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Models of Corporate / Board Governance

Governance can be defined as: the combination of policies, systems, structures and a strategic/operational framework; which the governing body puts in place to ensure the leadership of the organization makes appropriate decisions, and takes appropriate actions to deliver services in an effective and accountable manner. This includes transparent and equitable stewardship of resources which will sustain the organization, and keep it relevant to both the community in which it operates and the clients/customers it serves. Today and into the future, the standards for what makes governance "good" are rising, and demanding more time and attention from those serving as Board members.

When one talks about a *model* for governance, the model represents an approach to the combination of the above elements. Beyond attention to Processes, Policies, Structures, etc. there are considerable differences in the kinds of Boards in the world today. And these unique forms of governing bodies, drive specific considerations to the application of different models.

There are five fairly commonly identified models in use today: Traditional, Carver, Cortex, Consensus, and Competency. There are of course advocates for each model which often focus on <u>their</u> particular model – usually at the exclusion of the others – though the models are in fact not mutually exclusive. Indeed, each model focuses on one or two elements of governance important for the effective functioning of a Board. Many Boards actually adopt a combination of these models, in a blend appropriate to the unique features of their organization and Board composition. However, in and of themselves these models do not provide a comprehensive prescription for Board work. There is much more to good governance than simply adopting a particular model of governance.

Let's look at each of the mainstream models in practice today.

1. The Traditional (Structural) Model

This is the oldest model, created in the earliest of corporate structuring (1700's) and passed down over the years into corporate, charitable and not-for-profit organizations, even government crown corporations. It is the template most law firms use to establish articles of incorporation even today. It is somewhat out-of-date for today's realities; however it still useful. Acts of Legislatures also follow this approach in bringing into force the existence of a specific state-owned enterprise.

The structural model has its foundation upon the concept that the Board is the legal ownership entity, and in some ways even more – it is the body corporate itself, a 'legal person' in view of the law. This is true whether the entity is a for-profit, not-for-profit, or charitable Corporation or even a Society. These structures have changed significantly in the eyes of the law since their earlier forms, and have evolved today to limit the liabilities of both the corporation and its directors. This structural approach also has evolved slightly differently in the Anglo/American accountability to widely held shareholders approach, compared to German/Japanese cross-ownership governance, and also family-owned enterprises with either other family members or minor partner ownership structures.

A basis of this model is that the structure of the Board itself, and the way in which it makes decisions, holds meetings, and the parameters by which it must abide are put into an approved structure and format. Another fundamental concept in this model is that the Board only speaks as a Board, and members of the Board speak on behalf of the Board but do not have an individual voice in the outside world. The Board Chair is usually structured to be the official "voice" of the Board, but again can only speak in a way authorized by the Board as a whole.

The structural model will usually define the delegation of responsibilities from the Board to:

(a) The CEO and Management, and/or
(b) Board Committees (including Executive Committee)

Unfortunately, where this helpful model often goes awry, is that it is silent on the accountability mechanisms and expectations for reporting-back when the Board delegates its powers. Thus, any Board utilizing this model must create Policies or By-Laws to define responsibilities, expectations, and accountability requirements for both Management and Board Committees. The Board should also create clear job descriptions for Board members, Board Executive positions, the CEO, along with Terms of Reference for Board Committees. An Annual Board Calendar should also be developed to ensure specific annual/quarterly/monthly accountability and reporting (as appropriate) to the whole Board by Management and the Board's Committees.

Another area of challenge comes when the CEO creates operating committees of management/staff that interface with Board committees of similar-sounding responsibility. For example there may be a Human Resources & Compensation Committee of the Board, and there may also be a Management executive-level committee that addresses job classifications, benefits, promotions, high-performers, bonuses, performance management, labour relations and even discipline. Board committee members may interface with executives from the Management committee to gain information for the Board concerns around Risk Management, Transparency/Accountability, etc. and may inadvertently direct staff without going through the CEO, leading to confused staff and Board members crossing the boundary between governance and operational management.

