

BOARDROOM SECRETS



CORPORATE GOVERNANCE
FOR QUALITY OF LIFE

YILMAZ ARGÜDEN



Recent high-profile corporate failures have clearly demonstrated that good governance is the key to sustainability of the corporation. Good governance is a lot more than compliance. It is a culture and a climate of consistency, responsibility, accountability, fairness, transparency, and effectiveness that are deployed throughout the organization (CRAFTED principles of governance). This book focusses on the behavioral aspects of good governance and helps address questions such as:

How confident are you that the Board of Directors of your company is providing the right kind of guidance and oversight?

Do you think that in your company the right balance is achieved in the following areas?

- short-term v. long-term performance
- risk v. reward
- ethical considerations v. market practices
- competing interests of different stakeholders

Does your Board pay adequate attention to strategic planning processes, processes for identifying major risk areas, communication and disclosure policies, and effectiveness of internal control systems?

Is your Board effective in terms of critical but constructive questioning and identifying and addressing key risk areas?

What is your Board doing to improve its own performance?

Boardroom Secrets focusses on the required structure, processes, information needs, culture and behaviors so that any Board of Directors is able to ensure good governance.

"A pertinent and timely read in these difficult times." – **Baron David de Rothschild**, *Chairman, Rothschild*

"Yılmaz Argüden's untiring campaign to promote good corporate governance in Turkey is largely responsible for the priority it has today among both businesses and the public at large. Drawing on his vast experience, Dr Argüden offers invaluable insights and universal guidelines for good governance. I have no doubt that *Boardroom Secrets* will become a reference book for businesses everywhere." – **Bülent Eczacıbaşı**, *Chairman, Eczacıbaşı Holding*

"Shareholders, directors and top managers will welcome this wise, insightful, and practical book. I know of no better single source for getting it right in the boardroom. Read these secrets, apply them diligently, and improve your board's performance." – **David R. Beatty**, *OBE, Founding Managing Director, The Canadian Coalition for Good Governance*

"Dr Argüden's book focussing on governance as a culture and a climate is based on insights coming from long experience and will be invaluable to all who must try to rebuild the world economy on more solid foundations." – **Kemal Derviş**, *Head of UNDP*

"The global financial and economic crisis is above all a corporate governance crisis. Dr Argüden's book provides timely insight and guidance on how the fundamentals of good governance can be improved." – **Klaus Schwab**, *Founder and Chairman, World Economic Forum*

"Perfect timing for a book containing carefully researched, cross-national prescriptions for ethical and effective corporate governance. This should be a valuable resource for leaders in both the commercial and non-profit sectors." – **Michael D. Rich**, *Executive Vice-President, RAND Corporation*

"In these times of serious economic crisis the value of strong corporate governance becomes even more apparent. Yılmaz Argüden's book shows this in a clear and concise way." – **Mustafa V. Koç**, *Chairman, Koç Holding*

"In this wise and practical book, Yılmaz Argüden argues that trust lies at the heart of corporate governance. It will be of significant use in guiding the thinking of board members and company stakeholders alike." – **Roger Barker**, *Head of Corporate Governance, Institute of Directors (London)*

"I wish *Boardroom Secrets* had been available when I was getting a start in business 35 years ago. I would have read it line by line and my business life would have been much more effective. New generation business leaders are fortunate to have this reference book available for them." – **Tuncay Özilhan**, *Chairman, Anadolu Efes*

Boardroom Secrets Introduction*

Trust is the foundation of sustainable success. Companies who earn the trust of their stakeholders are able to mobilize more resources throughout their value chain to achieve sustainable success. The essence of good corporate governance is ensuring trustworthy relations between the corporation and its stakeholders. This is the fundamental reason why good corporate governance is being embraced by companies in diverse industries, small and large, and publicly or privately owned, throughout the world.

Good corporate governance is the key to attract financial and human capital to the corporation, strong business partners to the value chain, and to ensuring sustainability of value creation. **Corporate governance** refers to the **quality, transparency, and dependability** of the **relationships between** the shareholders, board of directors, management and employees that **define the authority and responsibility of each** in delivering sustainable value to all the stakeholders.

While good governance is the responsibility of all those who conduct the relations with stakeholders, it is the board of directors who sets the tone at the top and are responsible for ensuring that the right climate and culture exist within the organization. The key to good corporate governance is ensuring that the principles of **Consistency, Responsibility, Accountability, Fairness, Transparency, and Effectiveness** are **Deployed (CRAFTED)** throughout the organization. Applying CRAFTED principles is a *sine qua non* of sustainable success. Any lapse in applying these principles results in failure of even global giants such as like Enron, Arthur Anderson, or more recent notable corporate casualties at the blink of an eye.

Earning the trust of the stakeholders is the key to mobilize their resources towards a common vision. **Transparency** in the relationships is the key to earning that trust. Success requires **effective** utilization of resources entrusted to a corporation. Being **fair and accountable** to all the stakeholders whose resources are entrusted to the corporation is the key to sustainability of access to those resources. The communication and behavior of each institution influences not only how its own resources are utilized, but also those of its stakeholders. Therefore, **consistency** of the policies of a corporation is the key to ensuring that right expectations are formed throughout the value chain, thereby making the whole value chain stronger. Value creation requires measured risk taking. Risk is the kin of profit. Therefore, taking initiative and **responsibility** which naturally involves risk taking is a key element of value creation. Sustainability of success requires continuous improvement and innovation. This in turn requires the participation and involvement of all in the organization. Hence, creation of a climate that emphasize good governance principles and **deployment** of a good corporate governance culture is the key for sustainability.

