



The Governance  
Institute

# Certificate in Corporate Governance

Discovery Pack



# Overview

This discovery pack has been created to give you an in-depth understanding of what is involved in studying for the Certificate in Corporate Governance.

The pack is divided into five sections:

- Introduction
- The short syllabus
- Study text sample chapter
- Tuition options
- How to register

## **Introduction**

The introduction tells you, at a glance, what the certificate involves. It provides key details such as entry requirements, study mode, content and benefits of the certificate.

## **The short syllabus**

The short syllabus provides more details about the certificate: key features and qualification structure.

## **Study text sample chapter**

We have included a chapter from the study text to give you a taster of the subject matter and format of the material that we provide to support your learning.

## **Tuition options**

We recommend our students take tuition and have a number of partners who are registered to provide tuition in person and through distance learning. We provide a list of our partners who deliver tuition for the certificate.

## **How to register**

The final section of this pack explains how you can register for the Certificate in Corporate Governance.

# INTRODUCTION

# Certificate in Corporate Governance

## Introducing the UK and international governance landscape

**Experience/qualifications:** No prior qualifications required

**Study mode:** Self-study, though tuition from one of our registered providers is highly recommended

**Support:** We provide textbooks and support resources such as examiner's reports and past papers. Students are also very welcome at ICSA events

**Cost:** £910 – 1,500

**Dates:** Exams Jun 2019, Nov 2019

**Web:** [icsa.org.uk/discovercertcorpgov](http://icsa.org.uk/discovercertcorpgov)

This Level 4 qualification introduces you to the key frameworks, codes and legal and regulatory requirements which underpin effective corporate governance. It is designed to help you to navigate complex governance structures, understand risk and support your organisation's governance needs.

If you work in a role with governance responsibilities attached to it, such as secretarial assistant, executive assistant or governance officer, this qualification can help improve your performance and add value to your organisation.

### Content

The qualification takes 200 hours' study time over six to nine months. The topics covered include:

- General Principles of Corporate Governance
- The Board, Shareholders and Corporate Reporting
- Board Procedure and Governance Administration
- Risk Governance

### Benefits

You will gain a better understanding of:

- the role of the board and company secretary;
- how to support and engage with the board on legal, financial and regulatory issues;
- frameworks and principles of governance and how to apply the relevant codes;
- key players in governance; and decision-making complexities; and
- key ways to manage risk.

# THE SHORT SYLLABUS

# Key features

## **The ICSA Certificate in Corporate Governance:**

- is aimed at individuals who are working, or looking for a role, with governance responsibilities in the private or other sectors
- is a Level 4 qualification – set at first-year undergraduate level
- contains four compulsory modules
- is an open-entry programme with no prior qualifications required
- is externally assessed – ICSA will set and mark the assessment
- is assessed twice a year, in June and November
- is graded at Pass (P), Merit (M) or Distinction (D) – students whose level of achievement is below Pass will be classified as Fail A, Fail B, Fail C or Fail D, depending on the number of marks achieved.

## **Prior knowledge, skills and understanding**

You do not need to achieve any other qualifications before registering for this qualification. No prior knowledge, skills or understanding are necessary. There are no formal entry requirements and the qualifications are suitable for non-degree holders, although it is recommended to be working in a relevant occupation.

## **Assessment**

The modules within the qualification are externally assessed via one closed-book examination that will cover content from each module. The examination is set and marked by ICSA and the pass mark is 50%. See the *Qualification structure* section for further information.

The examination provides independently assessed evidence of learning. It also enables students to demonstrate the range of transferable skills they have developed throughout their programme of study by requiring them to apply their knowledge in unfamiliar contexts.

# Qualification structure

This qualification comprises four modules and is assessed via **one** three-hour (plus 15 minutes' reading time) closed-book examination which is set and marked by ICSA. Students must pass this paper to be awarded the qualification. The pass mark is 50%.

