INTERNATIONAL ACADEMY for QUALITY

The Impact of Corporate Governance On the Quality of Management

Project Coordination:
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The impact of Quality on the effectiveness of Boards of Directors

The aim of this paper is to help business men, directors and consultants in the implementation of a sounding board practice, which will result in a better quality of management In doing so we address:

-why quality of the Board of Directors is a key subject today

-how to evaluate and measure the performance of Board of Directors for a wide range of companies based on their maturity level in corporate governance

-how to make Board of Directors assessments

The relevance of this paper can be seen in the comments of Ira Millstein , Chairman of the Private Sector Corporate Governance Forum of the World Bank, made to the authors.

"You may wish to know that the New York stock exchanges listing standards require that a listed company have a set of corporate governance guide lines and principles that address among other things, board evaluation. Additionally NYSE´s listing standards also require that the key committee charteres provides for annual evaluation of committee operations"

From the President of the International Academy for Quality

For the quality profession to turn its attention to corporate governance is an entirely appropriate undertaking. Just as we long ago made the move from an inspect-and-fix mode to a prevention mode, corporate governance is undergoing a similar transformation and I believe our experiences can be transferable.

These developments are gaining ever more attention around the globe, as evidenced, for example, by the requirement that firms listed on the London Stock Exchange have a plan for ensuring quality of governance. And there is growing recognition that ensuring excellence in the governance process is not a burden; rather, it is an obligation of leadership that offers an opportunity to distinguish one's organization from all others.

We in the International Academy for Quality are pleased to undertake this corporate governance study and to present the ideas of thoughtful leaders such as Armand Feigenbaum, Gregory Watson, Marcos Bertin, Hugo Strachan, and Tito Conti.

A principal aim of IAQ is "to promote research into the philosophy, theory and practice of all activities involved in achieving quality for the best use of world resources…" . This is an ambitious charter that compels us to branch out and expand the scope of our inquiries and interests. It leads us to projects such as this examination of the interconnectivity of corporate governance and quality management. We are hopeful that readers will find it a useful contribution to advancing worldwide organizational excellence.

Spencer Hutchens
President
International Academy for Quality

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THE FAVORABLE BUSINESS POWER OF EFFECTIVE CORPORATE GOVERNANCE

Armand V. Feigenbaum
President and CEO General Systems Company

One of the most basic principles of business success recognized by those of us who have spent our careers in corporate leadership is the great management value, the absolute organizational strength and the essentiality to economic and social responsibility of effective Corporate Governance.

Effective Corporate Governance is key to generating and supporting continuously strong and meaningful corporate profitability and growth in today's brutally competitive global markets. It is fundamental to a company's integrity throughout its human, customer, public and financial affairs that is the necessary condition for the genuine and lasting business growth of today's twenty first century organization.

And our experience shows that effective Corporate Governance is a key foundation for providing the all-important business operating results of:

- Empowering a company-wide culture of superior performance, and
- Providing and emphasizing consistent customer value leadership throughout all the company's products and services.

A fundamental determinant of effective Corporate Governance is the clarity and visibility of the responsibilities and ongoing activities of the company's Board of Directors. This requires, among other key demands, the specificity of the definition and assurance of the responsibilities and relationships within the Board and among its members and between the Board and the CEO.

And, because what is measured and evaluated well in corporate affairs will be managed and implemented well in corporate action, a basic demand for establishing and assuring such effective Corporate Governance is a clear, systematic and well structured process for its measurement and evaluation. This report on *The Impact of Corporate Governance on the Quality of Management* provides such a process for evaluation of a Board of Directors.

It brings together and systematizes in a clear and tested structure data, experience and information from responsible applications and sources. Moreover, as has importantly been taking place with great value in other key areas of corporate activity, this work benefits from utilizing the new focus on quality with a more powerfully productive role for its

principles, methods and disciplines. The report also discusses information regarding quality assessments aimed at improving Corporate Governance as well as focusing on review of Corporate Governance in terms of quality at the top.

This report brings together the research, experience and insights of some of the most highly qualified and experienced quality and management experts. It provides an important resource and guide for the men and women who are committed to effective Corporate Governance and to application of principles and methods in terms that fit today's new governance demands.

CORPORATE GOVERNANCE REQUIRES QUALITY LEADERSHIP

Gregory H Watson
President and Managing Partner
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Good governance is often observed in its absence – the failure of business leadership to provide adequate due diligence or responsible oversight. In recent years abuse of the top leadership positions of public companies has lead to escalating emphasis on issues related to shareholder responsibility, corporate ethics, and executive compensation. In response to the recent Enron – Arthur Andersen and the Worldcom crises, there has been a call for reform in administration of governance with an emphasis on increasing ethical behavior of management and avoidance of conflict of interest among the competing corporate stakeholders. This interest has focused on corporate reform in both public and private sectors for the way that top executives and board members are held accountable. This call for transformation in the 'rules of governance' is projected to grow as dissatisfaction with the execution of governance provides justification to focus attention on the issue: what is ***good*** governance? Good governance delivers benefits to each organizational stakeholder – but the question that is debated is which stakeholder rights are most significant. Good governance plays an important role in the process of assuring customer satisfaction with the management of business in all areas from the flawless manufacture of products and consistent execution of services. It also assists in assuring employee satisfaction with such issues as equitable distribution of fair compensation packages and security of the work environment. The way an organization is governed particularly assures the shareholders that management will make all decisions at 'arms length' and consider ownership's fiduciary interests as a priority. In short, governance defines the value context of the organization and shapes the direction of its mission while setting the long-term business perspective for ethical conduct and effective public responsibility. This paper focuses on the role of quality as a management practice for establishing and implementing processes that support good corporate governance and assure long-term, mutual success for all stakeholders in the modern corporation.

Introduction

After the American revolution of 1776, the United States Federal government transferred to state legislatures the power to control "crown corporations" – the group of companies established by the King of England (e.g., such as the Hudson's Bay Company and the East India Trading Company). The states defined the purpose of a corporation through the charter that it issued (also called a certificate of incorporation). In exchange for the charter, a corporation was obligated to obey the laws, serve the common good, and cause no harm.

Early state legislators wrote charter laws and actual charters to limit corporate authority, and to ensure that when a corporation caused harm, they could revoke its charter. The responsibility for establishing a framework of authority for corporations was exercised by the legislative branch of government, not by the judiciary or executive branches. This had an effect of maintaining close oversight of the corporation by the public's duly elected representatives who tended to keep a tight hold on corporations by spelling out rules each business must follow, holding business owners liable for harms or injuries, and revoking charters when there was noncompliance with their stated terms and conditions.

Throughout the 1800s, under pressure from industrialists and bankers, the judiciary branch gave corporations greater leeway and more rights than the founding fathers had originally anticipated. Perhaps the most significant ruling came in 1886 when the US Supreme Court ruled in Santa Clara county v. Southern Pacific Railroad (118 U.S. 394 (1886)) that a private corporation was a "natural person" under the US Constitution, sheltered by the 14th Amendment, which requires due process in the criminal prosecution of "persons." According to the record Supreme Court Justice Morrison R. Waite made the following business-changing decision:

> "The court does not wish to hear argument on the question whether the provision in the Fourteenth Amendment to the Constitution, which forbids a State to deny to any person within its jurisdiction the equal protection of the laws, applies to these corporations. We are all of opinion that it does." He also stated: "The defendant Corporations are persons within the intent of the clause in section 1 of the Fourteenth Amendment to the Constitution of the United States, which forbids a State to deny to any person within its jurisdiction equal protection of the laws."

Once corporations were legally defined as "natural persons", they automatically were endowed with the same "Bill of Rights" as human beings, and thus came to possess and exercise the same rights of those granted to individuals by the constitution.

Prior to this point in time (the mid-1800s) corporations had limited duration (10 to 30 years) and were restricted in terms of their business purpose, amount of land that could be owned and their level of capitalization. In these corporations the sharing of power was in favor of the shareholders where unanimous consent could be required for some of the largest shareholder decisions, such as a merger. In addition, there was no limitation to protect the liability of the corporation – managers, directors, and shareholders were all held personally liable for all debts of the corporation and in some states, doubly or triply liable for any damages caused by the corporation. Further, the states reserved the right of review and the ability to either amend or revoke the corporate charter – in some instances not even requiring a reason for this action.

Today's model for governing a corporation is very different: In a speech presented to the Stern Graduate School of Business of New York University on March 26, 2002, Alan Greenspan, Chairman of the Federal Reserve Bank, made the following observations about corporate governance:

> "Generally speaking, the resulting structure of business incentives, reporting, and accountability has served us well. We could not have achieved our current level of national productivity if corporate governance had been deeply flawed."
>
> "Thus, it has increasingly fallen to corporate officers, especially the chief executive officer, to guide the business, hopefully in what he or she perceives to be in the best interests of shareholders. Indeed, the boards of directors appointed by shareholders are in the overwhelming majority of cases chosen from the slate proposed by the CEO [Chief Executive Officer]. The CEO sets the organization's business strategy and strongly influences the choice of the accounting practices that measure the ongoing degree of success or failure of that strategy. Outside auditors are generally chosen by the CEO or by an audit committee of CEO-chosen directors. Shareholders usually perfunctorily affirm such choices."
>
> "To be sure, a CEO can maintain control over corporate governance only so long as companies are not demonstrably in difficulty. When companies do run into trouble, the *carte blanche* granted CEOs by shareholders is withdrawn. Existing shareholders, or successful hostile bidders for the corporation, usually then displace the board of directors and the CEO. Such changes in corporate leadership have been relatively rare but, more often than not, have contributed to a more-effective allocation of corporate capital."

Greenspan succinctly described the current management situation for corporations and has laid the foundation for a discussion of the role of quality management in governance through the effective and efficient management of a corporation by the CEO and his team of directors and managers to deliver value on behalf of its owners to the shareholders, not the state legislatures, as the new dominant external force in corporate governance.

What is corporate governance?

Corporate governance is a structural system of institutional policies, implementing rules and business controls that establish a framework under which corporations are managed and operate. This framework governs all actions of corporations from initial founding, through their period of entrepreneurship and growth, through their development into a mature structure for their administration and governance, and to the point of their exit of the market as an independent identity (by merger, dissolution or insolvency).

This definition raises the question: who governs (participates in making decisions and with what degree of authority) and to what extent is their power exercised in management of the capital that the corporation that has been invested by the financial market?

Governance is a form of managerial oversight – and the reform movement has been pushing toward implementing more democratic forms of governance – but what does that really mean? Is governance more than just 'boardroom performance' by the directors of a corporation? The reform movement is asking for a higher degree of participatory governance with democratic control exercised by all stakeholders – especially the shareholder and the community. Many of the reform movement consider a movement to greater stakeholder participation as a return to the initial principles laid down by the Founding Fathers for 'corporate governance' – a way to correct changes that they perceive as an imbalance of power from the individual's rights to place a more dominant degree of power into corporate hands – in particular the hands of the CEO.

What is the current state of governance that Greenspan referenced? The current practices focus the decision authority on the CEO – the board of directors provides oversight while management provides advice and executes the final decisions (using authority that is delegated by the CEO). When all power is focused into one position, the question that is always raised is the degree of checks and balances to assure ethical conduct – do actions taken benefit all of the stakeholders and not just one dimension. This is a core problem as perceived by the reformers – they want to have a broader distribution of decision-making authority than the centralized focus in a CEO.

However, a board of directors fills a crucial role in the accountability chain representing interests of the owner-investors – both legal and moral owners (society when the corporation consumes public resources may be considered to have a moral ownership right to the corporation) – and operators who work in the business processes of the firm to meet its operational mission. The board does not exist to support staff – it serves to represent ownership provide a controlling voice. The owner-representative authority of a board of directors is executed as a single unit, prescribing organizational direction – providing limitations on the staff means to achieve an end without directing the specific means that the staff takes to achieve the desired results.

