-specific scientific advisory groups, rather than through building a Board with a depth and breadth of research related expertise that mimics staff capacity and duplicates checks and balances available elsewhere, including the CGIAR system, the professional culture of the sciences, and the competitive market for resources..."*.

The Panel went so far as to recommend abolition of the Program Committee of the Board and substituting it with a Scientific Advisory Committee (SAC), which could advise the Center and Board on the quality of its science.

The Panel identified several areas of the Board's operations that required remedial attention such as

- The size, composition, and committee structure of the Board
- Board orientation and learning
- Board evaluation of the DG, the Board Chair, and itself
- Board oversight of the Centre's finances and resource development

The Panel particularly emphasized the need for a smaller and more compact Board and a more strategic approach to populating it.

It urged the Board to "...determine the expertise, networks, and skills that CIMMYT requires at the Board level to be an effective body, and recruit carefully against these criteria. In identifying new members, it needs to emphasize skills that relate to governance of a complex enterprise confronting challenging financial and strategic issues, and bring the level of expertise in finances, planning and management in balance with the current depth of Board experience in CIMMYT's program and research activities...."

In the new formulation of the Board's role, the Panel envisaged an emphasis on :

- Oversight and stewardship responsibilities for Center's financial operations, the prudent use of resources, financial stability, and financial sustainability
- Evaluation and decision-making that are strategic, well informed and forward looking
- A relationship with the DG that is collegial but rigorous
- A capacity to build resources and forge new relationships

A de-emphasis on

- Stakeholder representation as a role for the Board
- Direct Board oversight of the research agenda, scientific outputs, and the quality of science

The governance issues raised by the EPMR panel are not unique to CIMMYT and could well be very valid for other CGIAR Centers in varying degrees.

6. Elements of Governance

Governance today means not so much what organizations do but how they do it. It is about how an organization steers itself as well as the structures and processes created to achieve its goals. It influences how the objectives of an organization are set and achieved, how risk is monitored and assessed, and how performance is optimized.

The major elements of Governance are described below:

6.1 Authority and accountability

Governance is oriented towards setting and enforcing boundaries. It is concerned with structures and processes for decision-making and with the controls and behaviors needed to support effective accountability for performance outcomes and results. They include:

- Defining and monitoring the strategic direction
- Defining policy and procedures to operate within the economic, legal and social requirements
- Establishing control and accountability systems;
- Reviewing and monitoring management and the organization's performance; and
- Risk management

As the Board is responsible for directing and controlling the organization on behalf of the stakeholders, it is ultimately accountable for its own performance as well as that of the organization. The governance framework should clearly identify and articulate the responsibility as well as the various relationships between the organization's stakeholders and management.

6.2 Strategic Leadership

The Board is responsible for the stewardship of the organization, setting its overall strategic direction and overseeing the management of its business. The stakeholders have ascribed importance and leadership to the Board to play the critical role of the strategist. Leadership also involves clearly defining the values, standards, and culture of the organization and the expected behavior of staff members.

6.3 Behavior

Organizations operate in an environment of trust by the stakeholders and the community. Its reputation is its most valuable asset. To nurture reputation, the organization must maintain a high level of integrity and propriety in its dealings. This requires a clear code of ethical behavior and personal integrity exercised by the Board, management, and staff and these being openly and continuously communicated to the stakeholders. This promotes ethical and responsible decision-making.

6.4 Social Responsibility

Even the private sector is actively adopting greater social and community responsibilities. Boards are beginning to recognize that being seen as 'good corporate citizens' is integral to the long-term viability of an organization and, therefore, of primary interests to the stakeholders. The result is that organizations are responding to public concerns to enhance the confidence of community and stakeholders

6.5 Transparency

Organizations should clarify and make publicly known the roles and responsibilities of Board and management to strengthen the faith of the stakeholders. They should implement procedures to independently verify and safeguard the integrity of the organization's public disclosures, especially financial reporting. Disclosure of material issues concerning the organization should be timely and balanced to ensure that all stakeholders have access to clear and accurate information.