Traditional models have also been used in the past to create large Boards with "representative" members from either geographic, family, or constituent elements, and may ascribe weighted voting to different ownership parties/classes. Trends recently have been to reduce the size of such Boards and seek Board members capable of real governance for the whole, as opposed to simply representing constituents. However, this "representative-ness" structural design is one of the most potentially debilitating aspects to proper governance today. Constituency thinking or even negotiation behaviour at the Board table flies in the face of *Fiduciary Duty* to the good of the whole. Boards with this constituency or representative structure need to be able to engage the knowledge and perspective from different stakeholder groups, but still come together to focus upon and make *consensus* decision in the best interests of the whole enterprise.

Thus, the Traditional model helps organizations define Board structures, but requires the Board to actively and specifically address appropriate processes (especially accountability and communication) through Policy or By-Law creation. It must also work very hard to not have its committees delve into operational matters and end-run the CEO in the process. And, it must remember its legal Fiduciary Duty to avoid conflicts of interest and focus on the good of the whole, in particular their obligation to the good of the Corporation.

2. Carver (Policy) Model

This model popularized by John Carver over the past 20 years, is in his own words, "a rigorous academic approach to a practice area that has had very little research over the years".

The Carver model has 2 fundamental concerns:

(a) Boards focus on defining the "ends" of the organization – i.e. what the organization strives to achieve or in some cases what it must do in order to put itself out of business; and
(b) Creating the policies by which the Board and Management must abide in its pursuit of the ends.

The Board's main role in this model is to create <u>policy</u> to guide management in its operational work, and to guide the Board in its governance work.

The policy approach favoured by Carver is through developing or clarifying statements of "limitation". In the operational environment, the Board's policies define what the CEO is not allowed to do, the limits to his/her decision-making, and the guide-posts within which he/she must operate. As long as the CEO doesn't break these limitations, he/she has significant freedom to decide how, when, where to do things – the *means* of getting to the *ends*. This is of course motivational to CEO's and recognizes the competence, knowledge and full-time focus that a CEO gives to an enterprise compared to the part-time focus given by Board members.

Policies also describe the parameters within which the Board must operate: minimum number of meetings per year, minimum number of members, requirement for annual meeting with members, etc. As long as the Board operates within these parameters, Carver's model suggests that the Board Chair has the freedom to decide how to do things in the area of governance. This is very beneficial when a Board has a knowledgeable and competent Board Chair with the time or specific responsibility/compensation to work almost full time in this capacity.

Carver also suggests the reduction/elimination of Board committees and to do as much as possible as "Board of the Whole", recognizing that all Board members are equally accountable for the decision-making of the Board.

The challenges of this model come when the Board spends so much time focused just upon Policy-building, that they actually miss attending to some of their other responsibilities. Many Boards that have gone through the in-depth, time-consuming process of policy-building, reach the end of the process, and then ask what's next? Only to find that the "real work of governance" has been waiting all the while they have been developing policy.

Policy is good, it is helpful, and it helps define parameters – potentially protecting the Board and organization, plus giving broad guidelines in moving forward. However, this Model doesn't help in establishing clear strategic/annual expectations or outcomes measures of success. Ends help define direction and goals to pursue but they don't necessarily connote strategy. These measures of success and strategy for example, are given over to the (assumed competent) CEO and/or Board Chair to decide if the Board policy doesn't define.

As such, "Carver Boards" must augment their policy work with the creation or approval of a comprehensive Strategic Plan, Business Plan and Budget. They must look beyond the guidelines of the Policy to assert the need for fund-/friend-raising efforts, government relations, community interface, and more.

3. Cortex (Outcomes) Model

Developed by John Por of Toronto, the Cortex Model challenges the Board to focus on their: customers/clients, the community/marketplace, legislation, best practices of other similar organizations, and employee knowledge; in order to define the standards, expectations and performance outcomes to which the organization aspires.

The Board's main job under this model is to clarify and set the outcomes measures of success. To do this, the Board must truly seek to understand the value their organization provides to the community. Finally, the Board creates an Accountability Framework around the outcomes measures, and identifies who is responsible for leading/taking action in each area – Board, CEO, Staff, or even a 3rd party.