The governance process sets policy for corporate decisions using the principles of policy management [also known as *hoshin kanri* and policy deployment] – an approach that enables extensive empowerment to staff while preserving business controls necessary for accountability for shareholder-owners. The system of policy management includes both strategic direction setting as well as the deployment of the policy to the organization. It provides a moral and ethical foundation of values, a framework for exercising all of the management disciplines, an approach for precision in delegation of authority, as well as a long-term focus on the organization's purpose rather than on its operational actions. In this context, how is quality governance achieved?

While board members are usually intelligent and experienced persons as individuals. Yet boards, as groups, are mediocre. Indeed, boards have been the subjects of much derision:

- "Effective governance by a board of trustees is a relatively rare and unnatural act ... trustees are often little more than high-powered, well-intentioned people engaged in low-level activities."

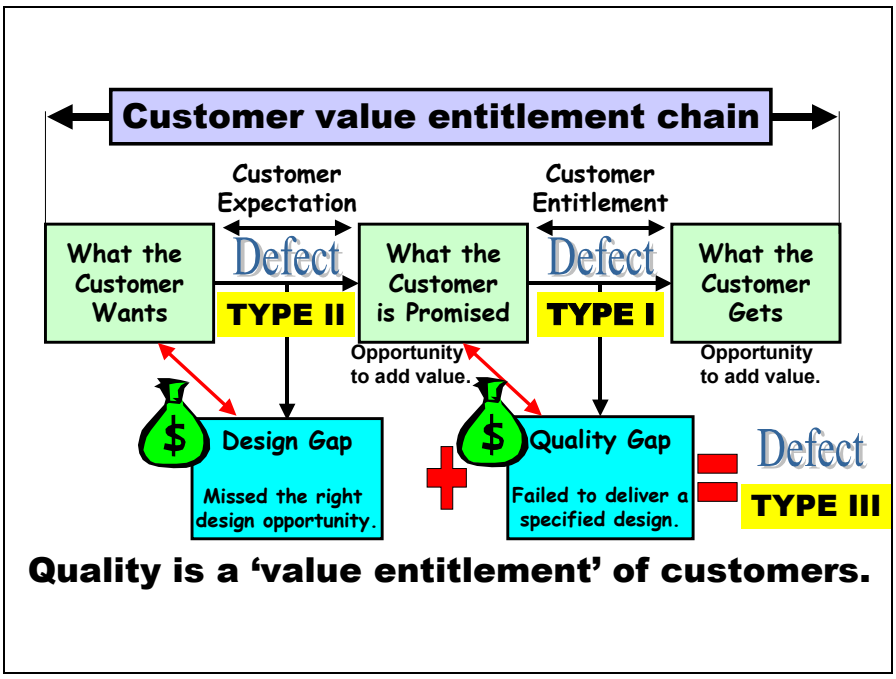
- "There is one thing all boards have in common ... they do not function."
- "Ninety-five percent [of all boards] are not fully doing what they are legally, morally, and ethically supposed to do."
- "Boards have been largely irrelevant throughout most of the 20th century."

In the wake of the Enron debacle, there has been an intense call for more independence of boards, separation of CEO and chair roles, rigorous audit committees, as well as much more responsible accounting. Interestingly, almost all recommendations put forward involve enhancing the current features of boards. These recommendations offer a series of improvements that are defined by a set of 'best practices' that do not establish a system for governance. When a set of disjoint best practices are integrated into a management system, this can create managerial confusion because they do not fit into a higher-level governance process. When a systems approach is not used for setting a management framework, board members and senior managers suffer confusion between their roles creating a conflict between strong board and management components of the business model that may, in turn, lead to either a situation where the management pre-empts the authority of the board or the board micromanages management. Neither alternative is a healthy situation.

What is a better way for boards to work? Boards must serve as "devil's advocate" and "sounding board" for management. Board members should refuse to engage in rubber-stamping executive initiatives or the micromanaging the activities of the business leaders. In general, boards must become far more enlightened and more competent as groups than they have been.

In the previously referenced speech, Fed Chairman Alan Greenspan observed: "In a further endeavor to align boards of directors with shareholders, rather than management, considerable attention has been placed on filling board seats with so-called independent directors. However, in my experience, few directors in modern times have seen their interests as separate from those of the CEO, who effectively appointed them and, presumably, could remove them from future slates of directors submitted to shareholders. I do not deny that laws could be passed to force selection of slates of directors who are patently independent of CEO influence and thereby significantly diminish the role of the CEO. I suspect, however, that such an initiative, while ensuring independent directors, would create competing power centers within a corporation, and thus dilute coherent control and impair effective governance."

What is an objective way to consider how to appropriately govern a corporation? One way to understand what reforms are needed to correct symptoms of poor performance observed in many boards is to take a process perspective and more fully define what is 'quality' governance and then develop an operational definition for 'good governance' based on the actions that must be taken to assure effective, efficient, economical and representative governance. Let's consider an approach for applying policy management (also called by its Japanese name *hoshin kanri*) quality approach to corporate governance by first defining what is meant by quality in this context.



What is quality?

Quality is one way to describe the "goodness of the results" or outcomes accomplished by a corporation. With such a results focus, quality becomes a value proposition. How this value is developed, managed and captured is the work of the corporation's leaders and managers. In a simple model of business activity, quality is assured through the effective design of innovative goods and services for real needs in competitive markets and through the consistent production and delivery of these goods and services to their final consumer. A competitive product design is based on understanding expectations of customers and serves as the basis for the market promise from the corporation. Once a promise has been made the act of consistent promise keeping represents the second dimension of quality – reliable performance against its promises made. In considering where this performance can go wrong there are three types of defects observable:

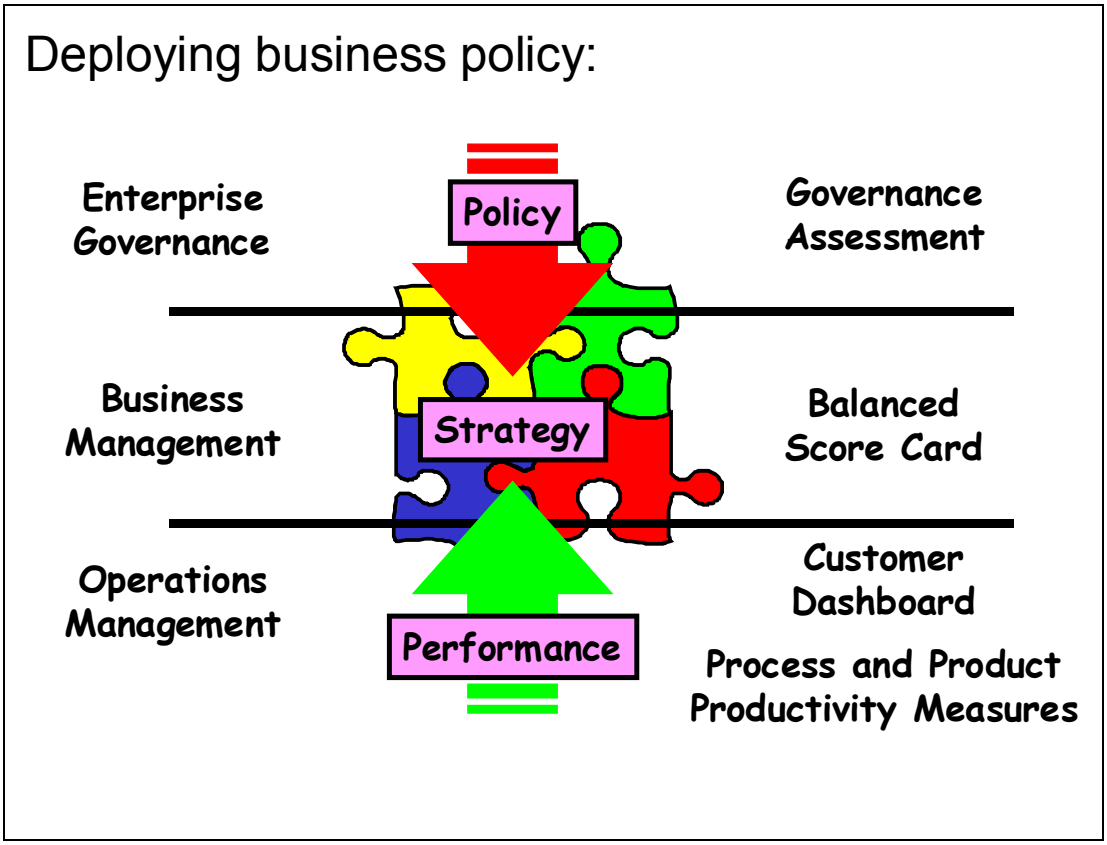
- A Type I Defect occurs when organization do not keep its promises to the market.
- A Type II Defect occurs when organizations do not design product to meet the expectations of its market or targeted customers.
- A Type III Defect happens when Type I and Type II defects occur simultaneously.

In this model, the operational performance of the organization is focused on one of the key

stakeholders – the customers and markets. However when a Type III defect occurs, then the consequences are born by the shareholders. Good corporate governance should protect the shareholders from such failures of the management system and also assure that the work of the corporation is done in an ethical, moral and legal manner. How is this achieved in the context of the management system's structure?

What is 'good' corporate governance?

A systems approach to management of a corporate entity can proscribe three levels of abstraction in defining ***WHAT*** organizations do and ***HOW*** they operate. This three-level model describes how the governance function, business process management function and operational management function collaborate to produce the desired business results. Rather than describe the model in detail (another paper for another time) the activities of the three levels may be summarized in the following graphic and its related commentary:



Governance establishes the policy framework within which business leaders will make strategic decisions to fulfill the organizational purpose as well as the tactical actions that they take at the level of operational management to deploy and execute the organization's guiding policy and strategic direction. The guiding policy is the output of the board of directors from the enterprise governance level to the management team through the CEO. The business management team sets the strategic direction and progress toward their specified direction is reported in the form of a 'balanced scorecard' that describes the organizational performance from the perspective of each of its unique stakeholders. The strategic direction is deployed to operational management through a cascade of objectives and performance indicators in a customer dashboard – an action-oriented measurement system defining linkages between internal performance measures and external measures of performance that deliver value to customers. Operational results are then reported back to the business managers to indicate performance against their objectives. The role of business leaders and board members in this management system is to set the guiding policy and strategic direction that the organization will execute in the future, while the role of business leaders and their team of operational management is to execute the firm's strategic direction within the context of the board's delegated authority.

Based on this model of a business system 'good governance' is quality in terms of the response of the organization to the guiding principles and strategic direction: does it do what is right, reliable and responsible to assure the desired performance within a context of holistic oversight that is provided through the system of business controls?
Good corporate governance must focus on ensuring that corporations take into account the interests of a wide rage of constituencies (stakeholders such as customer-consumers, investor-owner-shareholders, employee-associates, legal-regulatory, and the communities in which the corporation operates) and that the board of directors is accountable to both the company and its shareholders.

What conditions must be satisfied in order to hold boards and managers accountable?

What does it take to hold someone accountable for the quality of his or her work? There are three necessary and sufficient conditions that must be met for management to be able to properly hold individuals as accountable for the quality of their work. All of these three conditions must also be met in the following sequence in order for them to operate:

- ***Defined expectations*** – Employees must have clear knowledge about the expectations of management – people must have good knowledge of the work they should accomplish and proper preparation in right way to perform work procedures (effective training) as well as the resources needed to get the job done (resources refers to material, equipment, information and time).