6.6 Control

Governance is the organization's strategic response to risk. Appropriate levels of control promote effective performance and ensure that accountability and compliance obligations are appropriately discharged. They facilitate effectiveness by enabling the organization to respond appropriately to significant business, operational, financial, compliance and other risks. A robust system of risk management should complement and underpin the administrative control systems.

6.7 Effectiveness

Governance, whether in the corporate or not-for-profit sector, must ensure effectiveness as its key accountability to maximize stakeholder value. Therefore, it becomes necessary to balance the varying interests of the stakeholders and make decisions that contribute to the overall efficiency and effectiveness of the organization. Governance serves its purpose only when it results in effective accomplishment of goals, sustainability and growth of the organization. The decision-making processes, critical to the delivery of corporate objectives, are of paramount significance.

The real challenge is not to define the elements of effective corporate governance but to ensure that all the elements of good corporate governance are effectively integrated into a coherent corporate approach. The other challenge is to ensure that this is well understood and applied throughout the organization.

7. Governance – Critical Success Factors

*The Board need not and should not control everything,
but it must control the definition of success.*

While good corporate governance will not assure corporate success, it does provide the sound platform essential for organizations to perform. The following factors substantially increase the effectiveness of Boards

7.1 Ability to function independent of Management

The underlying theme of an effective governance structure is the ability of the Board to function independent of management. The Board has the responsibility to appoint and monitor management. This also creates the stakeholder perception that the Board is independent and operates at a level higher than management. So the Board has to put in place appropriate structures and procedures to achieve and project its independence, with a clear demarcation of its responsibilities from those of management and ensure an effective accountability regime.

7.2 Guiding the Strategic Plan

Management is accountable to create a framework to manage staff. The CEO, with the active involvement and overview of the Board, is responsible for leading the organization into the future and must, therefore, take the initiative of setting the vision and long and short-term goals. (S)he must ensure that an appropriate strategic planning process is in place and take the lead in proposing a strategic plan and the specific objectives to be achieved. The Board will bring to bear its breadth of judgment on the plan and provide an objective assessment. In a good governance system, the Board approves the organizational objectives and strategic plan with appropriate measurable benchmarks, which are then entrusted to the CEO to achieve. Board is responsible to monitor management's success in implementing the strategy and achieving results. This approach provides a clear division of responsibilities between the Board and management and sets out the basis for measuring the CEO's effectiveness.

7.3 Board Members acting as Delegates

A significant weakness arises from the composition of the Board when members are chosen as representatives of various sectoral interests or constituencies. The Board members have the over-riding responsibility to bring diverse viewpoints together for the advancement of the institution rather than represent sectoral interests. Robert Smith is of the view that governing bodies cannot effectively discharge both responsibilities and that members must represent the organization as a whole, and not be advocates for a particular group of constituents or of a particular viewpoint. (Smith, 2000). It is difficult for Boards to function effectively when there is no agreed understanding on the difference between the "trustee" and "delegate" roles. Board members should be drawn from a worldwide pool of diverse skills with a clear understanding of these roles and the induction and training must continuously reinforce this difference.

7.4 Avoidance of Information Overload

One of the largest impediments to focused meetings is the tendency to flood the Board with reports and presentations, often for information. While it is nice to know everything, and while some of them may be relevant to decision-making, the Board meeting is the wrong venue for their presentation. Reports on past events should be sent

in writing along with the agenda package. Then they can be read at the Board's leisure and the Board will already know the information they contain before they have to rely on it for making decisions. Setting of unrealistically large number of items on the meeting agenda also adds to this overload and decreases the effectiveness of meetings and the decisions made.

7.5 No Over-reliance on CEO

The Board is accountable for the CEOs work, but the converse is not and should not be true. However, the 'Board-staff inversion' is very common. The CEOs drive Board meetings through the agenda provided by them, control of information flow, and in worst cases through distortion and fallacy. In such models, according to Herman and Heimovics (1991), "...the Board's performance becomes the executive's responsibility... a position we contend excuses and prolongs Board irresponsibility..."

