LECTURE 04: CORPORATE GOVERNANCE

A- Board Organization:

Corporate governance is the way a company is organized and managed at the highest level. This can have a critical influence on the company’s performance and behaviour.

A company’s board of directors includes:

- executive directors: the chief executive and other senior managers such as the finance director.
- non-executive directors or non-execs: outsiders with management experience who are invited to sit on the board, bringing their expertise and an outside view. Large investors in the company like pension funds may also have seats on the board so that they can influence how the company is run.

In some countries such as Germany, there are two boards. Above the management board is a more senior supervisory board.

B- Separation of Roles:

Another key issue in corporate governance is whether the most senior job in a company should be split into two or not. Should the roles of chairman/chairwoman and chief executive be held by one person, or should there be a separation of these two roles?

Some people say that these two functions should be separated in order to avoid concentrating too much power in one person’s hands. Supporters of combining the two roles, however, say that this gives the company stronger leadership.

C- Rewards for success (and failure):

Also important are executive remuneration or compensation. Top executives are rewarded for success in the form of high salaries and share-options (BrE) or stock options (AmE): the chance to buy shares in the company cheaply. These highly-paid executives are often called fat cats by their critics. Executives say in their defence that share-options are one of the incentives that can make them perform better.

But they may also be ‘rewarded’ for failure, with high severance payouts or payoffs when they leave the company following poor performance.

Executive pay is becoming an increasingly sensitive issue - for example, executive pay in the UK has risen three times faster than average pay in the last five years. Company boards may appoint a remuneration committee to make decisions in this area. And in the UK there are proposals that shareholders should have the right to vote on executive remuneration.

4.1. *Two articles have been mixed up. They contain expressions from A, B and C opposite. Which paragraphs make up each article? (The paragraphs are in the correct order. Article 1 contains four paragraphs; the first is "a". Article 2 contains four paragraphs; the first is b.)*

a- Article 1: Corporate safeguards go back to the board

A large majority of top executives in Britain have; given the thumbs down to proposals designed to strengthen the role of non-executive directors in the boardroom. A survey by the Confederation of British Industry showed that 82% of FTSE-100 chairmen feel that their role would be undermined by proposals contained in the Higgs report released in January.

b- Article 2: Rewards for failure are too high, says Lord Mayor

The City needs to tighten up its standards of corporate governance to restore public and investor confidence, according to the Lord Mayor of London, Gavyn Arthur. It was unacceptable for failure to the almost as well rewarded as success and for executives to take decisions designed to trigger short-term share options rather than act in the long-term interests of the company.

c- 'We have to have an ethos where the long-term stability of the company is what matters most; where it is bad form and seen to be bad form to the taking actions to generate short-term benefits and share options." Mr. Arthur is expected to use a keynote speech at a dinner to be attended by Trade and Industry secretary Patricia Hewitt this month to highlight the need to bolster credibility.

d- The report from Derek Higgs, a former investment banker, called for an enhanced role for non-executive directors, as part of a stream of proposals designed to prevent an Enron-type scandal in the UK. Specifically, the Higgs report called for an independent non-executive director to chair the nominations committee, which nominates people to join the board, splitting the functions of chairman and chief executive, and the appointment of a senior independent director to liaise with shareholders.

e- Ms. Hewitt has already announced a review on the issue of rewards for failure. However, last month Labour blocked an attempt by Tory MP and former Asda boss Archie Norman to change the Companies Act to allow directors to challenge executive payoffs.

f- But in the CBI survey, most chairmen believed that the Higgs proposals would undermine their position and lead to divided boards and therefore hamper the way they run their businesses. "What the chairmen are saying is that they need to have unified boards, especially in difficult economic times, " said Digby Jones, the CBI director-general.

g- Chairmen of the FTSE-100 companies can also argue that corporate governance in the UK already meets high standards, building on past milestones such as the 1992 report by Sir Adrian Cadbury in 1992 and Sir Ronald Hampel in 1998. Be that as it may, Enron and WorldCom changed the corporate landscape. Those mammoth scandals led to major reforms in the US, notably the Sarbanes-Oxley law. which had the creation of an accountancy oversight board as its centerpiece. Once the US started overhauling corporate governance practices, the rest of the world was forced to go some way to meeting these new best practices.

The Guardian

h- Mr. Arthur argues that the current situation cannot be allowed to persist. "I can't bear to see failure being almost as well rewarded as success. It is morally wrong for those who have destroyed their company to walk away with an obscenely large payout. It does a disservice to investors and to public confidence,

The Guardian