- ***Capability to perform*** – People must have knowledge of the standard of performance that they are being asked to attain and an objective measurement system must be in place to assure that the data is being collected objectively to evaluate this performance and provide the necessary knowledge required to operate the work process so people can effectively and efficiently address the set of expectations (and thereby assume the delegated responsibility).
- ***Ability to self-regulate their own work*** – People must have the ability to observe the work process measures and to make decisions about corrective action in order to keep their process operating according to the standard when they are not going to meet the original expectations for desired performance targets (and thereby exercise their delegated authority to manage within the limitations of control that has been granted to them).

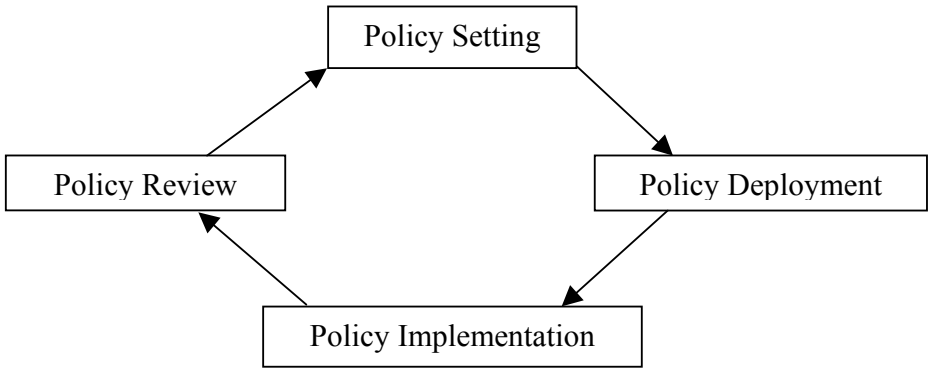
When these conditions are met, then an individual may be appropriately held accountable for the quality of their work – this includes the board's initial delegation of authority to a CEO as well as the CEO's delegation of authority to the organizational management (this authority delegation is cascaded, with prescribed limitations, like the tree diagram that is the structure of the organization chart. A delegation diagram that is constructed using a decision tree format is one way to assure clarity in expectations for the limitations of the decision and fiduciary authority that has been entrusted to different levels of the firm. The effective delegation of authority and appropriate accountability for work are key elements of good governance.

The Policy Management Approach to Corporate Governance

Policy management delivers strategic direction through breakthrough projects that deliver the long-term performance goals for achieving sustainable business strength while, at the same time, delivering an operating plan for achieving short-term performance through the daily management system of the organization. Policy management methods anticipate long-term requirements by focusing on annual plans and actions that must be met in each year to accumulate into long-term strength. Policy management processes begin when senior management identifies the key issues or statements of vulnerability, based on the guiding policy of the board, where improvement will have its greatest impact on business performance. This perspective is an essential starting point for policy management. As Dr. Noriaki Kano of the Tokyo Science University points out, without such direction "the ship would be rudder-less." Communication of focus areas or themes for improvement provides a cohesive direction to assure alignment of the entire organization and to build consensus among the management team on business priorities. This focusing of policy is a critical contribution of the board in alignment with the executive team.

Policy management is able to create the type of organization that William McKnight, former CEO of 3M, expressed as his desire: "an *organization* that would continually self-mutate from within, impelled forward by employees exercising individual initiative."

In short, an organization where creativity is managed through a combination of self-initiated continuous improvement projects with engaged teams focusing on the things that they know best, combined with focused strategic projects that use organization-wide resources to make a difference on the larger organizational scale. Policy management encourages both types of improvement with the strategic projects directly tied to a top-down view of what needs to be improved.



The policy management system consists of 'kanri' or control mechanisms that deploy business policy through four steps in order to execute management's program to improve business direction using a systematic sequence of steps that achieve strategic project objectives within the constraints of assigned resources and policy constraints. These four steps define policy setting (or establishment of the subjects for these strategic projects), deployment (or propagation of these projects throughout the organization to engage the resources of the operational layers of management), implementation (or integration of the results of change into the daily management system), and review (the monitoring and assessment of the results achieved from this process). These four steps define a business improvement cycle.

Strategic direction must be determined by discovering the alternatives for achieving the organization's vision and choosing the direction that will accomplish it. This direction is modified through the power of the incremental change to act as the 'rudder' that steers the ship by making 'finely tuned' changes to the general direction of the strategy.

What are the essential ingredients in choosing strategic direction? This process of policy management engages senior management with the board to focus on a policy regarding the future and then it integrates strategic planning, change management, and project management with the performance management methods that focus on delivering results.

This is the policy setting process. Once a policy has been set, the next challenge is to align the strategic direction with the work that must be performed to change the daily management system. This is the deployment of policy where change projects are defined and implemented.

Throughout this process the actions of the board are focused on defining the policy while the management's actions are focused on translating the board's improvement policy into improvement projects and then deploying the improvements generated by these projects into full-scale implementation in the daily management process. Finally the executive and board conduct regular reviews of the policy to assure implementation reflects intent of the policy. Some specific actions across these four steps include:

- Identifying critical business assumptions and areas of vulnerability (board)
- Identifying specific opportunities for long-term improvement (board)
- Establishing business objectives to address the most imperative policies (board)
- Setting performance improvement goals for the organization (board/management)
- Developing change strategies to address business objectives (management)
- Preparing an annual policy implementation plan for the organization (management)
- Defining project charters for implementing each change strategy (management)
- Implementing the change projects (organization)

As the senior management creates its annual policy implementation plan to reflect the high-priority areas for investigation, they address five elements to establish the plan for conducting the individual improvement projects:

1. Statement of desired end: statement of an improvement policy to be accomplished
2. Metrics to measure progress: The measurement that describes progress toward a desired result (expressed as a target value).
3. Target value: The value or level of the metric that you want to attain.
4. Deadline date: a date by which the target value must be achieved.
5. Means: a strategy (approach) to accomplish the target – what must be done to achieve a desired result or outcome (the target value).

As Dr. Peter F. Drucker once commented: "for full effectiveness all the work needs to be integrated into a unified ***program for performance***." The policy management program for performance improvement is designed by the top management team to provide a very specific, effective course of action to achieve its desired results. In order to achieve these results, then all the dimensions of the business must be consistent with each other as work together as an engineered system. This is exactly what a board intends to happen when it establishes the policy and delegates implementation to management.

What is the role of the Board in assuring 'good' corporate governance?

As the representative of the owners inside the corporation, a board serves a unique role in the corporate governance system. One way to evaluate roles that are played in making decisions about business is the so-called RASCI model. In this model (see the following graphic) the participants in decisions are identified, along with the role that they take in making a decision and the measurements that they use to evaluate as decision criteria for the business situation. Using this methodology, decision accountability may be tracked to individuals who may then be held accountable for specific actions.

Process accountability analysis – RASCI:

ID#	Process Name	Key Decision Point	Decision Participants	Role (RASCI)	Measure
			Name and Title		

For each key decision in the process map (deployment diagram), identify and specify the decision process that is used to make the decision – including the measures used for decision criteria and the roles of the individuals involved in the decision – what are the decision rights of each person?

Responsible for change:
(only one "R" per decision point)

Role Codes:

Responsible – Conducting the work
Expectation – " Completed staff work"
performance to schedule and quality

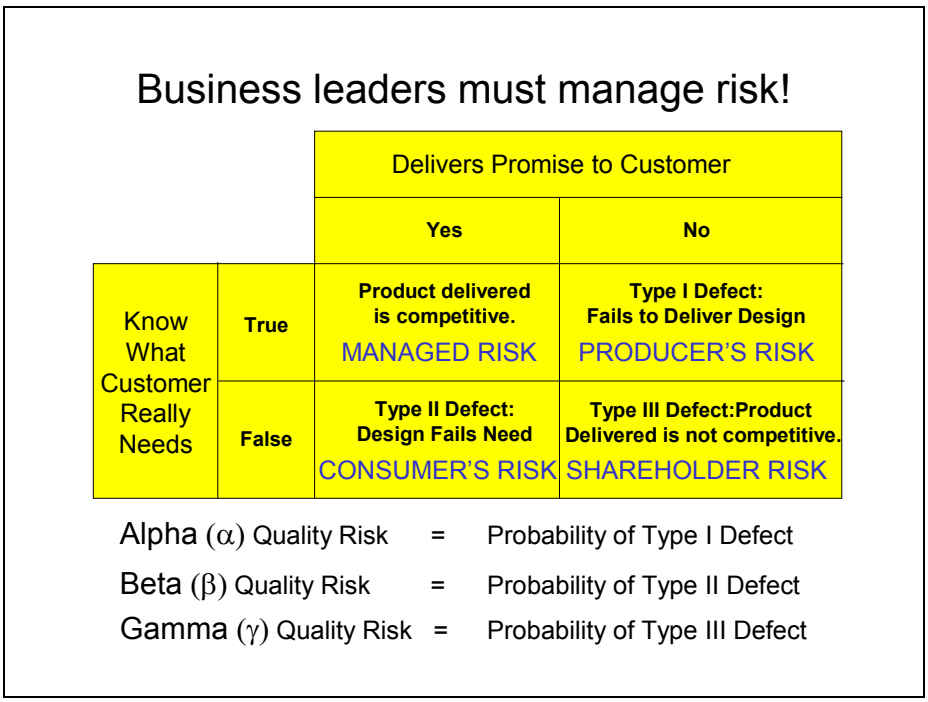
Accountable – Oversight and coordination to completion
Expectation - Deliver project results

Supports – Involved in action during and after the fact
Expectation – Dedicated teamwork

Communication – In process communication
Expectation – Consensus, review, feedback and dialog

Informed – After the fact
Expectation -Compliance

What happens when a bad decision is made? The risk of bad corporate decisions as they affect the delivery of quality to customers can be seen in the following truth table where the impact of the quality defects from bad decisions are clearly seen in terms of the individuals who bear the brunt of the risk. Only when the organization does the right thing at the right time – knowing and delivering on customer needs – does it manage risks in an appropriate way for all stakeholders. The role of corporate governance is to assure that this option is the normal way of doing business for the organization. In this way business leaders can assure the quality of their management efforts.



Business leaders must manage risk!

		Delivers Promise to Customer	
		Yes	No
Know What Customer Really Needs	True	Product delivered is competitive. MANAGED RISK	Type I Defect: Fails to Deliver Design PRODUCER'S RISK
	False	Type II Defect: Design Fails Need CONSUMER'S RISK	Type III Defect:Product Delivered is not competitive. SHAREHOLDER RISK

Alpha (α) Quality Risk = Probability of Type I Defect

Beta (β) Quality Risk = Probability of Type II Defect

Gamma (γ) Quality Risk = Probability of Type III Defect

How is corporate quality assured through good governance?

Governance is based on three cornerstone principles: ownership, stewardship and accountability:

- ***Principle of Ownership*** – Ownership is a principle that describes the way an individual cares for a resource. Owners will establish a system of business control for preservation of capital and risk management methodologies for defining and operating with their personal comfort zone for potential loss of capital (or any owned asset) in order to achieve their desired level of return.

- ***Principle of Stewardship*** – Stewardship is a principle that directs a person to take responsibility for the management of resources that have been entrusted into their care by an owner. Corporate stewardship implies that the value of capital investments is preserved and enhanced by the actions of management. Stewardship impacts all business issues (e.g., social, health and environmental ramifications of the production methodologies as well as the use and eventual disposal of products). The primary roles in assuring stewardship in the life cycle of a product typically involve manufacturers, retailers, service providers, consumers and government. Stewardship acts on behalf of these participating

communities to preserve value and exercise due diligence in the management of the organization's resources to achieve is purposeful ends.

- ***Principle of Accountability*** – Delegation of authority and resources from an owner to a designated steward brings accountability for how the authority is used and how the resources are deployed or consumed.

In a corporate governance structure, owners are the shareholders while the CEO is the steward. The board of directors provides the mechanism by which owners delegate authority to the steward. How are these three principles integrated into a draft definition of 'good governance' that can be used in a corporate context for quality management?