7.6 Non-involvement in Staff Management

Some Boards tend to get involved in staff/management issues and conflicts, which is undesirable. While Board members have a responsibility to understand union negotiations or conflicts with management, putting themselves in the middle can seriously damage the leadership and create irreversible and long-term damage to the organization.

Such practices allow CEOs and Board members to interfere in areas where they should have no role. Board members may begin to interfere in the day-to-day operations of the organization. Micro managing by Board members undermines the credibility of the CEO and sends conflicting messages to other senior managers, staff, and the public.

Conversely, CEOs can intrude on the responsibilities of the Board and make Board members feel their ideas and participation are not wanted. The Board's role might be marginalized to the point where the Board members become disengaged and apathetic, and serve only to "rubber stamp" management decisions.

7.7 Effective Risk Management

The Board must ensure that the operations of the organization are conducted in conformity with the laws and the organization's policies. Business decisions involve taking risks. The Board's must ensure that the organization's policies and systems are effective enough to achieve a prudent balance between the risks and potential rewards.

Management has the first level of responsibility for risk management through establishment of a comprehensive risk management process, which identifies, monitors, and controls different types of risks. The Board should critique and approve the risk management policies, systems, and procedures proposed by management to establish practical norms for different types of risk. The Board should also periodically review

management's performance in controlling the risks. Any departure by management from the acceptable norms should require approval of the Board.

Implicit in the effective discharge of the Board's responsibilities are the adequate functioning of a:

- Well-designed internal control, and
- Management information systems.

Board has to ensure that proper systems and controls are in place for tracking the performance criteria so that it can monitor the implementation of strategy. The Board must also ensure that there are proper systems in place to ensure the integrity, accuracy, sufficiency and timeliness of the data and information being produced and disseminated to various users.

7.8 Strong Audit Functions

The role of internal and external auditors is crucial to ensure an effective control environment. Management and the Board can enhance their effectiveness by ensuring that the internal audit function is duly recognized in the organization and profiled accordingly.

Some measures that could support this approach are:

- Raise the profile of the audit function by highlighting its contributions
- Appoint the head of audit at a senior level reporting directly to the CEO
- Enhance the auditor's independence by providing him/her with direct access to the audit committee and the Board
- Staff the audit unit with qualified and experienced professionals
- Ensure timely action on suggestions and deficiencies identified by audits

7.9 Honest Self-Evaluation

Board's role in governance is incomplete without periodic and honest evaluation of its functioning both individually and collectively. Individual directors can be evaluated on their level of attendance, participation at Board meetings, on their knowledge and understanding of the organization's vision and strategy, and on the quality of their performance. Key to evaluation of the Board as a whole is careful appraisal of the quality of the Board's processes, its composition, and its commitment. The critical questions involved in Board evaluation are:

- ✓ Is every director, executive, and non-executive, wholly committed to the concept of accountability of the Board as a whole, primarily to its shareholders but also to its other stakeholders?
- ✓ Do Board members act as a team rather than as advocates of particular sectoral or functional interests?

- ✓ Is every member of the Board free to question and challenge corporate leadership on any matter? Is this freedom exercised, and is it actively fostered by the Chairman?
- ✓ Does the Board regularly define and validate its responsibilities to its stakeholders – vision, mission, values, timescales - setting and reviewing policies, goals, and standards?
- ✓ Does the Board regularly discuss and review its long-term visions and strategy for the organization; and commit to clearly defined corporate plan?
- ✓ Are the agendas, papers and forms for Board meetings constructed with relevance, timeliness and appropriate information; and with the aim of exposing the issues and presenting options rather than single path recommendations?
- ✓ Does the Board's composition include depth of knowledge of the business and of its functions, and breadth of experience, background, age and gender?
- ✓ Are the non-executive directors sufficient in number and weight that their views cannot be ignored?
- ✓ Does the Board have appropriate mechanisms for the appointment of top executive management, for reviewing the performance and remuneration of all directors, and of ensuring an open interface with its auditors and other professional advisors?
- ✓ Given that the stakeholders cannot in practice hold the Board to account against these criteria, does the Board review its own performance, including that of the Chairman, and identify the issues impeding full effective corporate governance?