Module number	Modules	Total hours study time	% weighting	Description
1	General Principles of Corporate Governance	55	27.5	<p>This module introduces the general principles of corporate governance including what corporate governance is, its purpose, scope and history, and why it is important. It also looks at how different countries have approached corporate governance, including the use of non-statutory governance codes and where it fits in a country's regulatory framework.</p> <p>The module covers an overview of corporate governance, explains the difference between principles and provisions and introduces some key governance theories. It then considers how corporate governance has developed in the UK, first for companies listed on the London Stock Exchange and then in other sectors and explains how governance has developed globally.</p> <p>Finally, the module covers some of the current key issues in governance and likely developments, including the influence of recent scandals, the importance of ethics, values and corporate culture, what organisations exist to do and their place in society and corporate social responsibility.</p>
2	The Board, Shareholders and Corporate Reporting	50	25	<p>This module takes a closer look at boards, shareholders and corporate reporting. It covers the role and structure of boards, how they are remunerated and the main board committees. It also looks at common problem areas for boards and directors in making good decisions.</p>

				<p>The module then explains the rights and responsibility of shareholders, the investor chain linking individual savers to legal share owners, engagement by shareholders with companies they invest in and some of the problem areas.</p> <p>Finally, the module examines corporate reporting – how companies report to shareholders. It looks at the purpose and contents of the annual report and some of the practical issues for reporting</p>
3	Board Procedure and Governance Administration	40	20	<p>This module explores board procedure and governance in practice. It covers good meeting practice for boards, including the documentation that boards can use to improve meeting practice and the procedures for running a meeting.</p> <p>The module then looks at board effectiveness and the role of the company secretary in helping to ensure meetings are effective, and considers how boards should evaluate their effectiveness and some of the things that can challenge effectiveness in making good board decisions.</p>
4	Risk Governance	55	27.5	<p>This module explores risk governance, explaining the role of the board in relation to ensuring the resilience of the organisation and its strategy in the face of risk. It covers the concept of risk, key risk terms and the board's role in risk governance. The module then covers sources of risk, practical issues and challenges of managing risk and considers what can be learned from the 2007/8 financial crisis.</p>
<b>Total</b>		<b>200 hours</b>	<b>100%</b>	

# STUDY TEXT SAMPLE CHAPTER

ICSA Study Text

# Certificate in Corporate Governance

Paul Moxey

 **icsa**

The Governance  
Institute

# Chapter nine

## Boardroom effectiveness

### CONTENTS

1. Introduction
2. The company secretary
3. Board effectiveness evaluation
4. Problem areas for directors and boards in effective decision making

## 1. Introduction

This chapter builds on the previous chapter on good meeting practice, setting out what else makes boards effective. Section 1 is about how the company secretary supports the board, including their role and responsibilities. The next section looks at board evaluation, what it involves and ways of doing it. The last section considers some of the problem areas for directors and boards in effective decision making not already covered in this or the previous chapter.

## 2. The company secretary

### 2.1 The legal and code requirement

All public companies are required to have a company secretary (CA2006 s. 271). The model articles for public companies contain a number of references to the company secretary in relation to meetings and documents. Together with the directors a company secretary is an 'authorised signatory' under s. 44 for executive documents.

Private companies were required to have a company secretary until the Companies Act 2006 but they may still choose to have one (CA2006 s. 270). If a private company does not have a secretary, anything required to be given or sent to its secretary may be given or sent to the company itself. Anything else required to be done by the secretary may be done by a director or person authorised by the directors.

Principle I of the 2018 Code says 'the board, supported by the company secretary, should ensure that it has the policies, processes, information, time and

resources it needs in order to function effectively and efficiently. Provision 16 provides 'all directors should have access to the advice of the company secretary, who is responsible for advising the board on all governance matters. Both the appointment and removal of the company secretary should be a matter for the whole board'.

So the company secretary's role is one of supporting the board, and particularly the chair, in the performance of their duties. Exactly how much each company secretary does will differ from board to board.

## **2.2 The role and responsibilities of the company secretary**

As the ICSA Guidance note, 'The corporate governance role of the company secretary' (2013),<sup>1</sup> says, the company secretary is at the heart of the delivery of good quality corporate governance. Much of the governance work described in this study text will be done by the company secretary.

The FRC confirms this in its Guidance on Board Effectiveness. In a section entitled 'Board support and the role of the company secretary', it says that 'the company secretary is responsible for ensuring that board procedures are complied with, advising the board on all governance matters, supporting the chair and helping the board and its committees to function efficiently'.

Other responsibilities set out in the guidance include ensuring good communication and facilitating induction, training and general professional development. Another responsibility is to ensure that directors have access to independent professional advice at the company's expense. The company secretary should report to the chair on all board governance matters. This does not preclude the company secretary also reporting to the chief executive in relation to their other executive management responsibilities. The remuneration of the company secretary should be determined by the remuneration committee.

Another aspect of the company secretary's role is assisting in the establishment of policies and processes that the board needs in order to function. The company's governance processes, for example board and committee evaluation, should be regularly assessed by the company secretary and the chair, along with any potential improvements that arise from the assessment.