Given these perspectives, how should 'good governance' be operationally defined?

The following modest proposal is made to operationally define 'good governance' in the context of corporate management. 'Good governance' occurs when all of the following conditions are met:

- The board sets policy that defines the purpose and long-range vision of the total corporation and places limitations on the methods and style that management may use to achieve its purpose [under conditions where shareholder requirements are known and defined as objectively measurable and auditable business objectives].
- The board establishes framework for execution of the way that the organization may elect to meet these business objectives (moral, ethical and legal boundary conditions that limit the actions of management) and describes this framework in terms of guiding principles or policies that the organization is obligated to apply.
- The board deploys this policy to the CEO for further delegation to the operational managers through the business management organizational structure.
- The board reviews performance against the objectives using an objective system of measurements that reflect the concerns of all major corporate constituencies.
- The board encourages the CEO to self-regulate the action of the organization in order to achieve the desired results.
- When the organization is found to be operating outside its business control system that was been established by the board, then boards must take corrective action to bring realign the organization [if they do not do so, then inaction will undermine the authority of the board that has been granted by the corporate stakeholders].

How does this operational definition compare with commonly promulgated definitions of good governance?' This follow-up question and also further refinement of the proposed operational definition are both areas that require greater work; however, there is a basis for making a comparison between the operational definition and principles of corporate governance.

Proposed International Principles for Corporate Governance

In May 1999 ministers representing the 29 governments participating in the Organization for Economic Co-operation and Development (OECD) voted unanimously to endorse the ***OECD Principles of Corporate Governance***. These principles are the principal response by governments to the G-7 Summit Leaders' recognition of corporate governance as an important pillar in the architecture of the 21st century global economy. The Principles were welcomed by the G7 leaders at the Cologne summit in June 1999 and are being considered as a governance model by the International Monetary Fund, the World Bank, the United Nations Development Program, and other international organizations.

The OECD principles define a broad outline of criteria for excellence in governance that collectively represent a set of good practices. However, these principles fail in the sense that they do not provide an operational definition of the ***system of management*** that is necessary to achieve good governance, including the related measurements that can be used to implement a governance-monitoring scheme. Integrating the good practices within the context of the policy management approach to consensus development and delegation of authority has promise as the basis of an excellent approach for corporate governance that supports its system of management.

How does this proposed structure of principles related to corporate governance relate to the operational definition? This is a question currently being pursued by a study team of members of the International Academy for Quality (IAQ).

What should be the next steps?

For years quality professionals have worked to build more reliable organizations that do the right work effectively, efficiently and economically – this is, organizations that are promise keepers for their customers, shareholders, employees as well as the public at large. Today, the quality challenge is to build organizations that are right **AND** reliable **AND** responsible – not just accomplishing results, but doing so in a way that respects the rights of all constituencies and responsibility to society for the public trust that has been endowed to the corporation. In order to accomplish this challenge, it will be essential to develop a consensus on the meanings of both 'good governance' as well as 'responsible organization' [preferably as an operational definition]. The governance improvement project of the IAQ should provide leadership to establish a starting point for consensus on this issue and to formulate a body of knowledge regarding quality and governance.

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An approach to the evaluation of a Board of Directors

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Corporate Governance is presently being recognized as a key factor at the level of long-term success of Companies around the world, operating within an accepted framework of values.

In this regard, Corporate Governance best practices have been established in different International collaborative projects.

We have developed a system through which a Board of Directors can be measured against those best practices using a matrix where key attributes are evaluated and the results are expressed in a simple, numerical way. The evaluation process not only provides the status of Governance at a certain moment, but also serves as the basis of information for the needed improvement plans.

As they are implemented, the procedure constitutes an excellent feedback mechanism. The matrix allows showing graphically and clearly the situation of the board at a given time, thus being an excellent management communication tool.

What follows is a description of the key elements used in the construction of the matrix, as well as of its numerical evaluation process.

Criteria for Board Evaluation

The Criteria are the basis for Board evaluation and self-assessment to help improve performance practices, capabilities and results.

Core values and Concepts
The Criteria are built upon the following set of interrelated Core values and Concepts:

Leadership
The Board should set directions with high expectations and clear and visible values, aligning the interests of all stakeholders to support and guide the decision making of all members of the organization.

Independence
Board independence from management is crucial to ensure that the Board effectively carries out its mission and responsibilities and holds management accountable to shareholders fairly.

Ethics & Transparency

The Board should ensure ethical behavior and compliance with laws and regulations, auditing, and accounting principles.

Difference between Governance and Management

Board effectiveness is reduced by the failure of board members to think through and understand the distinction between governance and management. The main functions of the Board are to effectively:

- Ensure the strategic guidance of the company, and
- Monitor management.

The roles of Directors and Managers must be defined assuring that implementation is clearly a Management responsibility.

Focus on well documented processes that add value

Corporate Governance must be good for the company business by creating value for all stakeholders. This should be the guidance for the selection of Board Best Practices. All items in this Board Evaluation Approach require formal, transparent, and well-documented written processes.

Focus on results

Although all the above items are necessary, they must focus on results and not on procedures, tools or organizational structure.

Criteria Categories for Board Assessment

Seven Criteria Categories were established and subdivided into items as follows:

1- Mission and Principles
2- Board structure
3- Board operating procedures
4- Board & Management
5- Board & Shareholders
6- Board & Community
7. Board contributions

1. Mission and Principles

1.1. The Mission of the Board

The Mission of the Board must be in line with the Mission of the Company, and both must answer the question "What are we attempting to accomplish?"

The basic mission of the Board should be to ensure the strategic guidance of the company and the effective monitoring of management.

1.2. Legal framework – Liabilities

The legal framework is defined by the company statutes, law doctrines and organizational documents that define duties and liabilities in the jurisdiction where the company is organized, and must comply with the letter and spirit of the law.

1.3. Code of Corporate Governance Best Practices

This document should include rules and procedures for Board and Company operations that assure compliance with laws, regulations and OECD Principles for

Corporate Governance. Key success factors are: transparency, accountability, integrity, communication, fairness, independence, credibility, honesty, and mutual respect.
The Code should include only what is needed by the company to accomplish its business objectives.

2. Board Structure

The composition of the Board varies depending on the needs of the Company. It is not possible to formulate or design a model Board that would represent the best solution for even a small proportion of companies.

2.1. Board size

Boards should be small rather than large, but should include diversity of backgrounds in order to ensure at least two different ways of tackling problems. In other words, understanding something from at least two angles, since seeing a problem from just one viewpoint is a rather fragile kind of understanding.
A Board should have a majority of independent directors with a wide range of talents, expertise, and occupational and personal backgrounds.
Avoiding too big Boards that usually become two speed Boards where it is difficult for each member to make effective contributions, and even more difficult to make decisions, is recommended.

2.2. Chairman - Lead Director

The Chairman controls the environment within which governance takes place, ensuring effective meetings with free and focused discussions.
It is the Chairman's task to turn a group of capable individuals into an effective Board team.
In order to ensure effective company leadership directed by an effective and accountable Board, it is advisable that the Chairman and CEO are not the same person. When this is the case, the Board should designate a lead director to Chair independent directors' meetings to discuss items such as compensation, auditing and governance.

2.3. Mix of inside and external independent Directors

The number of independent directors should assure strong independent opinions in Board meetings.

2.4. Board committees

The functions performed by Board committees are key to effective governance.
Boards that are too small to have committees must perform committee functions.
The most common Board Committees are Auditing, Compensations and Governance. They should consist of a majority of independent directors in order to assure strong, independent, and transparent opinions in critical business areas.
Committee functions and processes should be clearly established and communicated to all those involved.

3. Board Operating Procedures

3.1. How to select new members

Boards should seek candidates with the skills and capacities that meet the needs of the business.

They must be defined taking into consideration, age, personality, education, candor, experience, languages, commitment, availability, and the ability to challenge without confrontation.

The core competencies of the Board are:

Accounting and Finance
Business judgment
Crisis response
Industry knowledge
International markets
Leadership
Strategy/Vision

Directors should have a basic knowledge of the statutes, law doctrines and organizational documents that define their duties and liabilities as directors in the jurisdiction where the company is organized. They must not only know the letter but also the spirit of the law.

3.2. Definition of independence

Outside directors are independent when they:

- have never been employed by the company
- are not related to any company employee
- are not employed by any firm that provides major services to the company, and
- receive no compensation from the company other than director fees.

Outside directors need to be more than independent; they must be independent-minded as well

3.3. Directors Function Description

All members of the Board and the Chairman should have an updated function description.

3.4. Training and orienting directors

The Board should have an adequate process for orienting and educating new directors, as well as training all the members of the Board.

3.5. Meetings, agenda, minutes and follow up

The Board should have an established schedule of meetings. Business needs might require the Chairman to call for special meetings. The agenda and all relevant information should be provided well enough in advance of meetings, to be reviewed carefully beforehand. Minutes should be precise and should focus on actions and decisions.

3.6. Election term/ Term limits/ Mandatory retirement

All three issues should be clearly established and respected.
Exceptions require approval.

3.7. Board compensation review

Compensation for directors and the process to review directors' compensation should be appropriate.

3.8. Participation of Senior Managers and other non-directors in meetings

The Board should provide appropriate advice and counsel to senior management. Senior management should be invited to participate in Board meetings when necessary. The CEO should participate in all Board meetings.

3.9. Board and Director assessment - Self-assessment

The Board should have an effective process to assess its own performance.

4. Board and Management

4.1. Formal evaluation of the CEO

The Board should have a formal process to evaluate the CEO.

4.2. Senior management compensation

The Board establishes senior management compensation and relates it to their performance.

4.3. Board access to senior management

Individual discussions between the CEO and the directors should be frequent and there should also be periodical meetings with other senior managers such as the CFO and COO.

4.4. CEO succession planning

The Board adopts and maintains a senior management succession planning process to its satisfaction.

4.5. Company information

The Board should receive reliable, accurate and timely information about company operations. It should be brief and clear enough to be assimilated and understood without undue difficulty, and above all, it must be relevant to the strategic issues the company faces.

4.6. Risk assessment and risk management

The Board should review and discuss periodically company policies and compliance systems including security, IT related, safety, auditing and others, depending on the kind of business.

4.7. Clear definition of Board and top management roles

The roles of Directors and Managers must be defined assuring that implementation is clearly a Management responsibility.

Management recommends and implements. The Board approves vision, mission, strategies, major projects and budget, and conducts frequent, consistent and disciplined follow-up to ensure actions are being taken and improvements are being made.

5. Board and Shareholders

5.1 Content and character of disclosure

The company governing documents should include disclosure to shareholders of information on ownership structure, compensation to CEO and Board members, accounting practices and any other company information needed to guarantee transparency and assure compliance with regulations and protection of basic shareholder rights.

5.2 Compliance with basic shareholder rights

All shareholders should be treated equally. They must:

- Obtain relevant and sufficient information on the company on a timely and regular basis
- Participate and vote in general shareholder meetings
- Elect and remove members of the board
- Share in the profits of the company
- Participate in extraordinary transactions such as the sale of a business, etc.

6. Board and Community

Disclosure to the government and community should comply with the law and regulations.

The press, customers, and institutional investors should be kept informed major issues regarding the Company, the top management, and the Board.

7. Board Contributions

7.1 On company results

Successful critical strategies generated and controlled by the board should be evaluated as well as key performance indicators, including intangibles.

7.2 Stakeholders evaluation of the Board

Stakeholders include management, personnel, major suppliers, customers, government, society, and controlling and minority shareholders.

The board should define how the stakeholders' opinions are determined and evaluated.