Executives are responsible for managing a corporation on behalf of its shareholders. In order to ensure that the risks taken by management on behalf of the shareholders are consistent and balanced and to prevent any potential conflicts of interest between the management and shareholders, an effective guidance and oversight are required. Provision of such a guidance and oversight, requires an in depth knowledge of the industry dynamics and company's competitive positioning. The sustainability of an organization requires striking a fine balance between risk and reward, and ensuring that there are effective internal control mechanisms. This in turn requires a fair process to challenge the management about their decisions, particularly on strategic choices. The board of directors is the key to providing such guidance and oversight. The relevance of the experience and expertise of the board members to the corporation's business and risk profile, their integrity, independence, involvement, and their understanding of fiduciary duties, are critical for ensuring the sustainability of the corporation.

* Yılmaz Argüden, "Boardroom Secrets: Corporate Governance for Quality of Life" 2009 Palgrave Macmillan reproduced with permission of Palgrave Macmillan. This extract is taken from the author's original manuscript and has not been edited. The definitive version of this piece may be found in **Boardroom Secrets** by Yılmaz Argüden which can be purchased from www.palgrave.com

Among the most important assets of a corporation are its human resources, especially its management team. The competencies and performance of this team must be assessed and new members introduced should the need arise. Another factor that will determine the future of a corporation is the introduction of a fair reward mechanism designed to maintain a high level of motivation among team members. A board that operates soundly will ensure that these assessments are conducted in a fair and balanced manner.

The mission of the board, as the highest decision making authority, is to guide the corporation in a proactive manner and, in the long term, to ensure that value is created for its shareholders. One of the most important elements that pave the road to success is the corporate strategy. The essence of strategy is choice. Therefore, each rejecting another. Taking one road means eliminating another. Strategic choices are intended for the future, whereas the future is uncertain. The quality of strategic decisions can be enhanced by boards that scrutinize these strategic choices based on the experience of their members. Therefore, having a board with sufficiently diverse experience, and critical and independent thinking skills to challenge the strategic choices from multiple perspectives increases probability of success.

The fiduciary duties of the board require them to oversee the protection of corporate assets, tangible as well as intangible. For example, protection of the reputation of the corporation in the minds of its all stakeholders requires board oversight not only from a financial or legal perspective but also with respect to value creation capabilities.

Therefore, the composition, processes, and culture of the board of directors are critical for the sustainability of the organization. Adherence to good corporate governance principles is a precursor to continuously improving management quality. In many countries where families hold controlling stakes in the corporations, the relationship between the board and the majority partner is often the greatest obstacle to the development of corporate governance. For this reason, a critical priority for the board of directors is to assume responsibility for guidance and oversight of the corporation rather than implicitly assuming the role of an advisor to the controlling shareholder. Boards are responsible not only for looking out for the interests of an institution's largest shareholder but also for overseeing the interests of other small shareholders and all stakeholders alike¹.

The board of directors is among the most important strategic assets of any institution. Consequently, the competencies and experience of the board members, and their ability to remain independent and to adhere to the principles of good governance, bear great importance on the institution's success and sustainability.

Corporate governance is relevant not only for large publicly traded companies, but also for SMEs, family businesses, and even for non-profit organizations, as each of these organizations is dependent on sustainable access to the resources of other stakeholders, and would benefit from balanced guidance and oversight. Therefore, having a reputable board may be useful in avoiding family conflicts, in attracting talent, and in improving the reputation and value of the organization. A good board can also aid in attracting partners, in raising capital and in supporting the establishment of trustworthy partnerships with the stakeholders.

In order to be competitive, organizations should apply good governance principles. This is so, not due to some external pressure such that from the OECD, EU, World Bank, IMF, shareholder activist or any regulatory agency, but in order to ensure proper management of risks, to be more competitive, and to gain access to more resources for continuous development.

¹ In some jurisdictions, such as the United States, the main responsibility of the board members is defined as protecting the interests of shareholders, in other jurisdictions such as Canada, directors' duties require them to carefully consider the reasonable expectations of all stakeholders (see December 2008 dated decision of Supreme Court of Canada on BCE case). The Dutch Corporate Governance Code also assigns the responsibility for reasonable and fair dealing with all stakeholders to the boards. The author is of the view that for sustainable success a corporation as an on-going concern needs to balance the expectations of all stakeholders.



Yılmaz Argüden is a leading strategist, advisor, and board member of major public and private institutions, as well as of non-governmental organizations. He is the Chairman of ARGE Consulting, a leading management consulting firm based in Istanbul, Turkey. ARGE has been recognized at the European Parliament as one of the best three companies "Shaping the Future" with its commitment to corporate social responsibility and is the first Turkish signatory of the Global Compact. He is also the Chairman of Rothschild investment bank in Turkey. He has served on more than fifty different boards and is currently the Chairman or member of corporate governance committees of Coca-Cola İçecek, Vestel, Yazıcı Holding, and Inmet Mining (based in Toronto). He is Adj. Professor of Business Strategy at the Bosphorus University and the Koç University, an author of numerous books, and a columnist focussing on business and strategy issues. He is a recipient of numerous leadership, distinguished citizenship and career awards, and was selected as a Global Leader for Tomorrow by the World Economic Forum for his commitment to improving the state of the world.

www.arguden.net/eng/index.htm