The King IV Report™ says that governing bodies should have 'access to professional and independent guidance on corporate governance and its legal duties', and 'support to coordinate the functioning of the governing body and its committees'. It says 'the governing body should approve the arrangements for the provision' of such guidance and ensure that the company secretary 'is empowered and carries the necessary authority'. It recommends that even companies and other organisations not required to have a company secretary should consider appointing one. King IV™ says the company secretary 'should have unfettered access to, but for reasons of independence ... not be a member of, the governing body'. Finally, King IV™ says that the company secretary

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1 ICSA (2013) The corporate governance role of the company secretary, [www.icsa.org.uk/download-resources/download0?fileId=7960](http://www.icsa.org.uk/download-resources/download0?fileId=7960)

'should report to the [board] via the chair on all statutory duties and functions performed in connection with the governing body'. The company secretary may report to executive management on other matters.

It follows that company secretaries should develop and maintain a professional, objective and effective relationship with the chairman and other board members. They should be seen as trusted advisers who enjoy board members' confidence and be a confidential sounding board on matters that concern them. They can be an unobtrusive but, if necessary, firm voice in board discussion. They are not, however, board members and should not vote in a board meeting. They should be abreast of new governance legislation, regulation and codes and any other governance developments relevant to the company and brief the board appropriately.

Agendas will normally be prepared by the company secretary in consultation with the chairman. As part of the agenda setting they should agree what the meeting needs to achieve, including any decisions that are required.

The company secretary will attend board meetings and be the chairman's right hand. The effectiveness of the chairman and of the board meeting will, to a considerable extent, depend on the company secretary. They are responsible for board and committee administration and the issue of board papers including calling meetings, agendas, resolutions, supporting board papers and board minutes after a meeting. They can also advise on procedure during the meeting and on regulatory matters. The company secretary, or one of his/her team in a large organisation, will have the same role in committee meetings.

The company secretary will draft the minutes of the board or committee meeting. As discussed in Chapter 8, this is likely to be as soon after the meeting as possible, if not actually done during the meeting. The minutes of one meeting will normally be approved at the next meeting if not before. Once approved, they should be signed by the chairman and filed in the Minute Book.

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## Test yourself 9.1

### Which legislation removed the requirement for private companies to have a company secretary?



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The company secretary is likely to be responsible for many of a company's compliance requirements. This will include maintaining the various statutory registers and Companies House filing requirements and compliance with legislation.

The statutory registers which should be maintained at the registered office include:

- ◆ register of members and share ledger;
- ◆ register of directors and secretaries;
- ◆ register of directors' residential addresses;
- ◆ register of charges;

- ◆ register of people with significant control (PSC register); and
- ◆ minutes of board and company meetings including shareholder resolutions.

These registers may be inspected by the public. Information to be filed at Companies House includes:

- ◆ the company's financial statements once approved;
- ◆ an annual confirmation statement (this replaced the Annual Return in 2016);
- ◆ company resolutions (passed by the members);
- ◆ changes in directors or the secretary;
- ◆ changes in share capital or the rights of shares;
- ◆ changes to the articles of association or a new memorandum and articles;
- ◆ change of company name or registered address; and
- ◆ changes in mortgages or charges.

This information can be filed by post, courier or online. There are time limits for filing and penalties for late filing. Apart from the financial statements, resolutions and the memorandum and articles, changes should be notified on prescribed forms.

The company secretary will also be responsible for much of the work associated with shareholder general meetings, also called company or members' meetings. There are two types: the annual general meeting (AGM), at which matters to do with the accounts, audit, directors' remuneration, appointment of directors and dividends will be transacted. Any other matter for the members such as alterations to share capital can also be transacted at an AGM. Any other shareholder meeting is an extraordinary general meeting (EGM). An EGM would be called if business needs to be transacted at a different time from the AGM. Notice to convene a general meeting will be by the board (but see also Chapter 6) but will usually come from the company secretary by order of the board.

It follows that company secretaries must be well organised and have access to up-to-date compliance requirements. A timetable or series of timetables covering the main events such as production of an annual report, company general meetings and board meetings should be helpful, as would checklists for the various standard procedures.

In addition to all the responsibilities above the company secretary may also be the executive with overall responsibility for all other administrative matters.



## **Test yourself 9.2**

### **Which documents must be filed at Companies House?**

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### 3. Board effectiveness evaluation

All boards should benefit from board effectiveness evaluation. The benefit of having one is likely to be proportional to the effort made in carrying it out.