General guidelines to assign scores

We recommend following the methodology indicated in the Criteria for Performance Excellence published by the Baldridge National Quality Program. Many countries in the world have National Quality Awards that share the criteria established by the Baldridge

Award in the U.S.A. and are written in the local language. It is also highly recommended for Directors to be literate on how companies are evaluated for Quality Awards.
A procedure to evaluate the performance of a Board of Directors should be based on a comparison against a target model that represents the State of the Art, as is usually done in quality award programs. In this work we use the OECD Principles for Corporate Governance as the target model. Thus, a matrix can be constructed to consist of seven columns with the criteria described above, and four rows with the following levels:

- ***Level 1***: Understanding the need to improve Corporate Governance
- ***Level 2***: First concrete steps toward establishing best practices
- ***Level 3***: Implementation of best practices
- ***Level 4***: Leadership

Using our procedure is straightforward: for each of the seven columns, the cell that best represents the current situation of the Company is selected. The resulting matrix represents the performance of the Board of Directors and can help companies to perform their Board evaluation.

The Matrix

The evaluation matrix is composed of seven columns, the criteria categories, and four levels as described above. The levels considered in each category can be used as a way to build a continuum which helps the company progress toward Excellence in the Board of Directors. In order to work with actionable results, a certain score must be assigned to each level and a Factor to each category, for a total maximum score of, say, 1000.
Since the evaluation can be performed in quite a wide variety of business environments, we recommend developing a score system at the Company, Country or Region level. This is an important task that in every case should be carried out by a professional committee. If the Company, Country, or Region is progressing in its goals to improve Corporate Governance, the matrix score system must follow that status change, evolving over time so as to show the new minimum thresholds established in each particular area.

Values within a level
Once a certain score is developed for a Company, Country or Region, a matrix containing a certain range of values for each level and a factor for each category is obtained. Figure 1 illustrates the Board Evaluation Matrix, using a selection of scores and factors as an example.
For levels 1 and 2: If the situation of the company exactly matches the respective level description, the score should be the minimum for that level. It may rise to its maximum, according to the awareness and the level of implementation of the improvement plans that the Company can exhibit.
For levels 3 and 4: The company belongs to the highest level when each and every item is at least matched.

Factors within the seven Criteria

The system should be dynamic, dependent on time and geography. As previously commented, the scores and factors in the system must be updated on a timely basis according to the progress of the Company, Country or Region.

As regards the "factors", special consideration and importance should be given to the "BOARD CONTRIBUTION" criterion. It is the same concept as "RESULTS" in the Countries National Quality Awards; thus, similarly and for the same reasons, it should be given a significant score. The different actions of the board should ultimately be directed toward improving its Contribution to Company Results, and this contribution is shown here.

Figure 1: BOARD EVALUATION MATRIX

LEVEL	SCORE	Mission & Principles	Structure	Board Oper. Procedures	Board & MGMT	Board & Shareholders	Board & Community	Board Contribution	Total Evaluation
1	0-1								
2	>1 to 3								
3	>3 to 7								
4	>7 to 10								
Score		0	0	0	0	0	0	0	
Factor		20	7	7	10	10	6	40	
Total		0	0	0	0	0	0	0	0

Contents of the Matrix Cells

Following is a description of each cell.

1. **Mission and Principle**

   ***Level 1*:**

   The board is not active in establishing the Values and Mission of the Company.
   The Values and Mission have not been established or are not in use.

There are no signs of the utilization of the Country laws, including the spirit of the law, as a complete operational framework for the Company.
The BOD/Mgmt/Company lack a comprehensive understanding/acceptance of possible liabilities.
Information about board activities and decisions are kept to some members of the board, and are not disclosed at all levels.
There are no policies regarding risks and crisis management.
The board has not adopted a Code of Best Practices, including subjects such as:
- Code of Ethics;
- Potential conflicts of interest among Shareholders, Board members and Management;
- Nomination and election process for Board members;
- Adoption and use of internationally accepted standards.

Level 2:
The Values and Mission of the Company have been established but with no formal participation of the Management team.
The Values and Mission have been communicated, but employees are not committed to them.
The Company intends to operate in compliance with the spirit of Country laws, but there is no process to ensure this.
The BOD is aware of its liabilities as well as of those of the Company. There is no process to mitigate risks.
There are policies related to risks and crisis management, but they are not properly communicated or enforced.
The board has adopted a Code of Best Practices, including subjects as:
- Code of Ethics
- Potential conflicts of interest among Shareholders, Board members and Management
- Nomination and election process for Board members
- Adoption and use of internationally accepted standards,

but its implementation has not been completed or enforced.

Level 3:
The Values and Mission of the Company have been established with Management participation.
The Values and Mission have been deployed within the Company, and are shared by employees.
The Company operates in full compliance with Country law and with the spirit of the law.
The BOD is aware of its liabilities as well as of those of the Company. There is a risk mitigation process.
There are policies regarding risks and crisis management, which are well communicated and enforced throughout the organization.
The board has adopted a Code of Best Practices, including subjects as:
- Code of Ethics
- Potential conflicts of interest among Shareholders, Board members and Management

- Board members' nomination and election process
- Adoption and use of internationally accepted standards

and it is fully operational.

Level 4:

The Values and Mission of the Company are proactively established by the board, with Management participation.

The Values and Mission are fully deployed within the Company. Employees are fully committed to both.

The Company operates in full compliance not only with Country laws but also, and more importantly, with the spirit of the law, and there is a process to ensure its sustainability.

The BOD is fully aware of its own liabilities as well as of those of the Company. A process is in place to anticipate and mitigate risks.

There are comprehensive, updated policies regarding risks and crisis management. Crisis management rehearsals are performed.

The board has implemented a Code of Best Practices, including subjects as:

- Code of Ethics
- Potential conflicts of interest among Shareholders, Board members and Management
- Board member nomination and election process
- Adoption and use of internationally accepted standards

It is fully operational and the Company is fully aware of new developments in such areas.

2. Board structure

Level 1:

Chairman/CEO functions:

- There is no separation between Chairman and CEO roles.
- There is no lead director

There are no external, independent Directors.

There are no Board Committees, nor is the board performing those functions.

Board members as a whole do not have the collective knowledge to make a significant contribution to the company.

Board size is not adequate for effective board performance.

Level 2:

Chairman/CEO functions:

- Chairman and CEO are two separate functions.

Or,

- There is no separation between Chairman/CEO roles, but the company is in the process of incorporating a lead director.

The need for external, independent Directors has been established. The process is in progress.

Board member selection on the basis of knowledge, experience, personality and expected-contribution has not yet reached full implementation.

Board size has been identified as an issue. A process to correct this situation is underway.
Board Committees:
- The need for Board Committees has been established, but is still in the implementation phase.

Or,
- The board is starting to assume basic Committee functions due to its small size.

Level 3:
Chairman/CEO functions:
- Chairman and CEO are two separate functions and the Chairman assures that proper Corporate Governance practices are in place.

Or,
- There is no separation between Chairman/CEO roles, but there is an independent, external lead director who clearly chairs the Independent Directors meetings (on subjects such as auditing, compensation/Governance issues/ and others requiring an independent view.)

External, independent Directors have been incorporated and are fully operational.
Board members are selected on the basis of knowledge, experience, personality and expected-contribution, and this helps the Company to achieve its very good performance.
Board size is adequate to ensure effective board performance.
Board Committees:
- All required Board Committees are fully integrated, following industry best practices as regards participants.

Or,
- The board is performing all the required Committee functions due to its small size.

Level 4:
Chairman/CEO functions:
- Chairman and CEO are two separate functions and the Chairman assures that outstanding Corporate Governance practices are in place.

Or,
- There is no separation between Chairman/CEO roles but there is an independent, external, strong lead director, ensuring an excellent level of diverse, constructive opinions at board meetings - a key factor in the level of excellence of Corporate Governance of the Company.

External-Independent Directors are a majority in the board, including the Chairman's function.
Board members are selected on the basis of knowledge, experience, personality and expected contribution. This is also a key factor as regards Company Performance.
Board size is adequate for excellent board performance. Diversity through external directors is a fact.

Board Committees:
- All required Board Committees are fully operational, within the highest levels of excellence in the Industry.

Or,
- The Board is performing these functions due to its small size.

3. Board Operating Procedures

Level 1:
There is no clear, accepted definition of Board Member Independence.
Election Terms/Term limits have not been clearly established.
Mandatory retirement has not been established as a norm, nor is it used as a de-facto standard.
There is no clear, accepted procedure as regards board compensation.
Senior Managers and non-Directors are never invited to participate in BOD meetings.
The Committees/Members/board Function Descriptions have not been established.
Not all board members can participate in the preparation of agenda items.
BOD meeting agendas or minutes are not regularly produced or are not available.
Information for BOD meetings is not produced and distributed to all members in advance to the meetings.
There is no process for selecting board members or the CEO.
Directors are not trained according to company needs. There is no introduction program for new Directors.
There is no evaluation process for the Board, board members, or Committees.

Level 2:
Even though Board Member Independence has been defined, there are no signs of its implementation.
Election Terms/Term limits have been established, but are not enforced.
Mandatory retirement has been established as a norm, but is not implemented consistently.
There is an accepted policy on board compensation, but it is neither fully utilized nor enforced.
The board has created the Committees/Members Function Descriptions, but they are not used consistently to assess performance.
Agendas and minutes are regularly produced for each board meeting. Not all BOD members can include items on the Agenda.
Information on BOD meetings is not always produced and distributed to all members in advance to the meeting.
There is a process to select board members and the CEO, as well as to manage their succession, but its utilization is neither consistent nor enforced.
Directors are not fully trained according to company needs.

Level 3:
The BOD has a number of Independent Directors, in compliance with its policy and in line with the best practices of the Industry.
Election Terms/Term limits have been clearly established and are normally enforced.
A mandatory retirement age has been established as a norm, and is in use.
There is a clear and accepted policy on board compensation, which is in use.
The Board/Committees/Members Function Descriptions have been created, and are regularly reviewed and used to assess their respective performance.
Professional management of BOD meetings is consistent. Agendas and minutes are regularly produced for each meeting.
Information for BOD meetings, containing all relevant information, is provided in advance to the meeting.
All board members can contribute to the agenda content.
Directors are trained according to company needs. The outcome is positive for the Company.

Level 4:
The BOD has a number of Independent Directors, in accordance with its policy. This number assures strong independent opinions.
Election Terms/Term limits have been clearly established and are mandatory.
A mandatory retirement age has been established as a norm and its application is enforced.
There is a clear, accepted and competitive policy on board compensation, which is in use and enforced.
The Board/Committees/Members Function Descriptions have been created, are regularly reviewed and used; this in turn, improves board performance.
Professional management of BOD meetings is consistent. Agendas and minutes are regularly produced for each meeting.
The quality of the Information provided for board meetings is excellent.
All board members normally contribute to agenda content.
Directors are fully trained according to company needs. The outcome is excellent for the Company.

4. Board and Management

Level 1:
There is no clear division between Board/MGMT responsibilities in areas such as:
- Budget
- Planning
- Strategy
- Risks
- Crisis Management

There is neither a policy nor a Compensation Committee to manage Senior Management Compensation.
Board members do not normally meet with Senior Management.

The CEO is not formally evaluated by the BOD on a regular basis.
CEO/Senior Management succession is not planned.
There are no training/development plans for MGMT.
Relevant information related to Company performance is either not complete or is not received by the board on a timely basis.

Level 2:
Board/MGMT responsibilities have been clearly defined but not fully implemented, in areas such as:
- Budget
- Planning
- Strategy
- Risks
- Crisis Management

There is a policy or a Compensation Committee to manage Senior Management Compensation, even though it is not fully enforced.
Non-board members occasionally attend board meetings.
There is a process through which the BOD evaluates the CEO, but it is not used on a regular basis. Quality of evaluation is poor.
CEO/Senior Management succession is planned, but not 100% enforced.
There are training/development plans for MGMT, but they are not fully implemented.
The Company has a Risk assessment (including security) as well as a Crisis Management program, which are not fully functional.
Relevant information to be used by Board and MGMT has been defined and agreed upon, but is not available on a regular basis.