It is not easy for a Board to judge itself, but it should make sincere attempts to do so. Better still that the Board seeks external help, with all the advantages of objectivity, in reviewing its effectiveness against the proper criteria. Such a review, however it may be conducted, will identify issues and provide an agenda for action.

8. Roles and responsibilities of the Board

All authority vests with the Board until delegated to others. The Board generally uses a single point of delegation – the CEO – and holds this position accountable for meeting all the Board's expectations for organizational performance. In effect, the authority and accountability granted by the Board to the organization tend to be actually granted personally to the CEO.

It is important to clearly distinguish the roles of the Board from the duties of management. For example, in strategic planning, a Board should not involve in the actual development of strategy. The role of the Board is to oversee and bring an independent and objective view to management's proposals and decisions.

But to establish and maintain the organizational culture, a Board must be proactive in ensuring that the organization's ethics are sound and meet the standards of the law.

Following is an indicative list of Board responsibilities:

- **Strategic Direction and Oversight**
 - Set organizational vision, mission, and strategy.
 - Keep abreast of the major trends impacting on the organization and its major risks and opportunities.
 - Ensure periodic environmental scans are conducted to identify shifting macro trends and analyze their implications for the strategic sustainability of the organization.⁵
 - Define the organization's ethical values and behavioral standards and promote them
 - Ensure organization's long-term financial viability
- **Control and Compliance**
 - Provide clarity on management roles and responsibilities by delegating to the management the day-to-day operations and then holding it accountable for overall operations
 - Approve business plan, budget and policies
 - Approve key performance goals (KPGs)
 - Evaluate management and organizational performance on an on-going basis⁶
 - Ensure that a system of internal controls and risk management framework are in place⁷
 - Ensure compliance with various laws, regulation and standards
 - Approve annual accounts, annual report and other public disclosure documents
- **Appointments**

⁵ This may warrant periodic review of the strategy vis-à-vis the organizational vision and mission. Such reviews are ideally undertaken to synchronize with the organizational medium-term plans, which typically cover a 3-5 year cycle.

⁶ Apart from yearly reviews, a mid-year review would provide opportunity for timely corrective measures as needed.

⁷ Management should be asked to provide assurance to this effect every year. The Audit Committee also plays an important role as they are provided an independent evaluation by the internal and external auditors.

- Appoint, plan succession, assess performance, decide remuneration and change CEO as required
- Appoint auditors and new directors
- **Managing Stakeholders**
- **Effective communication with stakeholders.**
- **Conduct Self-evaluation**
- **Role Model the values**

9. Roles and Responsibilities of Management

Following is an indicative list of the responsibilities of management:

- Recommend the strategic direction
- Implement approved strategy and deliver the agreed results. Develop business plans and obtain Board approval
- Ensure compliance with laws, regulations, and standards.
- Develop, implement and manage the organization's risk management and internal control frameworks
- Develop, recommend, implement, and update policies and procedures
- Stay updated regarding trends in the industry and the organization's operating environment
- Ensure proper information flow to the Board.
- Develop healthy and synergistic relationship with the Board
- Optimize the use of the organizations human, physical and financial assets to achieve the organization's objectives.
- Implement and role model the value system

10. Models of Governance

There are different governance models accepted and practiced worldwide. They differ according to the socio-economic environment in which they are embedded. The liberal model that is common in Anglo-American countries tends to give priority to the interests of shareholders. The coordinated model that one finds in Continental-Europe and Japan also recognizes the interests of workers, managers, suppliers, customers, and the community. Both models have distinct competitive advantages, but in different ways.

The liberal model of corporate governance encourages radical innovation and cost competition, whereas the coordinated model of corporate governance facilitates incremental innovation and quality competition.

