CREATING AN EFFECTIVE BOARD AND CORPORATE GOVERNANCE STRUCTURE

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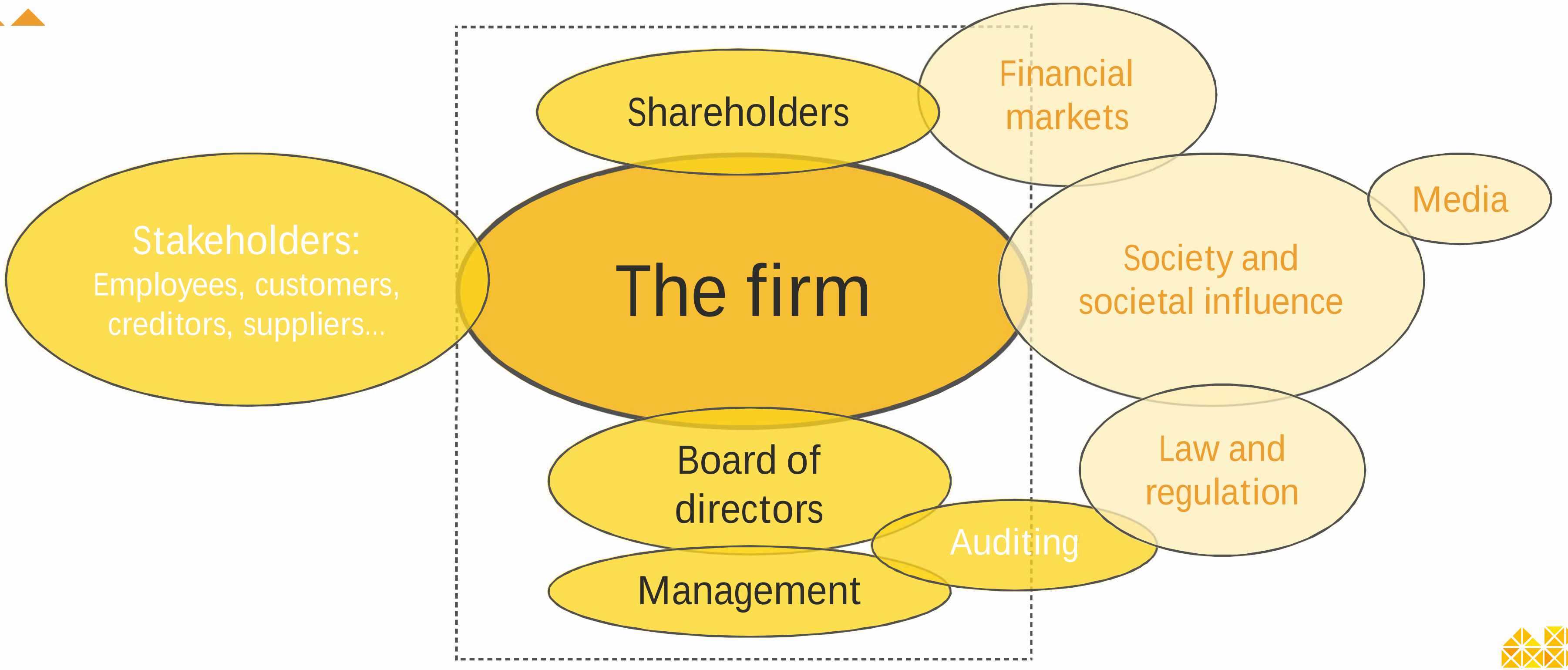
Corporate governance

- Corporate governance can be defined as the set of institutional structures, processes, and rules that guide the decision-making and control of firms
- Corporate governance structures are influenced by legal rules, social norms, and best practices
- Effective corporate governance framework:
    1) Ensures long-term value creation for the firm's shareholders
    2) Aligns the interest of the firm's shareholders, management, and other stakeholders
    3) Promotes accountability, responsibility, and transparency

Corporate governance



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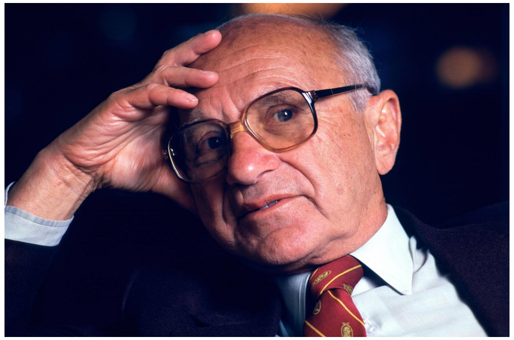
Corporate governance and long-term value creation