Level 3:
Board/MGMT responsibilities have been clearly defined, and are fully operational, in areas such as:
- Budget
- Planning
- Strategy
- Risks
- Crisis Management

There is a fully enforced policy, or a Compensation Committee, to manage Senior Management Compensation.
Non-board members attend board meetings as needed.
There is a process to evaluate the CEO and it is used regularly. Quality of evaluation is very good.
CEO/Senior Management succession is planned and implemented.
There are well-implemented training/development plans for MGMT.
Relevant information to be used by Board and MGMT has been defined and agreed upon, and is available on a regular basis.
The Company has a complete risk assessment (including security) as well as a crisis management program.

Level 4:
Board/MGMT responsibilities have been clearly defined, fully implemented, and this is a key factor in the excellence of Company Management.
There is a fully enforced policy, or a Compensation Committee, to manage competitive Senior Management Compensation.
Non-board members are regularly invited to board meetings. This is a key factor related to the excellent checks and balance program implemented by the board.
There is a process to evaluate the CEO, and it is used regularly. The Board's knowledge in this regard enables excellent/precise evaluation.
CEO/Senior Management succession is planned, and 100% enforced.
There are complete, state of the art training/development programs for Managers.
Relevant information used by the Board and MGMT is instrumental to the Company's excellent performance in this regard.
Security issues are addressed by the Board and MGMT on a regular and complete basis, providing the Co with a safe environment.
The Company has a complete Risk assessment program, which is regularly updated according to new situations.
The Company has a crisis Management program, which is fully implemented and includes rehearsals on a regular basis.

5. Board and Shareholders

Level 1:
Company information is not disclosed to all shareholders.
Remuneration of CEO/BOD members is not disclosed.
Director, Committee, and BOD assessments are not disclosed at the shareholder level.
'One share one vote' is not enforced as a rule.
Ownership structure is not disclosed to shareholders.
Compliance with regulations and with the spirit of the law is not disclosed to all shareholders.
Not all shareholders can participate in the election or dismissal of board members.
A fair participation of Shareholders in Company profits is not assured, nor is the inherent information transparent.
Not all shareholders can participate in decisions regarding extraordinary transactions.

Level 2:
Company information is partially disclosed to all shareholders.
Remuneration of CEO/BOD members is not disclosed on a regular basis.
Director, Committee, and BOD assessments are disclosed at the shareholder level, but not on a regular basis.
'One share one vote' is the rule, but is not enforced.
Company information relevant to the Shareholders is produced, but is not available on a regular basis.
Ownership structure is available.

Compliance with regulations and with the spirit of the law is addressed at board meetings but not entirely disclosed to shareholders.
The process in place does not ensure the participation of all shareholders in the election or dismissal of board members.
Shareholders' share of Company profits is not consistently assured, nor is the related information fully transparent.
Not all shareholders participate regularly in extraordinary transaction decisions.

Level 3:
Company information is fully disclosed to all shareholders.
Remuneration of CEO/BOD members is fully disclosed.
Director, Committee, and BOD assessments are disclosed to all shareholders.
'One share one vote' is fully enforced as a rule.
Ownership structure is disclosed to all shareholders.
Compliance with regulations and the spirit of the law is addressed at board meetings and is fully disclosed to shareholders.
All shareholders can easily participate in the election and dismissal of members of the board.
Shareholders' fair share of Company profits is a fact. Related information is fully transparent.
All shareholders have the same opportunity to participate in extraordinary transaction decisions.

Level 4:
Company information is fully disclosed to all shareholders through an excellent/consistent process.
Remuneration of CEO/BOD members is fully disclosed.
Director, Committee, and BOD assessments are proactively disclosed to all shareholders.
'One share one vote' is fully enforced as a rule.
The Company proactively delivers needed/relevant information to all shareholders, on a timely basis.
Ownership structure is proactively disclosed to all shareholders.
Compliance with regulations and with the spirit of the law is regularly addressed at board meetings, and completely disclosed to shareholders.
All shareholders are invited to participate in the election and dismissal of members of the board.
The Shareholders' share of Company profits is assured by means of an excellent/transparent information system.
All shareholders are invited to participate in extraordinary transaction decisions.

6. Board and Community

Level 1:
Issues are not fully disclosed to the Government and Community, in compliance with the spirit of the law and regulations.

There is no professional Company communication process for Institutional Investors.
There is no professional Company communication process for Customers.
There is no professional Company communication process for the Press.
The board is not addressing Community issues.

Level 2:
There is a process to disclose issues to Government and Community, as demanded by the law, regulations and the spirit of the law, but the latter is not fully implemented.
There is a process for Company communication to Institutional Investors, but it is not fully implemented yet.
There is a process for Customer Communication, but it is not fully implemented yet.
There is a process for Communication to the Press about Company related issues, but it is not fully operational yet.
The board is addressing Community issues and is starting to produce some positive results in this regard.

Level 3:
There is a professionally created process to ensure that timely and accurate disclosure is made on all material matters regarding the Corporation, including the financial situation, performance, ownership and governance of the company.
The board is actively working on Community issues. The Community's evaluation/perception of the Company is very good in this regard.

Level 4:
There is a professionally created process to ensure that timely and accurate disclosure is made on all material matters regarding the Corporation, including the financial situation, performance, ownership and governance of the company. The quality of implementation is within the best in the Industry.
The board is actively working on Community issues. The Community's perception of the Company is excellent in this regard.

7. Board Contribution

Level 1:
Company financial results are not aligned with shareholders'/owners' expectations/needs.
The Board is not contributing to the Company's competitive access to Capital.
The Board is not helping the Company to improve its performance indicators.
The Board is not a factor in generating either Brand value or an excellent Company Image.
Intangible Capital is not a Board concern.
Stakeholders' evaluation/perception of the Board is poor.
The board is not a key factor in generating critical/needed strategies.
Company contribution to the Community is neither evaluated nor perceived as good enough.

Level 2:
The Board is proactively aligning needed financial results with shareholders'/owners' expectations/needs; results are still below Industry Standards, but the trend is positive.
The Board is not aware of its role in helping the Company to obtain competitive access to Capital.
The board is helping the Company to improve its performance indicators, which are not in the desired state yet.
The board is proactively working on improving Brand value as well as Company Image. Goals have not been met yet.
The Board is active in generating/preserving the Company's Intellectual Capital value. The first signs of improvement are present.
Stakeholder' evaluation/perception of the Board is improving, but not at an Industry Standard level.
Evaluation/Perception of the Company's contribution to the Community is starting to improve.

Level 3:
Financial Results are consistent with Industry Expectations. The board is recognized as a key factor in obtaining such results.
The company is obtaining competitive access to Capital. The Board is very helpful in this regard.
The Company's performance indicators are within accepted industry parameters.
The Company's Brand value is aligned with Industry standards. Company Image is very good. The Board has been instrumental to this situation.
The Board is active in generating/preserving the Company's Intellectual Capital value, with very good results.
Stakeholders' evaluation of the Board is very good.
Community evaluation/perception of the Company as a whole is very good.

Level 4:
Financial Results are better than those of Leading Companies in the Industry, and the board is recognized as a key factor in obtaining such results.
Company access to Capital is within the best in the Industry. Board activity is critical in this regard.
The Company's performance indicators are among the best in the Industry.
The Company's Brand value is better than Industry Standards. Company Image is Excellent. The Board has been instrumental to this situation.
The Board is recognized as a key factor in generating/preserving the Company's Intellectual Capital value. Results are excellent.
Stakeholders' evaluation of the Board is excellent.
Community evaluation/perception of the Company as a whole is excellent.
There are training/development plans for MGMT, which contributes to the excellent results of the Company.

Conclusions

Evaluation of the Board of Directors is a key strategic decision of the Enterprise, which will improve the BOD's contribution to the Company over time, providing the Directors with a reference against which they can establish comparison.
This better Governance level will, in turn, improve Company performance and shareholder value in the long term.
The proposed evaluation process constitutes the basis for the development of improvement plans for the BOD, with the matrix serving as a clear information tool that can help to establish targets for each criterion. Once it has been implemented, the matrix will also allow measuring progress against the established goals, both as an overall result as well as for each criterion separately.
The score and the factors can be professionally selected according to the board's development status in the selected geography at a given time.
We believe that this procedure can help to improve Corporate Governance at the Company, Country, Region level in a complete, yet simple manner.

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A SET OF QUALITY ASSESSMENTS AIMED AT IMPROVING CORPORATE GOVERNANCE

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The Role of Quality in The Corporate Governance

Improvement in corporate governance is a topical issue today. To pursue improvement, board audits and board and CEO self-assessment are spreading. However, observing the approaches currently used, legitimate doubts arise about the effectiveness of many of them. They may be reasonably effective in providing transparency to the investors, seemingly not so much in improving corporate governance. In the following, we will discusses the issue of corporate governance related assessments and their effectiveness, maintaining that a plurality of assessments - related to the company, the CEO and the board – is required, the whole set being part of a corporate PDCA cycle aimed at continuous improvement. The approach to self-assessment is also questioned, warning against rules and procedures based assessment, supporting instead diagnostic approaches that give the appropriate weight to those intangible factors that are at the basis of excellence.

The first objection that must be answered when discussing about quality in corporate governance is: what has quality to do with corporate governance? The plain answer is that quality is a concept that applies to any relation where people are involved, whether individual or collective (Conti, 2003). Corporate governance consists of relations - and important relations in fact - the most important being that between the board and the CEO.

Relations always imply material and immaterial exchanges, which are valued by the involved parties according to their needs and to their subjective - or inter-subjective, or objective - scales of value. In business relations, the main value that is normally considered is *fitness for purpose* (to what extent what we receive fits our purpose). That holds true for economic transactions, but also for business-related meta-economic relations (like the relations between the different governing bodies). Quite often the main quality problem in business relations is lack of definition of the expected values, followed by lack of delivery of the agreed upon values. Lack of definition often comes from inadequacy of goals or of agreed upon rules. Lack of delivery can be ascribed to inadequate control and to absence of systematic assessment. Rules of corporate governance are certainly the first point to address, since it seems that many huge problems have emerged around the world due to too

much distraction from the rules. But beyond the primary need for rules, synergy and cooperation will be claimed here as the most critical success factors in corporate governance. The second point that needs to be addressed is control, in relation to the application of the defined rules. Finally, the issue of how quality assessments can be applied to corporate governance, to check the effectiveness of the rules in achieving the planned results and to identify areas for improvement, is worth a specific discussion. The latter - assessment for improvement – is in fact the core theme of this paper; but first some basic points will be recalled – or proposed – to create the framework for the discussion.

The Corporate System to Which Corporate Governance Refers

Creating a governing architecture and defining governing rules that best assure meeting the company mission should be the purpose of corporate governance. This may be considered an excessively wide scope. In fact, if we take for example Baysinger and Hoskisson's definition (Baysinger et al., 1990), corporate governance is "the integrated set of internal and external controls that harmonize manager-shareholder conflicts of interest resulting from the separation of ownership and control". I believe that this, however correct, is a kind of "reactive" view of corporate governance, seen as a way to avoid conflicts. A "proactive" view, aimed at fostering cooperation and synergy among governing bodies, probably better fits our quality improvement perspective.