Benefits for boards, committees and individual directors can include:

- ◆ recognising mistakes and learning from them;
- ◆ surfacing uncomfortable issues which no one wants to raise (identifying the elephant in the boardroom) and dealing with them;
- ◆ identifying what works and what can be improved;
- ◆ considering boardroom dynamics: are they healthy or do they need help?;
- ◆ reviewing the evidence of the outputs of the board and committees such as: whether good decisions been made, whether the strategy was a good one and whether the values and standards the board wanted are embedded in the organisation;
- ◆ identifying and addressing any gaps in knowledge or experience on the board; and
- ◆ the satisfaction of knowing the board, its committees and members are doing a good job.

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#### Stop and think 9.1

**The 2016 Carillion Annual Report described in three pages the annual review of board effectiveness which it said 'is an important process for helping to identify key areas for future improvement or focus'. The 2016 review was led by the chair and facilitated by Linstock Limited, an independent corporate advisory firm. At the December 2016 board meeting, the directors reviewed the results of the evaluation, which confirmed that the board, each of its committees and the directors continue to be highly effective.**

**Can the board of a company which a year later ran out of money justifiably have considered itself highly effective?**

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The requirement for boards of companies with a primary listing to evaluate their effectiveness was one of the recommendations by Sir Derek Higgs in his Review of the Role and Effectiveness of Non-executive Directors for the Department of Trade and Industry in 2003<sup>2</sup>. He recommended that the performance of the board as a whole, of its committees, and of its members, be evaluated at least once a year. It was a controversial suggestion but was included in the Combined Code later in 2003. It has now gained general acceptance and some now say it is the most useful part of the UK Code.

Many national codes of corporate governance and the New York Stock Exchange require board effectiveness evaluations.

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Derek Higgs (2003) Review of the Role and Effectiveness of Non-executive Directors, The Department of Trade and Industry.

The 2018 Code principle L says 'annual evaluation of the board should consider its composition, diversity and how effectively members work together to achieve objectives. Individual evaluation should demonstrate whether each director continues to contribute effectively'. Provision 21 says this evaluation should be rigorous and include the board, its committees, the chair and the individual directors. In FTSE350 companies, evaluation should be facilitated externally at least every three years, in which case the external evaluator should be named in the annual report.

The Higgs Report includes guidance on how evaluations should be carried out, part of which has been carried over into the FRC's 2018 Guidance on Board Effectiveness. The latter guidance suggests 16 areas which might be considered as part of an evaluation:

1. the mix of skills, experience and knowledge on the board, in the context of developing and delivering the strategy, the challenges and opportunities, and the principal risks facing the company;
2. clarity of, and leadership given to, the purpose, direction and values of the company;
3. succession and development plans;
4. how the board works together as a unit, and the tone set by the chair and the chief executive;
5. key board relationships, particularly chair/chief executive, chair/senior independent director, chair/company secretary and executive/non-executive directors;
6. effectiveness of individual directors;
7. clarity of the senior independent director's role;
8. effectiveness of board committees, and how they are connected with the main board;
9. quality of the general information provided on the company and its performance;
10. quality and timing of papers and presentations to the board;
11. quality of discussions around individual proposals and time allowed;
12. process the chair uses to ensure sufficient debate for major decisions or contentious issues;
13. effectiveness of the company secretary/secretariat;
14. clarity of the decision-making processes and authorities, possibly drawing on key decisions made over the year;
15. processes for identifying and reviewing risks; and
16. how the board communicates with, and listens and responds to, shareholders and other key stakeholders.

These areas are mainly input issues for the board. The areas underlined represent process issues. None of the areas represent outputs, i.e. what the board actually achieves in terms of results.

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## Test yourself 9.3



### Who introduced the requirement for UK listed companies to have a board effectiveness evaluation?

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Board evaluation is the responsibility of the board but it is the chairman's responsibility to lead it and ensure the board has sufficient time and resources for it. The company secretary is likely to be the key facilitator making sure it runs smoothly.

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## Making it work 9.1



After HBOS failed in 2008 the deputy chairman and senior independent NED told the Parliamentary Commission on Banking Standards<sup>3</sup> investigating the failure that 'I have no doubt that the HBOS board was by far and away the best board I ever sat on. My recollection of the culture and characteristics of the board was one of openness, transparency, high intellect, integrity, good working relationships between the chair and chief executive, and a suitable diversity of backgrounds, mix of experience and expertise to maximise effectiveness [...] If with the benefit of hindsight I was asked if I wanted to sit on this board again I would be saying yes.'