With a clear accountability framework, the Board now moves to ensure the capacity of resources exists in each group, and a mechanism for each group to report-back to the Board on its progress.

This model is useful in set-up for assessing performance of Board/Board Committees, CEO and/or staff; and is relatively easily done against the clearly delineated outcomes and areas of accountability. It is particularly valuable in assisting a Board become broadly *Transparent and Accountable*! For, in order to be transparent & accountable, an enterprise must have clear outcomes and performance measures established to report against.

One of the challenges to this approach is the Board's ability to understand the "business" well enough to clearly enunciate these outcomes measures. Being practical, the Board will have to rely on Management to do much of this research and develop draft performance statements. However, Board members also need to become more broadly knowledgeable of the industry segment, client expectations, trends etc. Another challenge is in the measurement and reporting of performance. In most cases, the organization is likely not to have current mechanisms or report structures in place to measure performance against the new outcomes, so these will have to be developed and shaped over time.

Boards and Management that adopt the Cortex approach will have to be careful to ensure the measurement of what is *important* versus what is *convenient*. And they will have to provide the resources required to appropriately design measurement mechanisms and collect the information regularly in new areas of performance assessment.

4. Consensus (Process) Model

This model is anchored by the understanding that all Board members are equal – with an equal vote, equal responsibility, equal liability for decision-making, and equal accountability for the actions of the organization/Board. It also recognizes however, that Board members have different areas of expertise, knowledge and wisdom to bring to the table.

As such, the model addresses how decision-making is achieved by the Board:

- How issues will be discussed, different experience and insight contributed.
- How differences of opinion or concerns will be handled
- How agreement is reached and whether members are: for a decision, will support it, have some objections/concerns but will not block a decision, or have too many concerns/objections about the good of the Corporation, to support the decision.
- How timeliness and agenda management is handled in such a consensus environment

This model is clearly valuable for the NFP sector, family-owned businesses, as well as widely held corporations with no major shareholder. It supports contribution from all Board members, and expects others to listen, respect, and consider their colleagues' input. It may well protect an organization in that all sides of an issue or decision are considered and resolved before making the decision.

Of course, it can also slow the proceedings of a Board. If for example, there are constituent representatives on the Board who must posture or receive authorization from their constituency before agreement is reached, then issues can get sidetracked; and particularly powerful individuals/constituencies can hold what in effect is a veto over other members – effectively nullifying an otherwise "consensus-driven" orientation. What is the status of the CEO, CFO or other executives on the Board – do they have equal voice/vote?

The consensus model developed by your Board, may rely on elements of Robert's Rules of Order, Parliamentary Rules of Order, or other aspects for when consensus is not possible.

As one can see, this model focuses on the way decision-making is made within the Board. As such the Board will have to develop Policy or By-Laws to convey its important processes, and then add attention to strategy, planning, reporting on operational issues, etc. in addition to the decision-making framework.

5. Competency (skills/practices) Model

This model is essentially a developmental one. It strives to ensure all members of the Board have the appropriate knowledge, skills and attitudes to be a good Board member. It addresses Board as a team – communications, trust, relationships etc. And, this approach seeks to continuously improve the performance of the Board over time.

The Competency approach can also prescribe behaviour expectations through the implementation of Board assessments (either external or self-driven) and ensure they have a common context for their work together.

While this is a strong model for recruiting and developing Board members, and it can prescribe types of practices and real work of governance to be done by the Board; it doesn't drive policy creation, establishment of strategy, or monitoring of practice per se. It may well identify that these later things are important practices of Board members, but doesn't prescribe through legal structure, Policy or By-Laws how it will be handled.

What an action-oriented Competency model can do however, is define the style of behaviour and frequency/or level of engagement for Board members in their work. It may assist new Board members by giving them a picture of the practices they should strive to adopt; and if combined with some mentorship from more experienced Board members, can bring new members up to speed fairly quickly to more fully discharge their Fiduciary, Trusteeship, Community interface and other duties.