Governance is in fact a whole, which involves different logical functions of the business:
1) overall strategic guidance of the company; 2) global company system oversight;
3) management of the company according to the general strategic directions, with the broad mission of generating maximum value for the company itself and its stakeholders in the long run; 4) monitoring for compliance with laws, regulations, ethical behaviors, environmental and social responsibilities. The above logical functions are quite often combined, particularly in the case of the smaller companies. In general, different kinds and degrees of overlapping are present in all organizations. In public companies however, the tendency is towards a clear separation of roles - a process similar to the separation of power that takes places in political institutions between the legislative, executive and judicial functions (Handy, 1992). In fact, good corporate governance is much about separation and balance of roles – and thus of power - to the best interest of the stakeholders.

Separation of roles takes different forms in relation to local traditions and national legislation, but the most frequent separation is between the group of functions listed above under 1) and 2) – which fall under the Board's responsibilities - and those listed under 3) – which fall under the CEO's responsibilities. Function 4) deals with matters that should

clearly be under the CEO's responsibility, but may deserve a separate board committee for oversight. Specific board responsibilities are in fact normally attributed to different committees, like the CEO Nomination Committee, the Auditing Committee, the Compensation Committee, the Governance Committee etc.

In our enlarged view, the corporate governance network is not limited to the relations between the main centers of power. Since management of the enterprise – the bulk of activities - is entrusted to the CEO, the way the CEO organizes resources to achieve the expected results, the way he or she delegates power throughout the organization is extremely important from the overall corporate governance perspective. From such a perspective, the "organizational architecture" of the company is an important part of the governance chapter and extremely relevant from the corporate assessment perspective.

If we now look at the company not from the governance perspective but from the value adding stakeholders perspective, a different picture arises that may contribute ideas to the discussion about corporate governance. Figure 1 is a representation of the company system aimed at highlighting the stakeholder role (let us recall, having also TQM models in mind, that stakeholders are all those parties who co-operate to generate value in relation to company goals and expect fair benefits in return). We can conventionally call first-tier stakeholders those who have *both* major stakes *and* a major role in the company. The property, or the lead investors, need to be considered first, but not from the financial perspective, to protect their individual investments (such stakeholder role will be considered shortly). The stakeholder's role that is considered here is played by those investors – or representative thereof – who take care of the *strategic guidance* of the company, the entrepreneurial role that tends to fade in the public company where "..ownership has become divorced from control and is a mere legal fiction.." (Drucker, 1992). In public companies, such active relation is normally covered by the board (see # 1 in the aforementioned list of roles), who really should represent virtual ownership that is lost as a consequence of fragmentation of property rights. Such a role should be kept clearly separate from that of oversight (# 2 in the above list). The internal active stakeholders, who stake themselves and their own careers, are considered next. First among this group is the CEO, the person appointed by the board on behalf of the investors to achieve the company mission (see # 3 in the above list of roles). Then we have management and the employees. While the CEO has a seat in the board (sometimes the Chairman's seat, but that is a deep anomaly and is bound to disappear), the other two stakeholders are not represented (with some exceptions: in Germany having representatives of the employees in the board is a common practice).

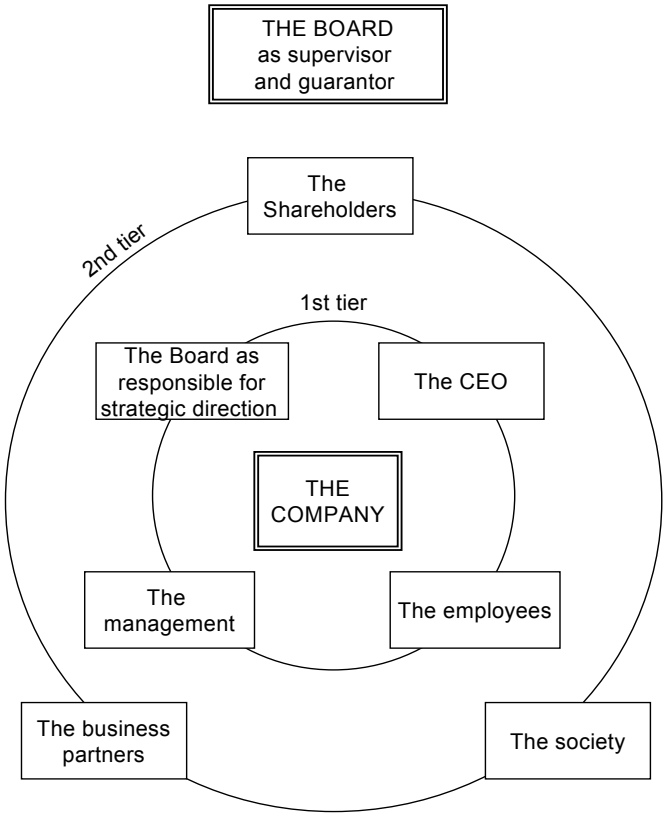

Figure 1 - Representation of the company stakeholders as a two tier system, focused on the company and supervised by the Board.

What I conventionally call second tier stakeholders are also represented in Figure 1. This group consists of two non-homogeneous categories that have *either* financial stakes in the company – the shareholders - *or* an active role in it (though not being formally part of it): the business partners. The society is an often hidden but important stakeholder that indirectly enters company transactions setting some rules (for example market related or aimed at protecting people and the environment) and controlling the outcome. The financial interests of the first category, the shareholders, are taken care of by the board. In fact this is considered today a major representative role for the board, aimed at protecting the large mass of the less protected, the small investors.

In the figure, the board's role as overseer and guarantor of the whole system (see # 2 above) is evidenced by representing it as a separate entity, above the parts. It is clearly separate from the stakeholders in that it should have no interest of its own to take care of: the good of the company should be its sole interest. To that aim, the board should also have the critical role of guarantor of the interests of all the stakeholders (not just the shareholders), in a fair and balanced way.

In previous papers the author represented the company/ stakeholder system as a kind of "gravitational system", with the company at the center and the stakeholders located on two orbits around it. Figure 1 is based on this view. However, it should be clear that neither the subdivision of stakeholders that has been chosen, nor the graphical representation, is critical to the aim of this discussion. What is critical to our discussion is simply the idea that corporate governance embraces all company activities *and relations* that are critical to the company mission, vision, and strategy. Among them, roles and relations between stakeholders are of paramount importance and the board should take care of them.

A Framework for Corporate Governance Related Quality Assessments

The above considerations allow us to define a comprehensive framework for corporate governance related quality assessments. In fact, the author believes that the effectiveness of the corporate governance system cannot be elicited by a board assessment only. A complete set of assessments is needed to check how the global governance system fits the purpose of fostering company performance. Such a perspective should not frighten the reader: we are not suggesting new kinds of assessments; we simply say that the board and CEO assessments should require, as a precondition, that the traditional company assessment is made (based on an appropriate TQM/Excellence model and using a diagnostic approach) and all the stakeholder related relations are properly explored.

The rationale of a comprehensive assessment is the following:

- The ultimate goal of corporate governance should be to favor successful performance in the long run and to make all the stakeholders benefit from it. The annual corporate self-assessment can be a powerful tool to identify the causes of the roadblocks and bring them to the attention of the board. To be really effective, such an assessment should be part of a systematic annual PDCA cycle.

- In the context of such self-assessment particular attention should be directed to the "organizational architecture", the way the company is organized and managed to meet its goals. As previously stated, the organizational architecture is part of the governance issue; not from the point of view of the balance of power between the major parties, but in relation to company operational management. This part of corporate self-assessment is not normally adequately investigated, and the focus of TQM assessments is often limited to the processes.

- Special attention should also be paid to the stakeholders, their relations with the company and among themselves. Stakeholders can in fact turn into strategic assets for the company, if properly managed. On the contrary, they can give rise to dangerous corporate diseases if mismanaged (Conti, 2002).

- On the foundation of sound corporate self-assessment (possibly followed by the CEO's review), the specific assessments required by corporate governance at the top can be

performed. In the author's view, since quality here is more a matter of each party giving the others the values that they expect (partly reflected by the rules, partly going beyond the rules), assessment should always be a reciprocal process: self-assessment in relation to the delivered qualities first, followed by the other parties' assessment in relation to the received (and perceived) qualities.

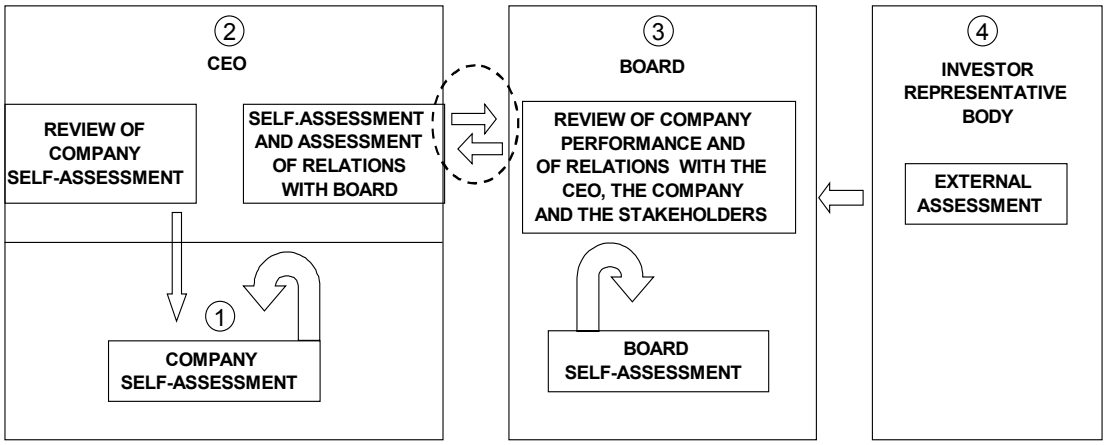

Figure 2 - A map of corporate governance improvement related assessments (1 and 2) completed with an external assessment (4) aimed at giving customer confidence about the state of corporate governance

Figure 2 represents the scheme of the assessments that ought to be carried out in accordance with the above view. Company self-assessment is the first (# 1 in the figure), possibly followed by a CEO's review. Such a self-assessment should be diagnostic, going from results to causes. It should start from company performance in relation to its current goals, reference competitors, performance in previous years – and taking into account future goals. The emerging performance gaps should then be the starting point to identify the relevant causes, both at the process and systemic factor levels. Second comes the CEO's self-assessment (# 2 in the figure) in relation to both previous company assessment results and to the CEO- board relations. This latter assessment deals with the CEO's perception of fulfillment of his/her own obligations to the board. It should be completed by the CEO's evaluation of the board performance in relation to his/her own expectations. Finally, (# 3 in the figure), two assessments should be made by the board. The first aims at evaluating the company's and the CEO's performance, based on the company/CEO self-assessments; the second is the board's own self-assessment. Board self-assessments should certainly be

based on clearly stated governing rules and an annual activity plan; but great emphasis should be placed on those immaterial aspects that are key to company excellence: creation of cooperation and synergy among the company stakeholders and among the governing bodies. In fact, quality needs rules, but real value creation depends on the ability of creating winning teams.

Company Self-Assessments

Let us examine assessment # 1, figure 2: company self-assessment. It is widely recognized that self-assessment can be a powerful tool to improve company performance, mainly if it is regularly performed in the context of an annual corporate PDCA cycle. From the board perspective it can be a valuable source of information about the company (quite often board directors complain of lack of information). Self-assessment can provide an exhaustive picture of the company's competitive performance, spanning from business results to customer satisfaction and loyalty, from employee motivation and satisfaction to levels of synergy in the company's relations with its business partners. In addition to that, self-assessment – if properly performed, i.e. with a diagnostic approach – can provide information about the state of those critical organizational factors that are responsible for company performance.

We do not enter here the specific issue of organizational self-assessment (Conti, 1997). Only some aspects that are particularly important from the corporate governance perspective will be discussed: the organizational architecture of the company and the relationship between stakeholders, two issues that are normally underestimated in the assessment process.