The HBOS chair told the Commission that he did not accept that the board he chaired failed in its challenge to the executive. He said that much thought was given to ensuring that 'there was a lot of challenge and different ways of challenging ... There was an atmosphere where people were able to be very direct and blunt. There were one or two occasions when great offence was caused, but we had a very open society. There was constant challenge, not just of corporate, but of the other divisions'. He concluded: 'I think the governance was rather good.'

Other directors reported positively about their experience on the board. The Commission concluded: 'the corporate governance of HBOS at board level serves as a model for the future, but not in the way in which Lord Stevenson and other former board members appear to see it. It represents a model of self-delusion, of the triumph of process over purpose.'

The more detailed report<sup>4</sup> by the FCA and PRA after the Parliamentary Commission report commented on the bank's disclosures on board effectiveness reviews in the 2005, 2006 and 2007 Annual Reports and Accounts. They all stated that 'performance and effectiveness of the Board and each of its Committees is evaluated annually'.

**The FCA/PRA report implies that such evaluations were weak. It reports**

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3 An accident waiting to happen': The failure of HBOS, <https://publications.parliament.uk/pa/jt201213/jtselect/jtpcbcs/144/144.pdf>

4 Financial Conduct Authority (FCA) and the Prudential Regulation Authority (PRA) (2015) The failure of HBOS plc (HBOS).

**that the bank chair said that he met with individual directors about once every two or three years to obtain and give feedback, and then he produced a report which would be discussed as a board. The Review was 'unable to form a view on this ... as no records of any such reviews have been found'. Nor had the Review seen evidence to confirm that the 'reviews were carried out, or what the outcomes if any, were'.**

**The report concludes there was insufficient evidence to suggest that the evaluations were in line with the guidance at the time or a formal and rigorous evaluation advocated in principle B.6 of the Combined Code and 'in none of these years did the evaluation identify material failings or weaknesses'.**

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Clearly, one lesson from HBOS is that board effectiveness evaluation should be properly documented.

Disclosures by UK listed companies about their board evaluations seldom reveal useful detail or insights. For many companies which actually give information about the process used, the main evaluation tool is a questionnaire, the results of which are collated and discussed in a board meeting. Some companies use a questionnaire followed by interviews between each of the directors and an external facilitator or one or more of the chairman, the senior independent NED or the company secretary. Some disclosures say that evaluation includes review of documents. A few companies disclose brief information about the findings of the evaluation and the action taken but most are silent or simply conclude the findings were satisfactory.



## Stop and think 9.2

**A 2016 study<sup>5</sup> of board evaluation of 187 North American public and private companies by the Rock Center for Corporate Governance at Stanford University and The Miles Group found:**

- ◆ **55% of the companies that conducted board evaluations evaluated individual directors (leaving 45% which did not evaluate individual directors).**
- ◆ **36% believed that their company does a very good job of accurately assessing the performance of individual directors.**
- ◆ **52% believed their board is very effective in dealing with directors who are underperforming or exhibit poor behaviour, while a quarter (26%) do not.**

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5 Rock Center for Corporate Governance at Stanford University and The Miles Group, 2016 Board Of Directors Evaluation And Effectiveness, Stanford USA, [www.gsb.stanford.edu/sites/gsb/files/publication-pdf/cgri-survey-board-directors-evaluation-effectiveness-2016.pdf](http://www.gsb.stanford.edu/sites/gsb/files/publication-pdf/cgri-survey-board-directors-evaluation-effectiveness-2016.pdf)

### Group dynamics and culture

- ◆ **46% believed that a subset of directors has an outsized influence on board decisions.**
- ◆ **74% said directors allow personal or past experience to dominate their perspective.**
- ◆ **53% did not express their honest opinions in the presence of management.**
- ◆ **47% said directors are too quick to come to consensus.**
- ◆ **44% said directors do not understand the boundary between oversight and actively trying to manage the company.**
- ◆ **39% said fellow board members derail the conversation by introducing issues that are off-topic.**

**This survey suggests a number of problem issues for boards in how they handle group dynamics. Do you recognise any of them in your own experience? On the positive side, 46% strongly believed that their board tolerates dissent.**

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A need to document effectiveness evaluations could encourage a formulaic box-ticking approach to provide evidence of their having taken place. This is a danger, especially if the primary reason for having an evaluation is to comply with the UK Corporate Governance Code. It would be better if the whole board sees board evaluation as an opportunity to improve the way they work and make decisions. This is of course easier for boards which already work well together and if the organisation they direct and control is also doing well. The board of an ailing organisation has a harder job and is more likely to have signs of dysfunction. Facing up to the challenge through a rigorous evaluation may be hard.