Types of Boards and Styles of Governance

While the above may be the most common models, there are many others written and being presented in governance circles today. Yet another way of looking at this issue is by the type of Board – which may have significant bearing on the blending of the various governance components into an appropriate model of governance for each unique need:

- Ownership/Corporate Boards – with governance/management responsibility
- Advisory Boards – only required to provide advice, no legal 'governance status'
- Trustee/Pension Boards – to oversee assets, investments and/or disbursements
- Operational Boards – Boards that do not have the financial resources to hire full time CEO/staff, and so must do operational work to sustain the organization and well as Governance work.
- Marketing Boards – responsible for allocation of quotas to members and for bringing goods to market – i.e. Chicken Marketing Board, Wheat Board, etc.
- Resource Boards – oversight of the environmental management of a region or territory
- Government Services Boards – Federal/Provincial responsibility downloaded to a Regional Board for carrying out of the government's mandate: Health Board, School Board, Social Services Board
- Religious Board – Local "ownership" of some assets, in collaboration with Faith body.
- Charity Board – Fundraising and service delivery
- Professional Association Board – includes self-regulatory elements & professional practice advancement
- Political: Town/Band Councils, Provincial/State Legislatures, Federal/Central Cabinets – often seen more in the light of the "politics" in which they engage and the policy agendas created, these bodies have an equal responsibility to discharge good governance for the community of their mandate.

As the reader will realize, none of the 5 popular Models of Governance, nor the Types of Boards consideration, address the need for the creation of a strategic/operational framework also described in our starting definition of Governance. Often this is the most important and time-consuming requirement in the work of Governance. To this end, Banff Executive Leadership Inc. described a couple of years ago, The *REAL* Work of Governance Model as an attempt to outline and systematize the work of the Board and their interface with Management in accomplishing these important aspects.

The *REAL* Work of Governance Model – Creative Abrasion between Board & Management!
Ultimately, the responsibility of Governance boils down to two fundamental aspects:

1. ***Ensuring the sustainability of the organization, and***
2. ***Ensuring the relevancy of the organization's services and products.***

Expectations for improved Governance in all organizations are changing the dynamic of the Board room in a big way. Stakeholder expectations for organizational sustainability, community relevancy, transparency, and accountability are demanding new practices – ones that are <u>not</u> in the domain of the executives hired to run the organization 24/7/365; but important, often neglected leadership tasks in their own domain. These practices require more information sharing, and enhanced collaborative efforts between Board members and executive team members. Such new, sometimes formerly taboo relationships can make or break executive careers, and they can either paralyze or mobilize the overall organization itself.

Beyond policy making, Board members today must be prepared to put time and energy into the following areas of Governance work:

Network Scanning. Board members must understand the "business" of the organization and industry or professional sector in which they govern. This includes knowing the business model(s) at play, the target audiences for services, and the "flow" of products, programs, services, and money related to clients, members, competitors and collaborative suppliers/ researchers, and partners In addition, Board members must regularly scan for insights into how their organization inter-relates to other elements of the global marketplace.

Executives can assist Board members in this understanding through presentations, comparative or educational field trips and first-hand opportunities to experience the organization's products, programs and services. However, Board members also need to be regularly reading newspapers, journals, and internet sites so they can see trends, highlight issues, identify "value shifts" and more.

If executives do this work and Board members do not, there is an immediate knowledge - and thus power - imbalance. How can Board members ask good questions of management, develop policy, and establish priorities without a personal sense of these aspects? In this scenario, Board members must rely on the CEO and his/her executives to summarize their views, thus becoming dependent on executive insight and analysis. This is a sure recipe for unsettled feelings at the Board level, or worse, superficial discussion and analysis.

Where this Network Scanning is done only by executive team members, they must ensure they are given sufficient time to present to the Board, and then answer questions.

The possibility of the reverse situation exists as well: Board members who have done their due research and network analysis only to encounter executive members who have been so focused on all-consuming day-to-day operations that they have not taken the time to step back and conduct a strategic review.

Future Relevancy & Community Engagement. Enterprises handle this component in various ways. Some Boards insist on developing the Vision, Mission, and Values, themselves using a Strategic Planning Committee or Board as a whole. Others use a more advisory approach, expecting the CEO and executives to develop draft Strategic Positions, Vision, Missions, Values, even Branding guidelines for their organization – to bring to the Board for review, comment and approval. Regardless which approach is utilized, Board members need to adequately prepare themselves for this strategic thinking process.

