Time to reboot governance

A new approach to accountability, based on performing, informing and holding to account, should replace the existing tick-box approach, argues an ACCA paper

There is confusion about what governance is for, and regulation of governance and risk management has not helped to create a healthy corporate culture or effective boards. These are two of the hypotheses advanced in a recent consultation paper published by ACCA, *Creating value through governance – towards a new accountability*. The paper and the current state of corporate governance were discussed at an ACCA Governance, Risk and Performance Research and Insights conference in March, attended by senior figures in the governance and risk reporting arena.

Adrian Berendt FCCA, chairman of ACCA's Global Forum for Governance, Risk and Performance, and co-author of the paper, sees considerable scope for improvement in current practice. 'Many people confuse governance and compliance,' he says. 'The last four letters are the same, but there the resemblance ends. Too many companies comply with the letter of governance codes without embracing the spirit.'

Such perceived problems have triggered ACCA's consultation, which seeks to achieve consensus on the purpose of corporate governance. 'The paper argues that corporate governance is all about creating long-term sustainable value, for business and for its stakeholders,' says Paul Moxey, head of corporate governance and risk at ACCA, and co-author of the paper. 'Governance codes should be evaluated on how well they create this value for real economic growth.' The paper also advises that value should be considered in a wider sense than simply profit, also taking account of societal and environmental value.

'The time has come to start again,' Berendt says. 'We need to remove the check-box approach and ensure that governance is appropriate for each organisation individually. In essence, our approach boils down to one question and one instruction. The question is: "Is the way in which the organisation is being governed adding value for the benefit of all stakeholders?" And the instruction is: "The board of directors must explain how its governance adds value and where it could do better."'

ACCA's paper proposes a new accountability framework for corporate governance based on three components: performing, informing and holding to account. As it explains: 'The need for companies to perform requires boards, management and staff to perform... Those responsible for performing then need to inform those to whom they are, or should be, accountable and to be held accountable in return. In a similar way, professional investment managers need to perform and be accountable to those who entrust their money to them.'

All three components must work effectively if a company is to create value sustainably for its shareholders and other stakeholders. They must also be working effectively at each of three interfaces: between executive management and boards, between boards and institutional shareholders, and between institutional shareholders and savers. The paper asserts that there are 'serious problems' with current levels of accountability. It states: 'The most intractable problems are in the investment management chain, where retail savers have no influence over institutional investors and fund managers, institutional investors have insufficient influence over boards, and boards have insufficient control over management.'

Frank Curtiss, head of corporate governance at RPMI Railpen Investments Elements, agrees that elements of the current framework are not working properly. 'The accountability of the institutional investor to the end investor, the people who supply the money, is

▲ CORPORATE DEBATE

Left to right: Paul Moxey, Adrian Berendt FCCA, Frank Curtiss and Sallie Pilot at the Research and Insights conference

PROVISIONAL RECOMMENDATIONS

1. There should be general acceptance that the purpose of governance is to create value sustainably.
2. Governance codes and policies should be assessed against the accountability framework (performing, informing and holding to account) at each of the interfaces between management, boards, institutional shareholders and providers of funds.
3. Companies and investors should develop and report using more suitable measures of performance and value creation. For example, corporate reporting should include probabilistic information on confidence and uncertainty, information on the ethical health and values of the organisation, and information on how, and by how much, companies create sustainable value and contribute to public good.
4. Policymakers and institutional investors should address the asymmetry in the risk:reward ratio between management, shareholders and other stakeholders, and seek ways to enfranchise savers. They should also examine ways to give investors incentives to favour companies that create long-term value for themselves and society.

perhaps the most problematic,' he says. 'The investor in a unitised fund has very little voice and with defined contribution schemes there is a deficit of governance. There is very little scope for a defined contribution member or even an employer to influence the engagement policy of the intermediary firm. Arguably more needs to be done on that.' However, although Curtiss describes ACCA's paper as 'thought-provoking', he adds: 'I stop short of saying the current corporate governance framework is not fit for purpose and in need of fundamental reform.'

Curtiss endorses an enlightened shareholder value model. '[At Railpen] we accept that companies have a wider social purpose and, given our long-term perspective, it's in our interest to encourage companies to take account of stakeholder issues,' he says. 'But that's the extent of it. Ultimately companies have to be accountable to the people who provide the risk capital.' Establishing the principle of accountability to a wider range of stakeholders could in practice result in accountability to nobody, he warns.

While there may be weaknesses in corporate governance frameworks which ACCA's paper seeks to address, there are encouraging signs too. Sallie Pilot, director of research and strategy at corporate reporting consultancy Black Sun, believes that companies are now discussing the concept of value and how they create it far more than before. In part this is being driven by developments in integrated reporting and new corporate reporting requirements, particularly the need to describe the business model. 'Companies are being forced to have conversations about what the business does, what the business model is, how the company actually creates value, and how it is going to measure that value,' Pilot says. 'We are also seeing financial reporting people trying to define who they create value for, beyond just shareholders.' She notes, however, that it is still 'early days' in terms of such developments, the concepts of environmental and social value being relatively new in comparison to financial value.

Consultation on the paper closes on 31 August 2014. Alongside the main paper is a working paper designed to capture key messages in the form of a practical action guide, drafted by Mark Wearden, director of strategic change consultancy MBS, a senior lecturer in corporate finance and corporate governance at the University of Lincoln and also part of ACCA's Global Forum for Governance, Risk and Performance. ■

Sarah Perrin, journalist

FOR MORE INFORMATION:

Creating value through governance – towards a new accountability, and supporting material, is available at www.accaglobal.com/ab79