If we think of the board as a system with inputs, processes and outputs, the 16 areas listed above which the FRC suggests might be considered in an evaluation mostly consider what could be termed input issues. They are the ingredients of what is needed for an effective board. The areas which have been underlined in the list above are process issues although number five, 'key board relationships, particularly chairman/CEO, chairman/senior independent director, chairman/company secretary and executive/non-executive', is both an input and a process issue.

The list above does not include output issues which consider whether the board actually does its job well. The example of HBOS above revealed a board which thought it was doing a good job. If it had considered its effectiveness in the light of what was really going on within HBOS it might have reached a different view. It is therefore important that boards consider their effectiveness in relation to the effect it has on the organisation and whether or not the decisions it made had been sound ones. An organisation which fails is unlikely to have had an effective board.

### 3.1 Asking good questions

Additional considerations for boards therefore include the following.

- ◆ How well does the board lead the organisation?
- ◆ Were all the decisions made by the board good ones?
- ◆ How well does the board set strategy?
- ◆ Is that strategy the best one available?
- ◆ Is that strategy being achieved?
- ◆ How well does the board ensure the necessary financial, human and other resources are present to achieve objectives in line with the strategy?
- ◆ How well does the board monitor organisational performance?
- ◆ How clear is the board that the organisation always operates within its risk appetite and tolerance?
- ◆ How confident is the board that it understands all the significant risks facing the organisation?
- ◆ How satisfied is the board that all these risks are managed, mitigated or transferred so that any residual risk is within the board's set risk tolerance?
- ◆ How well does the board set the values and standards, including ethical values, for the whole organisation?
- ◆ How sure can the board be that the values and standards it sets are indeed embedded throughout the organisation?

The above considerations also apply to committees but it is the board which ultimately is responsible for its effectiveness.

The FRC has highlighted culture, including board culture, as an important issue for companies. The Stanford University survey referred to above suggests a number of cultural issues which boards should be wary of, such as 74% of respondents saying directors allow personal or past experience to dominate their perspective and 39% saying fellow board members derail the conversation by introducing issues that are off-topic.

Not surprisingly, perhaps, annual report disclosures about the board evaluations which have taken place do not reveal whether such cultural issues were present in their boards nor do they reveal whether the evaluation was designed to include such cultural issues.

### 3.2 Methods of evaluation

Board evaluations will usually consist of a combination of questionnaires, interviews, group discussions, reporting of findings and discussion of findings, development of an action plan and implementation.

The questionnaires may use only closed questions (where the respondent would choose an answer from two or more options given), a mixture of closed and open (where the respondent could write a narrative response) questions or only open questions and each director will be asked to respond. The questionnaires may be designed within the organisation, be one of the standard formats widely

available or developed by an external facilitator. Open questions allow a rich source of information but closed multiple choice questions have the advantage of being quick, allowing comparison with other responses and easy to interpret. They may also be easy to misinterpret if the questions are not well designed or do not fit the particular circumstances of the board or organisation at the time. Questionnaires can be detailed: one Middle East bank uses a questionnaire with nearly 200 questions but length does not necessarily indicate quality. A shorter, more targeted questionnaire could be better.

Interviews with individual directors would be with the chairman, senior independent NED, external facilitator or company secretary. The interviews can build on the responses from the questionnaires. Both questionnaires and interviews will consider the board and committees. They may also consider the performance of individual directors. Individual directors will be asked to evaluate their own performance and they may also be asked to evaluate other directors. Criteria considered for individual directors will include input issues such as independence and number of meetings attended or been absent. More useful, but harder to consider, are matters such as the quality of constructive challenge and their contribution to the work of the board and its committees. Executive directors will also have a review of their performance as executives.

Interviews or discussions may also be held with investors and other stakeholders. The depth and scope of the evaluation will vary. A thorough review will take much time and effort. Evaluations carried out soon after they were required by the Combined Code were relatively perfunctory and focused on compliance with the Code. They would have been designed partly to enable the board to say they had performed an evaluation and that the results were satisfactory rather than uncover problems to be addressed. As experience of evaluations has improved, and boards have gained confidence in them and appreciate their benefits, boards are undertaking more rigorous evaluations. It can be difficult, however, for boards to be self-critical when directors want to retain their positions. As explained above, the evaluation should include board culture and output issues which link the performance of the board and individual directors to organisational performance.

