CRSA Forum 16 December

Diagnosing Governance and Risk Management then Future Proofing Them

On 16 December 2016, the CRSA Forum was kindly hosted by the Department of Health at Richmond House, Westminster. The meeting was an interactive facilitated discussion on why corporate governance and risk management have failed to prevent frauds and financial crises. The 25 participants included governance and risk experts, academics and journalists. We diagnosed why current governance and risk management systems have seemed ineffective in many cases and what could be done in four different scenarios of the future.

Peter Bebb of Perendie began by reminding us of recent corporate collapses, corporate wrong doing including mis-selling, fraud, rogue trading, poor controls over corporate assets resulting in security beaches and loss of physical assets and oil spills, and failure of care in the NHS and the reputation damage resulting from these incidents. Nations too have suffered from governance failure as exemplified by the inability in 2008/9 of Greece, Portugal, Ireland, Spain and Cyprus to repay or refinance their debt without external support.

We were asked if there is any evidence that corporate governance and risk management is useful or that its cost is less than its benefit. It would be difficult, if not impossible, to prove that absence of governance problems was a result of good governance, an absence of mistake or wrong doing or because no one has noticed mistake and wrong doing.

Possible weaknesses in corporate governance and risk management include:

1.   They are the concern of only a few people
2.   They try to stop people doing things rather than make them do the right things
3.   They pay insufficient attention to incentives
4.   They don't take human factors into account
5.   They work against psychology
6.   They provide no defence against self-interest
7.   They are over-complex and obscure
8.   They are expensive nut no one calculates their full cost
9.   corporate governance and risk management reports:
     a.   Retrospective
     b.   Out of date
     c.   Unchangeable
     d.   Obscured by detail
     e.   Incomplete
     f.   Manipulated

     and don't

     a.   Tell you whether the rules are being followed
     b.   Tell you whether the rules are likely to be followed
     c.   Say how the organisation will perform in future
     d.   Mitigate risks
     e.   Regulate behaviour

    f.   Support decision-making

In small groups we reflected on the causes and Tweeted our opinions of the causes of failure.

    A.   Recognising & agreeing risk plus complexity of risk

    B.   Personal interest and lack of personal responsibility on individual board members

    C.   Lack of transparency or ethics

    D.   Lack of appropriate personal responsibility (1st)

    E.   Short term targets, over long term culture (3rd)

    F.   Poor ethics and accountability at the top

    G.   Board clarity & accountability

    H.   Governance is very challenging in an ever changing world

    I.   lack of protection of whistleblower, rule breakers don't often lose out (2nd)

    J.   Not just the rules, culture too

One group talked about the theme of individual and shared responsibility within a company and how the lack of each has contributed to corporate governance failures. It was agreed that a company should be set up in such a way that individuals are treated as responsible adults where relationships are built on trust and people allowed to go about their jobs with a minimum of interference. In this individuals should understand the culture and ethos of their company and the importance of their role in the wider context of the company. Rules on governance should be explicit, transparent and clear to people at all levels of a company. Individuals must be accountable in a legal sense and appropriate deterrents must be put in place, such as the threat of jail. It should, the group thought, be made clear how the board of directors in a company, (especially private companies), are held accountable for their actions.

We all voted on which were the most important. The first choice was 'lack of appropriate personal responsibility', the second was 'lack of protection of whistleblower, rule breakers don't often lose out' and the third was 'short term targets, over long term culture'.

We then Tweeted our suggestions for action. These were:

    A.   Culture and values (1st)

    B.   Clarity of purpose, enabling appropriate behaviour (3rd)

    C.   Individuals understanding what is expected

    D.   Recognising & agreeing risk plus complexity of risk

E.   Create an international body who is able to hold the board to account

F.   Accountability & audit design

G.   Culture change - incentivise not penalise (2nd)

Getting culture and values right was seen as the most important, followed by culture change where based on incentives for a desired culture rather than penalties for those who misbehave) followed by having clarity of purpose and enabling appropriate behaviour. Clearly all three actions are related with the second and third serving to reinforce the first.