Engagement of the community the organization serves is perhaps one of the most important elements of governance work there is. Board members need to make regular face-to-face contact with various constituencies served. They need to ask how the organization and its products, programs, or services are viewed by the membership, clients/customers and other stakeholders. A few well-honed questions, consistently asked by all Board members in a variety of forums, should bring important, comparable insight to the Board table. These insights can then be shared with executives, ideally before they develop the strategic guideposts for the organization with the Board.

Here, discussions of sustainability and relevancy at the community level (Governance work), meets the strategy, competitive analysis, value-building & positioning work from the operational perspective (Executive work). Equally empowered and informed in these areas, the governance-executive exchange can be dynamic, creative, not always in agreement, yet balanced and respectful.

Oversight, Perspective and Ethical Reflection. Ask 100 Board members of various organizations, “what is the role of the Board?”, and likely 95 will first respond with: “financial and performance oversight”!

Of course, these *are* important areas of governance work; and the US Sarbanes-Oxley/ Securities Exchange Commission, the UK’s Cadbury Committee/London Stock Exchange Guidelines, the Norby Committee/ Copenhagen Stock Exchange recommendations, EU and other capital markets plus the OECD have focused huge attention on this area in the wake of Enron, and others. However, simple oversight is not enough. Perspective from the Board is also crucial. So executives report that you served X number of clients, averaged 8.5 out of 10 on program evaluations, delivered hundreds of thousands of dollars in net proceeds from the various country operations. What lies behind these statistics? What was required to achieve them? What unintentional side-effects did we create while achieving these results? Did we act ethically – following our Values statement? Did we actually advance toward the outcomes of the organization or the role we have in our industry or community?

Ethically, Board must ask/define To whose standards to we hold ourselves? A global company that operates in several jurisdictions may have to report their financials/operations in different formats and answer to different standards. Can we establish one standard/approach that will meet all the varied, yet somewhat align with requirements?

This area of governance-executive interaction also has the potential to be relatively undefined – with many companies operating without clear Board or CEO goals and few criteria-based measures of success established. In the absence of clear outcomes and success measures, assessment of the CEO and organizational performance becomes rather subjective.

How do you measure Ethical practices? Some organizations take a minimalist approach, creating a Conflict of Interest Policy. As long as you don’t break this policy, it is assumed all is well. Unfortunately, interpretation of the policy is often a confusing experience! Others create a Code of Conduct, and expect every Board member, the CEO and all executives to sign it. This requires individual and team commitment to live by practices described in the Code. The next level of ethical pursuit is the establishment of a clear Values/ Principles statement, which is well communicated and discussed with all Board members, staff and suppliers. Annual Performance (or contractor) Appraisals review performance against the values as much as performance against operational targets. This moves beyond a minimalist/compliance mentality into much more of a leadership mindset. Finally, the highest level of practice, is a public statement of transparency and accountability, and the creation of a feedback, comment, and information process accessible by staff, customers, suppliers and community at large. Annual reporting of performance against clear outcomes and goals is then provided to both network members and the public with specific, meaningful measures cited.

Ultimately, the CEO is accountable to the Board for the achievement of results, financial reporting, and accomplishment of other critical success factors for the organization. In doing so he or she may choose to defer some elements in favour of others. The CEO may even prioritize or carefully “frame” their reporting in order to set the stage for important future projects or strategic insights they have to present to the Board.

Boards meanwhile are now enhancing the role of the Finance and Audit Committee to ensure integrity and transparency of their organization. Boards as a whole, Audit Committees, and/or the Board Treasurer often require direct and independent reports from plus access to the CFO.

Of course, in strong Executive teams, the CEO and CFO are "in synch" and transparent. They have aligned interests and performance objectives. They have shared insights with each other and reached common perspective to present to the Board. In dysfunctional situations, the CEO and CFO, may present things differently to the Board, destabilizing the Board's trust, and ultimately leading to more hands-on micromanagement by Board members. The Treasurer and/or Audit committee may even dip down into day-to-day operations in the name of transparency.