## 4. Problem areas for directors and boards in effective decision making

This chapter and the previous chapter have already outlined a number of problem areas for boards which harm their effectiveness and good decision making, such as:

- ◆ adequacy of information available to make decisions;
- ◆ lack of clarity about the aim of a meeting and lack of focus;
- ◆ maintaining strategic overview and avoiding micromanagement;
- ◆ lack of constructive challenge; and
- ◆ cognitive biases.

Other problem areas are:

- ◆ personality and group dynamics issues;
- ◆ a dominant CEO or chairman;
- ◆ not knowing what is going on;
- ◆ maintaining independence and objectivity;
- ◆ illegal or unethical conduct; and
- ◆ conflicts of interest.

#### **4.1 Personality and group dynamics issues**

The Stanford University survey above highlights some of the problems caused by personality and group dynamics issues. Some people are just awkward. The vast majority are not and want to do a good job. Problems can arise if people feel they are not being listened to. Good chairing will help ensure that each director is able to speak and be listened to. Other problems can arise from genuinely held difference of opinion. Good chairing can help find any common ground from which to build some agreement. Problems in meetings can be reduced by good preparation smoothing the way before a meeting. A thorough and professional board effectiveness evaluation properly handled should help to identify and address more deep-seated issues.

The company secretary can assist, working with the chairman, in making sure people are as fully informed as practicable and alert for signs of trouble ahead.



#### **Test yourself 9.4**

**List two of the examples of dysfunctional group dynamics and culture in the study of board evaluation of 187 North American public and private companies by Rock Center for Corporate Governance at Stanford University and The Miles Group.**

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#### **4.2 Dominant CEO or chairman**

Years of code development have sought to eliminate the problem of one person, usually the CEO or chairman, dominating board proceedings. It is human nature though that one person is likely to have more influence and other people defer to that person, choose not to confront him/her or choose to leave. A good effectiveness evaluation should identify the problem and the dominant person might moderate his/her behaviour. Having raised the issue it should then be easier for other directors to assert themselves.

#### **4.3 Knowing what is going on**

Knowing, or rather not knowing, what is going on in the organisation is a problem facing all managers and board members everywhere except in the smallest organisations. Good induction procedures for new board members and updating for current directors can help ensure the board is as well informed as

reasonably possible. It simply is not possible, however, to know everything which happens yet directors, in legal terms theoretically at least, remain responsible for what goes on. The financial crisis highlighted examples not just of banks being too big to fail but seemingly too big to manage.

The solution is to accept that it is not possible to know everything but take care to ensure that the organisation:

- ◆ only employs good people with integrity;
- ◆ has a framework of prudent and effective controls;
- ◆ has good values and standards which are embedded throughout the organisation;
- ◆ sets clear aims or objectives for the organisation, team's and individuals which are all aligned;
- ◆ understands the significant risks and is resilient enough to deal with them;
- ◆ has sufficient resources to achieve what is expected;
- ◆ has clear delegation of responsibility and accountability;
- ◆ has effective monitoring; and
- ◆ has staff who feel free to speak up where they have concerns.

#### **4.4 Maintaining independence and objectivity**

Governance codes attach great weight to the appearance of independence for NEDs. Too much independence could mean detachment and disinterest. Too great an involvement in something means objectivity could be lost. What really matters is that all directors think independently and objectively and are engaged in a common purpose. A clear policy of what powers the board reserves to itself and what it delegates can help boards maintain independent and objective thinking, and stay concerned enough to be engaged but not so close as to lose objectivity.

#### **4.5 Illegal or unethical conduct**

Illegal or unethical conduct is a common problem affecting most large organisations. A web search looking for examples of illegal or unethical conduct in Fortune 500 companies will show most have had issues and some multiple issues. Illegal conduct at board level is rarer but does happen.

Boards will want to ensure as far as possible that this does not happen in their organisations. Surveys suggest that the most effective ways to ensure ethical behaviour are to have a good tone at and from the top of the organisation and to have a work culture where people feel free to raise any concerns they have without fear of any retribution. Creating such a culture may be difficult. Most boards and top management will say that values are important, that the code of ethics or conduct must be followed and violations will be severely dealt with. Such things may fall on deaf ears if the managers are set over-demanding performance targets and then managers, whose career and livelihood may depend on keeping their job, push staff to deliver. Whistleblowing procedures,

discussed in Chapter 12, can help deter unethical or illegal behaviour provided staff have confidence there will be no retribution against them for raising a concern.