We then moved on to exploring the future role and challenges for governance and risk management using four scenarios that have been used by Gill Ringland and her colleagues from SAMI Consulting in financial services, manufacturing, professional services firms and in a global supply chain conference to develop new insights. We considered what the world might be like in 2040. In each scenario we assumed

1.   The global population will grow and get older
     •   Most of the additional people will be in Africa and Asia
     •   Turbulence as the world rebalances to new centres of economic power
2.   New centres of population may not share the value systems or structures, and behaviours of the West
3.   Technology (info, cogno, bio, nano) will continue to introduce changes in personal capacity and lifestyles
4.   Ecological, energy and environmental limits will be tested or breached
     •   Population increases
     •   Population lives in cities (70% by 2040)
     •   New middle class uses electricity, travel, eats meat

We considered the future developing along four possible paths. In one, called *'Second Hand'* the world would seem most similar to today and have developed as a result of 1 to 4 above but without any significant disruption, in the second, '*Globalisation*' the main change would be the increased importance of virtual (web based) connections with less significance given to geographical place. This could cause strains to the existing world order and nation states would be weaker.

In two of these scenarios there were changes in the world order which could have resulted from a major systemic shock. In these two, in *'City Societies*' geographical place is still important but cities essentially took the place of nations. Cities become wealth clusters or brands, nation states fail and democracy, capitalism and western values compete with other organising concepts; and in *'Affinity Groups'* society has re-formed around affinity groups; multiple value systems are accommodated in a single geography. Democracy is not seen as universal good and there are complex arrangements of nation states and communities of affinity group.

We then formed groups to consider *Globalisation, City Societies* and *Affinity Groups.* The *Globalisation group* considered that most people would work virtually and anywhere in the world. There would be more isolation. Traditional management and governance controls may not work if people did not know what others were doing creating problems with lack of accountability a

dereliction of responsibility. Whistle blowing is an important issue at present; how might that work in future? Virtual working could however make it easier for corporations to control their staff, with unseen but all seeing eyes knowing where staff are and what they are doing.

In the *Affinity Groups* scenario groupings and people with whom others identify could take the form around common languages, corporations and conceivably intelligence as in Audous Huxley's Brave New World where the population was stratified according to intelligence with Alphas at the top and Gammas at the bottom. Current concepts of control and responsibility may no longer be relevant or needed if people share a common purpose. Eg the current problem with formal incentives incentivising the wrong behaviours would be less if people have a common purpose. However there could be rivalries eg between all powerful big corporations and other groups.

In the *City Societies* scenario a newspaper headline might read 'London's per head wealth 10 times that of Birmingham' as there are winner and loser cities. International affinity groups, including corporations, would be more powerful. Staff in corporations would have different cultures in different cities or they may try to impose a common culture across all the cities where they have staff. There would need to be trade agreements between cities and some commonality in the legal systems particularly around law of property. Cities would have good internal controls but there could be chaos externally. The more successful global cities might negotiate common frameworks benefitting everyone or they may benefit only the cities concerned with other cities becoming relatively poorer and ultimately disintegrating or being taken over by other cities. Some cities may create armies and try to expand by conquest. Others would expand by succeeding in the market place.

The four scenarios are not intended to be mutually exclusive. People felt that a combination of *City Societies* and *Affinity Groups* could be quite likely.

So what should we do today? The future is unknowable but consideration of these scenarios could help us better understand the world as it changes and spot what is happening earlier. The view of the room on corporate governance was very much around having a capitalism with social responsibility and having a shared sense of values and ethics. We should all try to view companies and the systems within which they operate from a boarder perspective looking down as if from a helicopter or observing it from several distant vantage points, or from the points of view of different stakeholders. We should focus on purpose but beware people whose purpose is world domination.

Globalisation, in some form, seems likely to continue in all four scenarios. Governance will need to embrace technology. In *City Societies* there must be accountability for leaders and transparency for cities and organisations.

It was suggested that the old political labels left and right are last century and are no longer appropriate, For example some of what our present Prime Minister is saying on business is well to the left of the previous Labour government. A better future could be one where people focus on responsibilities rather than rights. It was pointed out that ethical companies make more money and that should be a good incentive.