Risk Management. In addition to its concerns about sustainability, the Board must assess, balance, and prioritize the use of organizational assets to achieve its strategic goals. While the same holds true for the executive team, the Board must become adept at looking for indicators that the organization has both the ability and capacity to achieve its plans. They should ask good questions regarding the Strengths, Weaknesses, Opportunities, and Threats with respect to:

- Financial Capital
- Human/Intellectual Capital
- Relationships with clients and suppliers
- Social Capital with community and government
- Structural Capital – organizational design, infrastructure and technology

Executives must feel comfortable in raising concerns to the Board about their *capacity* to achieve Plan, and the potential risks they see lying ahead. Board members need to reflect on their role in finding additional capital or resources in order to achieve the organization's goals?

So, while it is clearly governance work to assess risk and mitigate it through prioritization or accessing additional capital; executive team members have to be sure they can deliver on their plans, ethically, and with the given assets.

Diplomacy/Influence Leverage. Board members have a lot to offer in this governance work area. They can be extremely credible with government, industry panels, and funders/investors. Most often they are the best ambassadors with the general community.

Clearly, the CEO and senior executives also play important roles in providing technical knowledge or on-the-ground follow-up that helps leverage the influence of Board members. This is particularly noticeable in the Health Services sector.

Board members can provide advocacy to politicians, speak to media, and build relationships with key influencers and/or alliance partners. Indeed, ***this is high value, potentially high impact governance work***. It also requires carefully coordinated support of staff providing effective technical and operational leadership, day-to-day interface with government employees, and development of policy or advocacy briefs, meeting arrangements, presentation preparation, research, and analysis.

Putting Models To Work for Your Governance Needs
Today's governing bodies are all looking for ways to continuously improve their practices and build trustful relationships with stakeholders and community.

A review of the various governance models described above, combined with an assessment of the specific nature of your governance responsibility-type may be an excellent exercise for your next governance/strategic retreat. All the models have elements that Boards of various enterprises can adopt and recombine together to create a dynamic, yet disciplined approach to improved Governance for your situation A reliance on only one model to the exclusion of the others may mean you are missing some very important aspects of Governance performance and may indeed have some exposure or liability as a result.

What will be the Top 5 most important improvements your Board can make to its practices this coming year?

Exploring the Web!

This month, the connections below take you to sites with more perspectives, commentary and discussions of Governance Models and adaptations:

"Corporate Governance & Accountability in the Marketplace" by the Institute of Economic Affairs in UK. Click on the PDF version to get the full 122 page report. This provides both an historical and contemporary look at how our Corporate Governance systems & models have evolved. It addresses the Anglo-American approach, German/Japanese, and others. http://www.iea.org.uk/record.jsp?type=book&ID=227

A "structural model" view on Pension Fund & Corporate Governance from an Anglo-American viewpoint.
http://www.hull.ac.uk/futgov/Papers/clarkpfunds.doc

Models and approaches for e-governance and e-democracy. This is an excellent foundational read for those starting to explore the concept, AND it has excellent links for those already in the field to get more in-depth information and ideas. Remember, there IS more to political governance than just politics!
http://www.publicus.net/articles/cliftegovdemocracy.pdf

Official website of John & Miriam Carver and their Policy Governance Model.
http://www.carvergovernance.com/model.htm

Official website of John Por and Cortex Applied Research.
http://www.cortex-consulting.com/articles.htm

Another view of looking at different approaches to Board Governance in the NFP sector.
http://garberconsulting.com/governance%20models%20what's%20right.htm

A look at potential models for corporate governance in Japan compared to those in Germany.
http://www.rieti.go.jp/cgj/en/columns/text_001.htm

A passionate response on the value of Consensus governance processes!
http://www.sudval.org/archives/dsm4/0372.html

Models of Corporate Governance and Employee involvement in Russia and Post-Soviet Economic Transition. A fascinating insight into societies transitioning into a market economy and how corporate governance and re-thinking traditional models, will have impact on their country. http://papers.ssrn.com/sol3/papers.cfm?abstract_id=997965

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