## Making it work 9.2

**This example is based on an article<sup>6</sup> in Vanity Fair by Bethany McLean in 2017.**

**Wells Fargo was founded in the USA in 1852 as a stagecoach express. By 2016 it had become one of the six major US banks after a series of acquisitions and mergers. It was focused on growth and customers. The bank had an initiative to sell each customer eight additional products. Each morning there was a conference call where staff had to tell management how they were going to make the sales goal for the day. Those who could not make the goal had to explain why and how they were going to fix it. 'It was really tense,' according to one employee. Achieving sales goals was difficult, especially with competition from other banks.**

**Unusual things happened. Customers took out large loans and then immediately repaid part of them so that the bankers could get credit for the bigger loan. New customer bank accounts were created without the customers' knowledge. Some customers were charged fees on these accounts. Managers ignored concerns raised by employees about such practices. Staff who failed to make their targets were dismissed.**

**An internal report in 2004 highlighted concerns of staff who felt they could not make sales goals without gaming the system. The incentive to cheat was based on the fear of losing their jobs. The report recommended reducing or eliminating sales goals as several peer banks had done, and warned that the issue could lead to loss of business and diminished reputation in the community.**

**Between 2011 and 2015 Wells Fargo employees opened over 2 million deposit accounts and credit card accounts that may not have been authorised. In September 2016, Wells Fargo agreed to pay a \$185 million penalty to various enforcement agencies to settle charges of fraudulent conduct. As part of the agreement Wells Fargo admitted no wrongdoing.**

## 4.6 Conflicts of interest

One of the directors' duties in company law (CA2006 s. 175) is to avoid conflicts of interest. A director of a company must avoid a situation in which they have, or can have, a direct or indirect interest that conflicts, or possibly may conflict, with the interests of the company. This applies in particular to the exploitation of property, information or opportunity. It is immaterial whether the company

6 McLean, B. (2017) How Wells Fargo's Cutthroat Corporate Culture Allegedly Drove Bankers To Fraud, Vanity Fair Summer 2017, [www.vanityfair.com/news/2017/05/wells-fargo-corporate-culture-fraud](http://www.vanityfair.com/news/2017/05/wells-fargo-corporate-culture-fraud)

could take advantage of the property, information or opportunity. If the articles allow it, the board may decide to authorise the decision provided the director concerned is not counted as part of the quorum.

The model Articles of Association for both private and public companies also provide that if a director is concerned in an actual or proposed transaction or arrangement with the company they should not take part in the decision-making process. The director may, however, take part in the decision if:

- ◆ the company allows it by an ordinary resolution of its members;
- ◆ the director's interest cannot reasonably be regarded as likely to give rise to conflict of interest; or
- ◆ the conflict arises from a permitted cause:
  - (i) a guarantee,
  - (ii) a subscription, and
  - (iii) arrangements which benefit employees and do not provide special benefits to directors.

## Chapter summary

- ◆ Public companies are required to have a company secretary, private companies may choose to have one.
- ◆ The company secretary is at the heart of the delivery of good quality corporate governance.
- ◆ The company secretary will be the first source of independent professional advice for the board; all directors should have access to their advice and services.
- ◆ The company secretary is likely to be responsible for many of a company's compliance requirements including maintenance of statutory registers and filing with Companies House.
- ◆ The company secretary will also be responsible for much of the work associated with shareholder general meetings.
- ◆ Many national codes of corporate governance and the New York Stock Exchange require annual board effectiveness evaluations.
- ◆ The UK requirement for board evaluation is in the UK Corporate Governance Code principle L.
- ◆ Board evaluation is the responsibility of the board but it is the chairman's responsibility to lead it and ensure the board has sufficient time and resources for it.
- ◆ Companies are required to explain in the annual report how the board effectiveness review was conducted.
- ◆ HBOS in 2008 highlighted an example of a board which claimed board effectiveness reviews had been carried out each year but there was no evidence of this and HBOS board was clearly ineffective.
- ◆ Effectiveness reviews should include consideration of cultural dynamics of the board and its effectiveness in terms of outputs.

- ◆ Effectiveness reviews consist of a combination of questionnaire, interview, group discussion, reporting of findings and discussion of findings, development of an action plan and implementation.
- ◆ Further problems which can harm board effectiveness, in addition to those already covered include: personality and group dynamics issues, dominant CEO or chairman, not knowing what is going on, maintaining independence and objectivity, illegal or unethical conduct, and conflicts of interest.
- ◆ Wells Fargo provides an example of fraudulent behaviour caused by staff being expected to achieve over ambitious performance targets.

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We hope this discovery pack has given you a good understanding of what studying the Certificate in Corporate Governance involves.

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