10.1 The Tricker Model⁸

This model defines governance by delineating the role of the Board in the process as shown in the following grid

The Tricker Model – Board Functions

	Compliance Roles		Performance Roles	
External Role	Provide Accountability ●●Report to Shareholders ●●Ensure legislative & regulatory compliance ●●Review audit reports		Strategy Formulation ●●Initiate & review strategic planning ●●Set corporate direction ●●Determine strategy	
		Appoint and work with & through the CEO		
Internal Role	Monitoring & Supervising ●●Executive performance ●●Review results ●●Monitor budgets ●●Investigate and check corrective action		Policy Making ●●Approve budgets ●●Determine remuneration policy for senior executives ●●Decide corporate policy ●●Create corporate culture	
	Past & Present		Future Oriented	

10.2 Guideline-Based model

Guideline-based models mean a set of standards or guidelines prescribed by someone, putting in place rules that companies are supposed to follow

John Carver's Policy Governance is perhaps the single most popular model of corporate governance, having been adopted widely in the not-for-profit and co-operative sectors. At its heart, is the premise that *Boards must focus on the ends and management on the means*. Boards achieve this by developing and approving policies, and then holding management accountable for effectively operating the organization within these parameters.

⁸ Source: Professor Geoffrey Keil, *Improving Board Effectiveness*, 2001

Management implements and acts.

This model enables the Board to focus on the larger issues, to delegate with clarity, to control management's job without meddling, to rigorously evaluate the accomplishment of the organization and to truly lead the organization. In contrast to the approaches typically used by Boards, Policy Governance separates issues of organizational purpose (Ends) from all other organizational issues (Means), placing primary importance on Ends. Ends are about the organization's impact on the world that justifies its existence. *Board is not charged with producing ends, only with defining them.*

10.3 Principle-based Model

A second broad approach, principle-based models, focuses on identifying overarching principles of governance, then encouraging Boards to evaluate and choose their own best practices using these principles as foundations and filters. The World Bank, OECD (Organization for Economic Cooperation and Development), and The Conference Board of Canada, among many others, have adopted this approach.

Different countries have developed different systems or models for governance. The differences between the Anglo-American and German system are often discussed. In the German economy, the owners looked for good investments but were not much interested in managing enterprises - they simply tried to supervise the business results. In contrast, in England, and the US, capital was scarce. Risk-taking owners were interested in profits. They did not only supervise, but they also managed. Their role of directing companies was more active than in Germany where it was limited to a supervising function only. In the US, the governing and managerial roles have been more often conducted jointly by the same persons, thus treated by many authors as one function. One of the consequences of the different development (and different culture) is that in the US, the roles of different bodies are decided upon at a higher degree by owners themselves, whereas in Germany, they are more or less determined by law. *For that reason, managers are more responsible to owners in the US and more to the law in Germany.*

In the Anglo-American model, there are two governing bodies: the shareholders' meeting and the Board of Directors. In the German model, there are three governing bodies: the shareholders' assembly, the supervisory Board (*Aufsichtsrat*) and the managerial Board (*Vorstand*). The shareholders' meeting and assembly are rarely emphasized, due to their formal and less important role. Governance in the Anglo-American model is conducted entirely by the Board of Directors (one tier system). In the German model, governance is conducted by two bodies: the supervisory and the managerial Boards.

10.4 Not-for-profit vs. Corporate Model

It is interesting to compare the corporate model of governance with the not-for-profit model. While the not-for-profit model stresses the values of community participation, due process, and stewardship, the corporate model stresses the values of strategy development, risk-taking, and competitive positioning as shown below:

Not-for-profit Model	Corporate Model
Large Board size	Small Board size
Wide range of perspectives/backgrounds	Narrow, more focused perspectives/ backgrounds
Small number of inside directors	Large number of inside directors
Separation of management and governance	Active management participation on Board
Meets less Frequently	Meets more frequently
Informal management	Formal management
Emphasis on asset and mission preservation	Emphasis on strategic and entrepreneurial activity

11. A Competency Model for the WorldFish Board

One of the major reasons why Boards have not been able to provide effective governance to CGIAR Centers is because, very often, for the sake of providing representation to diverse interests, considerations of competencies of the Board members are compromised.