- Shareholder-oriented view

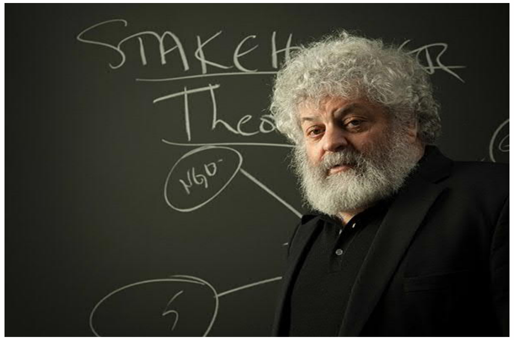
  Milton Friedman:



  The social responsibility of a firm is to increase its profits

- Stakeholder-oriented view

  Edward Freeman:



  Shareholder value is created by forging relationships with the firm’s key stakeholders

Board of directors

- The board of directors is the most important internal governance mechanism within a firm
- The board is responsible for monitoring and controlling the major long-term strategic decisions of the firm and ensuring that the firm acts in the best interests of its shareholders
- The board plays a key role in long-term value creation!

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Board of directors

- The board of directors has two key functions that contribute to long-term value creation:
  1) Advisory role
  2) Monitoring role
- In its advisory role, the board interacts with the firm's management in strategic decisions and direction
- In the monitoring role, the board has fiduciary duty towards shareholders to monitor the firm and its management

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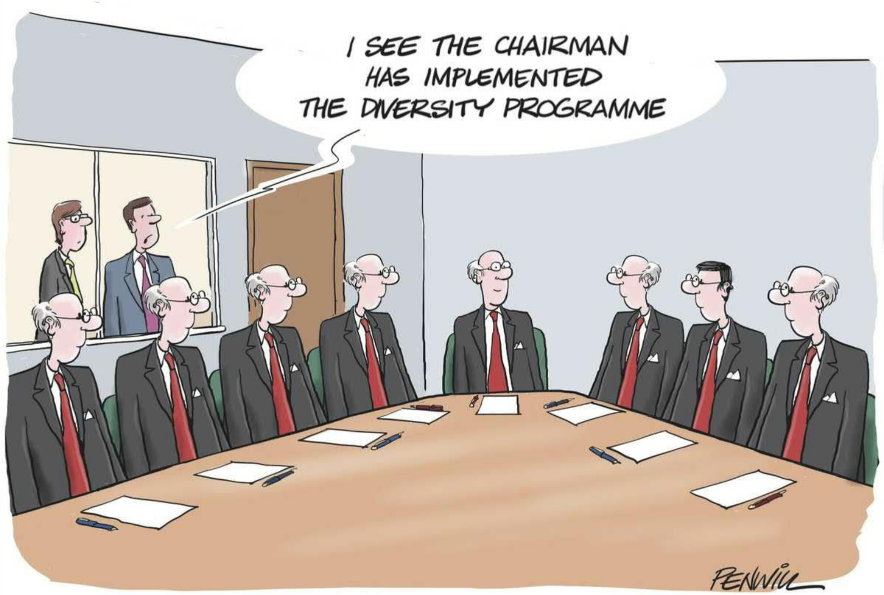
Board structure

- Boards are typically described and assessed in terms of observable characteristics:
  - Board size (medium-sized +)
  - Board independence (+)
  - CEO-chairman duality (-)
  - Board diversity (+)
  - The number of board meetings (?)
  - Board meeting attendance (-)
  - Average tenure of directors (?)
  - The number of other board affiliations of the directors (-)
  - Staggered/classified board (+)
  - Board co-option (-)
- Empirical evidence suggests that some of these observable characteristics are associated with the advisory and monitoring functions of the board

The anatomy of corporate boards in the U.S.

- 11 directors
- 8-9 meetings per year
- About 80 % are independent directors
- Average director age is about 61 years
- About 30 % are female
- CEO-Chairman duality in about 60 % of the firms



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Board independence

- Independent judgement is critical to the advisory and monitoring functions of the board
- Independence ensures that the board makes objective decisions and acts in the best interests of the firm
- Independence reduces managerial influence, entrenchment, and “empire building”

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Board diversity

- Diversity brings a variety of different perspectives to decision-making and reduces group-think
- Gender, age, experience, education…
- "What if Lehman Brothers had been Lehman Sisters?"
  (Christine Lagarde, 2010 WEF)
- Beware of tokenism and faultlines

"Today's theme is 'Getting Beyond Group Think'."

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Key takeaways

1) Effective design and implementation of corporate governance practices is important for long-term value creation
2) Effective corporate governance structure aligns the interest of the firm's shareholders, management, and other stakeholders
3) The board of directors plays a key role in corporate governance within its advisory and monitoring functions
4) Board independence and diversity foster effective monitoring and oversight

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THANK YOU!

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