Not-for-profit organizations are moving away from constituency-based membership in favor of members with the objectivity, commitment, and expertise to make decisions in the best interests of the entire system, its mission, communities, and other stakeholders.

Being at the heart of corporate governance, the composition of the Board becomes extremely critical in charting the course and future of an organization. The Boards must have a judicious mix of diverse competencies and experience. Another significant factor is that Board members require experience and competencies relevant to governance and not management.

While it is relevant to define roles and responsibilities for individual Board members, it must be derived from the overall roles and responsibilities of the Board as a group and not the other way around. Hence, Board practices must recognize that it is the Board, not Board members, who have authority.

To fill Board vacancies, it is important to understand the total skills, competencies, and capabilities that the Board needs as a body. The current Board is probably in the best position to advise on the skills and competencies required of Board members, the

complementary skills needed, and the skills gaps to be filled with new appointments. Current Boards must produce profiles that specify the experience and competencies of the current Board, those required to complement the existing Board, and those needed in the future. Board members should not be recruited based on profiles that mirror the skills of CEOs and senior executives.

Boards are often made up of remarkable individuals possessing an impressive array of management and other skills. However, the truly effective Board member never lets individual personality, no matter how brilliant, dominate the governance process. Instead, they encourage *group decision-making, teamwork, and a sense of shared purpose*. It creates collective goals for the Board - and collectively shares the glory or shame of evaluation according to these stated aims. The Board fosters a sense of inclusion and shared mission among Board members and extends this sense of fellowship to the management and stakeholders alike.

The Board of directors typically includes some members who have experience in the field of business. The Board also consists of members who do not have particular expertise in the field, but whose experience and knowledge in other fields of business or professions are considered valuable. Finance is one area, which could provide immensely valuable and much-necessary skills. Public Policy, Social Sciences and Management (with Governance background), Human Resources Management, Information Technology etc are other disciplines which add value to the skill mix of the Board. Regardless of the mix, the Board has to exercise a well-balanced approach to policy decisions.

The best Boards are possessed with the capacity for detachment. No matter how passionately committed individual Board members are to the organization's mission, they are able, as a group, to step back from situations and deal with problems analytically. This allows them to see the complexities in the issues they face, and to draw on multiple perspectives.

All Board members, even those elected by a particular interest group, lay aside their partisan views and try to consider the issues impartially in the light of what's best for the organization as a whole.

Competency Model for the Board

“Competency is an effective action or behavior”⁹.

The drivers of competency include Knowledge, Skills and Attitude. A suggested competency model for the Board of WorldFish is provided in Attachment 1. This model draws from the strengths of various models discussed in this paper.

⁹ “Competency Web The Corporate DNA”, N P Rajasekharan, Universities Press

Knowledge, skill, and attitude dimensions are captured in this model. These are characteristics the Board members should possess. While the list looks exhaustive, it is not essential for each Board member to have all the competencies. But as a group the Board must have all of them.

12. Operationalizing Competencies

Obviously, it will be almost impossible to find directors strong in all the areas. So organizations should conduct a competency mapping that results in a “value-creating competency profile” – a summary of the current capabilities of each director and key player on the management team. (Ziamba and Westman, 2003). Often, the value-creating competency profile identifies gaps in capabilities directors possess and the ones they lack.

In order to fill the gaps, Boards have these options:

- Add Board members with required competencies
- Replace current directors
- Develop the needed competencies in current members.

Board orientation, training and continuing education

New Board members need to be oriented to both the organization and their governance responsibilities to gain full understanding of their roles and legal and other obligations. While management training is devoted much attention, Board training is often neglected. Strategic competencies can be inculcated with focused training, and functional competencies can be honed by utilizing traditional education techniques. It is also important to support continuing professional updating of Board members on contemporary developments in business, regulatory, and other relevant areas.

13. Regulatory environment

Beginning with the Cadbury code in the UK, a series of legislative and regulatory guidelines have been introduced in various countries. A brief overview of the regulatory environment in select countries is given below.

United Kingdom: The recently (2003) reorganized Combined Code on Corporate Governance reflects the recommendations of the Higgs and Smith Reports, which were the products of working groups established to examine corporate governance practices and make recommendations. The Combined Code requires, among other things, consultation with shareholders and explanation when a chief executive becomes chairman of an organization’s Board, as well as independence criteria for Board members. Overall, greater disclosure requirements are intended to increase transparency.

United States: The US response to corporate governance movement is embodied in the Sarbanes-Oxley Act of 2002. Among the salient features of the Act are stipulations that

- Requires chief executive officers (CEOs) and CFOs to certify quarterly and annual financial reports and holds these officers responsible for restatements of results caused by misconduct.
- Redefines the relationship between external auditors and their client companies and makes audit committees directly responsible for those relationships and other aspects of corporate accounting and auditing.

European Union: In May 2003, the European Commission issued corporate governance action plan, which sets forth a series of legislative and non-legislative measures to be taken through 2009. The action plan does not propose a separate European code of corporate governance, but suggests a common approach on a number of key rules in areas such as corporate governance statements in annual reports, disclosure of risk management systems, Board and committee composition, shareholder rights, and relationships with major shareholders

In response to calls by OECD ministers, a revised version of its "Principles of Corporate Governance" was produced in 2004. First issued in 1999, this paper has provided the framework for regional corporate governance roundtables in cooperation with the World Bank around the world. It has been endorsed as one of the Financial Stability Forum's 12 key standards, and form the basis for the World Bank's Review of Observance of Standards and Codes.

India: One of the first codes developed in India was the Confederation of Indian Industries code for corporate governance developed in 1998 on the basis of Rahul Bajaj committee. Later, the Kumar Mangalam Birla code came into being in 2000 as a result of the committee headed by him at the behest of the Securities Exchange Board of India (SEBI). Also taking into account the recommendations of the Narayana Murthy committee in 2003, SEBI introduced clause No. 49 relating to corporate governance in the listing agreement, calling for, inter alia, transparency in governance and stringent reporting requirements.

The underlying spirit of corporate governance that runs through all the regulatory codes across various countries prescribe Board composition to include non-executive directors, transparency, and disclosure requirements especially in financial reporting and independent audit committees.

14. Conclusion

Good governance requires that principles, not just rules, guide the processes. The culture starts from the top of the organization, with strong emphasis on leadership, shared vision, ongoing commitment, effective mechanisms, continuous improvement, performance, transparency, and accountability. Governance is not only about establishing command and control structures for management but about empowering and enabling all people to develop their full potential and deliver to their maximum capability. It is about the creation of a framework of organization's vision, structures, and systems that embed the core values into its processes and which will ensure sustainable growth through synergistic interactions with all stakeholders.

Attachment 1

World Fish – Governing Board

Suggested Competency Model

Values

- 1 *Integrity* - Demonstrated high ethical standards and integrity in personal and professional dealings and willingness to act on and remain accountable for their Boardroom decisions
- 2 *Commitment* to the organizational mission – Genuine belief in the organizational mission and willingness to contribute to its accomplishment. The Board members themselves embody the organization’s core values.

Knowledge

- 3 Industry knowledge (CGIAR, Science Council, key stakeholders and their priorities)
- 4 In-depth understanding of WorldFish and the socio-economic context within which it exists
- 5 Awareness of the tenets of governance and contemporary trends in business and regulatory environment in which organizations operate.
- 6 Awareness (not necessarily expertise) of Fisheries, Agriculture Research and food & environment security issues
- 7 Awareness of public and social policy issues
- 8 An understanding of the threats, opportunities and trends that are relevant for WorldFish
- 9 Understanding of technology, including Information Technology
- 10 Understanding of current management trends and best practices

Skills

- 11 Financial acumen
- 12 Building and sustaining stakeholder relationships and networking
- 13 Policy development, analytical, financial, and decision-making
- 14 Identification and Assessment of risks

- 15 Provision of strategic insight and direction by encouraging innovation, and continuously challenging the organization to sharpen its vision
- 16 Objectivity : Ability to stand back and take objective decisions
- 17 Judgment: Ability to provide informed judgment and wise thoughtful counsel in the decision making process.
- 18 Leadership to attract, motivate and energize a high performance Leadership Team and to lead and support change management

- 19 Strong communication including patient listening

- 20 Multi-cultural sensitivity to respect, accept, and reflect on differing views and life experiences with regard to gender and ethnic diversity
- 21 Analytical reasoning and thinking
- 22 Managing group Processes and consensus building skills
- 24 Mature Confidence – Openness to the opinions of others, listen and comprehend and raise tough questions in a manner that encourages open discussion.
- 25 Business development and fund-raising

Experience

- 26 Professional skills and substantial experience including international experience

- 27 A track record of achievements that reflect high professional standards in business, industry or not-for-profit organizations

Attachment 2

List of 24 corporate governance provisions used by Gompers, Ishii and Metrick in their paper "Corporate Governance and Equity Prices"

1. **Antigreenmail** - Prevents accumulation of large blocks of stock, which manipulates control of companies.
2. **Blank Check** - Used as a takeover defense.
3. **Business Combination laws** - Prohibit certain kinds of transactions between a large shareholder and the firm.
4. **Bylaw and Charter** - Amendment limitations limit shareholders' ability to amend the governing documents of the corporation.
5. **Cash-out laws** - Enable shareholders to sell their stakes to a "controlling" shareholder at a price based on the highest price of recently acquired shares.
6. **Classified Board** - One in which the directors are placed into different classes and serve overlapping terms.
7. **Compensation Plans** - Allow participants in incentive bonus plans to cash out options or accelerate the payout of bonuses should there be a change in control.
8. **Director indemnification** - Contracts between the organization and particular officers and directors indemnifying them from certain legal expenses and judgments resulting from lawsuits pertaining to their conduct.
9. **Cumulative Voting** - Allows a shareholder to allocate his total votes in any manner desired, helping minority shareholders to elect directors.
10. **Directors' Duties** - Provisions allow directors to consider constituencies other than shareholders when considering a merger, which provides Boards of directors with a legal basis for rejecting a takeover that would have been beneficial to shareholders.

11. Directors' Duties laws - Allow similar expansions of constituencies, but in only two states are the laws explicit that the claims of shareholders should not be held above those of other stakeholders

12. Fair-Price - Provisions that limit the range of prices a bidder can pay in two-tier offers to prevent pressure on the target's shareholders to tender their shares in the front end of a two-tiered tender offer, and they have the result of making such an acquisition more expensive.

13. Golden Parachutes - Severance agreements that provide cash and non-cash compensation to senior executives upon an event such as termination, demotion, or resignation following a change in control.

14. Limitations on director Liability - Charter amendments that limit directors' personal liability to the extent allowed by state law.

15. Pension Parachutes - **PREVENT** an acquirer from using surplus cash in the pension fund of the target to finance an acquisition.

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16. Poison Pills - Provide their holders with special rights in the case of a triggering event such as a hostile takeover bid.

17. Secret Ballot - Helps eliminate potential conflicts of interest for fiduciaries voting shares on behalf of others, and can reduce pressure by management on shareholder-employees or shareholder-partners.

18. Severance Agreements - Assure high-level executives of their positions or some compensation and are not contingent upon a change in control (unlike Golden or Silver parachutes).

19. Silver Parachutes - Similar to Golden Parachutes in that they provide severance payments upon a change in corporate control, but differ in that a large number of a firm's employees are eligible for these benefits.

20. Special Meeting limitations - Either increase the level of shareholder support required to call a special meeting beyond that specified by state law or eliminate the ability to call one entirely.

21. Supermajority requirements - Charter provisions that establish voting requirements for mergers or other business combinations that are higher than the threshold requirements of state law.

22. Control-Share Acquisition laws - Laws that require a majority of disinterested shareholders to vote on whether a newly qualifying large shareholder has voting rights.

23. Unequal Voting rights - Limit the voting rights of some shareholders and expand those of others.

24. Written Consent - Establishment of majority thresholds beyond the level of state law.