Organizational structures "….rarely result from systematic, methodical planning. Rather, they evolve over time, in fits and starts, shaped more by politics than by policies." (Goold et al., 2002). Given the importance of organizational "fitness for purpose", a thorough and deep evaluation of such fitness by management, confirmed by the CEO, is extremely useful to the board in view of a global corporate assessment. A possible guideline for organizational architecture assessment is given in the author's book "Organizational self-assessment" (Conti, 1997), where formal and informal organization is investigated as well as the process/function tradeoff, the decisional processes, and internal communication. But an even more authoritative suggestion can be found in the paper by Goold and Campbell mentioned above. The authors propose nine tests of organizational design, dividing them into four "fit tests" and five "good design tests":

1. ***The market advantage test*:** "Does your [*organizational*] design direct sufficient management attention to your sources of competitive advantage in each market?

2. ***The parenting advantage test*:** Does your design help the corporate parent add value to the organization?

3. ***The people test*:** Does your design reflect the strength, weaknesses and motivation of your people?

4. ***The feasibility test*:** Have you taken account of all the [*organizational*] constraints that may impede the implementation of your design?

5. ***The specialist culture*:** Does your design protect units that need specialist cultures?

6. ***The difficult link test*:** Does your design provide coordination solutions for the unit-to-unit links that are likely to be problematic?

7. ***The redundant-hierarchy*:** Does your design have too many parent levels and units?

8. ***The accountability test*:** Does your design support effective controls?

9. ***The flexibility test*:** Does your design facilitate the development of new strategies and provide the flexibility required to adapt to change?

The above is just a bare list of the items discussed by Michael Goold and Andrew Campbell in their excellent paper, to which one should refer for deeper analysis. Additional ideas on this subject can be derived from reading the stimulating book written by David A. Nadler et al. "Organizational Architecture" (Nadler et al., 1992)). Our thesis here is that this area is so important that it cannot be ignored in corporate assessment. Surprisingly, TQM models normally limit their organizational scope to process management, just a part - however important - of the global theme of organizational fitness for purpose.

The second area that we warmly recommend addressing in company assessment (as well as in the subsequent CEO and board assessments) is that of stakeholder-related relations. Stakeholder-to-company relations are the most important and critical; however, stakeholder-to-stakeholder, stakeholder-to-CEO, and stakeholder-to-board relations should also be carefully analyzed when pertinent. Excellent companies are characterized by high quality (i.e. high value adding, or synergetic) stakeholder relations. On the contrary, imbalance and conflicts in the company stakeholder system are a frequent cause of serious organizational diseases (Conti, 2002).

CEO Assessment and Self-Assessment

CEO assessment by the board seems to be a rather widespread practice among the most prominent companies. According to the 1996 Korn/Ferry survey, about 70% of Fortune 1000 companies had adopted a formal procedure for evaluating their CEOs (Conger, J.A. et al. 1998). However, CEO assessment is normally linked to CEO compensation only – and is in fact taken care of by the compensation committee in most cases. Instead, CEO

assessment should be seen as an intrinsic part of the corporate governance improvement process and, as such, the board governance committee should be responsible for it.
Obviously, other board committees (or the whole board) can be involved from various perspectives or at different moments, as is the case of the strategic committee in the goal setting stage or the compensation committee when deciding on the amount of the compensation.

The CEO assessment process should involve at least two formal stages: establishing evaluation targets at the beginning of the fiscal year and assessing the results at the end of the year. At least one intermediate check is advisable, but not as formal and complete (in terms of data) as the final assessment. The goal setting stage should be based on the annual strategic plan, establishing both short term and long term objectives. However, limiting it to the business and financial goals may be sufficient from the compensation perspective, but not from the long-range governance improvement perspective. Goals related to customer satisfaction and loyalty, mutual satisfaction in stakeholder relations, and ratings from institutional investors should be added, as well as the most critical internal factors, related to people and process. But, when shifting from a compensation-related assessment to a governance-related assessment, the horizon should be still further enlarged. The nature and the rooting of corporate core values should be assessed, as well as the growth in corporate quality culture, corporate learning capability, sense of belonging, and care for the long-term success of the company. That is why company self-assessment becomes so important (see previous section): global company assessments based on advanced TQM/Excellence models can give appropriate answers to the request for tracking the company state and future perspectives beyond what the traditional business and financial indicators can say. If the aim is to have a global corporate assessment at the end of the fiscal year, as part of a corporate PDCA cycle, then appropriate goals should be envisaged wherever possible. Quite often, in particular when starting such an approach, board directors and even the CEO may find it difficult to identify appropriate goals for non-tangible factors. In that case, what is important is identifying appropriate assessment criteria for the chosen factors, so that improvement goals can be given and the results tracked.

The CEO's assessment by the board is then necessary but not sufficient. A sequence of three assessments is needed, where the first two are just part of the company improvement cycle; only the third is specific to the CEO's performance evaluation. The three assessments are represented in Figure 2 and the first is illustrated in the previous section. The second assessment is the CEO's self-assessment, which takes as a reference the goals agreed upon with the board at the beginning of the year and incorporates the major outcomes of the previous company self-assessment. In relation to compensation, the CEO's self-assessment form could be a synthetic document, a list of goals that allows for appropriate rating (poor, acceptable, outstanding), plus space for open-ended questions. In relation to corporate governance improvement, what becomes very important is the CEO's review of the company self-assessment, inasmuch as it contains extremely valuable information both to support the synthetic self-assessment document and to provide the board with the basis for its own assessment. Such review should be completed by the CEO's evaluation of his/her relation with the board.

The Board-Related Assessments

The specific issue of Board assessment is discussed with great detail in the paper by Bertin and Strachan: "The Impact of Corporate Governance on the Quality of Management" (Bertin, Strachan, 2004). Following, some of the aspect of the theme will be examined within the framework of the corporate assessments illustrated in Figure 2.

Board-related assessments - represented under 3 in the central block of Figure 2 - relate to the two main roles of the board (see Figure 1): as supervisor and guarantor on behalf of all the company stakeholders and as the party responsible for strategic direction, the entrepreneurial role that puts it in a dialectic position with respect to management, who is charged with turning strategic vision into operational reality. The author believes that such distinction should be made in order to have a less ambiguous assessment process. In relation to the first role, the main aim is to assess the whole corporate system to allow for a clear picture of the present state, strength and weaknesses in relation to future challenges and recommendations for improvement. A global evaluation of the "fitness for purpose" of the whole governance system should be part of such an assessment (including organizational architecture and stakeholder roles and relations). That should be the key assessment, which can provide visibility for stakeholders on one hand, and improvement suggestions for management on the other. Then comes the board's actual self-assessment, that deals with both roles: how well the board performs in relation to its supervisory role; how effective it is in supporting management with sound strategic directions.

The two assessments are conceptually so different that they need different rules and approaches: the first requires mainly a deep and critical analysis of the data coming from the company's and CEO's assessments, plus an independent analysis of the overall corporate governance system, while the second requires ability for introspection. Most board assessment schemes today are in fact board self-assessments. They make reference to questionnaires where the evaluation questions stem from good governance rules and recognized best practices. The NACD (National Association for Corporate Directors) Questionnaire, for example, lists twenty six questions, divided into seven groups: Overall, The right people, The right culture, The right issues, The right information, The right process, The right follow-through (NACD….). The UNOCAL Questionnaire lists forty three questions in five groups: Board structure, Board meetings, Key board responsibilities, Board and management, Other (NACD….). The American Red Cross Board of Governors Questionnaire lists thirty questions in nine groups: Rules and responsibilities, Board and CEO, Risk issues, Financial oversight, Board role in fund raising, Board member development, Board meetings – effectiveness, Committee meetings – effectiveness, Board effectiveness (NACD….).

The usual habit seems to be surveying board directors by means of questionnaires. While questionnaires are important to clarify and, to a certain extent, quantify directors' opinions, face-to-face interviews allow a deeper understanding and at the same time guarantee a more uniform comprehension of the questions. Combination of the two is advisable. Interviews to board members should preferably be conducted by an external high level person, possibly the same person who interviews the CEO (interviewing both parties provides additional insight).

The aforementioned questionnaires are designed expressly for the purpose of self-assessment. Although this is good, the author recommends that they be used in the context of higher scope TQM/Excellence models, like the American MBNQA or the European EFQM. In relation to the self-assessment *process*, the author suggests a diagnostic or "right to left" approach (Conti 1997), which starts with performance gap analysis and looks for causes. In fact, besides getting numeric scores for each assessment criterion, what is important for directors is to understand the cause for each performance that is below expectations.

As pointed out previously, to put board self-assessment in the proper light, the following information should be preliminarily available to the board directors, before any questionnaire is filled in or interview is made:

- The company's results in all areas of business and of stakeholder relations (shareholders, employees, business partners, the society)
- The results of the annual company self-assessment (validated by the CEO) to give evidence of organizational strengths and weaknesses in relation to the aforementioned results and to future goals. The extension from purely business and financial results to customer and stakeholder related results is important because it allows seeing reality from a different perspective. Critical analysis of the organizational architecture should be considered part of the assessment.

Beyond that, the self-assessment process should be based on:

- The board's annual objectives, defined at the beginning of the fiscal year.
- The results in relation to such objectives, with particular evidence of the relationship between what the board did and the relevant business outcomes.
- Corporate governance written rules and current practices, as well as external references and trends. .

The assessment should focus both on the board's performance gaps (distance between board results and objectives) and goal gaps (inconsistencies between board objectives and company objectives).

The board should appoint an assessment committee chaired by an external lead director, to manage the entire self-assessment process. The committee should take care of the complete evaluation process. Members of the board should be given enough time to analyze all the gathered information.

The assessment committee should analyze the results and compile a report that, while cumulating data to provide global information, preserves the comments – in particular the most significant – as intact as possible. The report is then presented to the board, who discusses it, identifies the areas for improvement and generates the improvement plan. Finally the self-assessment process itself should be discussed, to identify weak points and make improvements for the next round.

Board Self-Assessment Effectiveness

Having stated the above, a doubt arises: are we sure that defining board responsibilities, governance rules, best practice, self-assessment procedures, provides a reasonable guarantee against the occurrence of governance problems? Unfortunately the answer is no. The recent history of corporate failure seems to prove that just behaving according to the book does not guarantee success. As J. A. Sonnenfeld puts it in a recent Harvard Business Review article, the big companies that resoundingly failed in the recent past could all "pass the tests that would normally be applied to ascertain whether a board of directors was likely to do a good job" (Sonnefeld, 2002). "It's time for some fundamentally new thinking about how corporate boards should operate and be evaluated" continues Sonnenfeld " We need to consider not only how we structure the work of a board but also how we manage the social system a board actually is… Most of the remedies are structural: they are concerned with rules, procedures, composition of committees, and the like, and together they are supposed to produce vigilant, involved boards….The key isn't structural, it's social…What distinguishes exemplary boards is that they are robust, effective social systems". And then Sonnenfeld talks of respect, trust, candor, culture of open dissent…are these not values?

In fact, if compliance with rules is a necessary but not sufficient condition to avoid failures, it is not, by any means, a recipe for excellence. This paper started by saying that real quality is about value exchanged in any relation. **Rules and procedures can, at their best, guarantee conformance. Excellent performance can be achieved only by small or large teams of people who share those values that are fundamental to create the team spirit and pursue the same vision**. In such an environment, people are inclined to generate the reciprocally expected values and together, through a synergic effect, they are able to create and deliver high levels of value to customers and stakeholders.

That is why core values should be put in first place –followed by behaviors. Self-assessment, that aims at improving corporate governance and in particular board performance, should then start by addressing the issue of corporate values, to ensure that the company has not only defined but also deeply rooted a set of core values that have been

identified as key to sustained success. Similarly, the board should guarantee that the company vision and mission are shared at all levels in the organization. Values should dictate ethical behaviors, and this is the key to generating the expected values in any company relation, the elementary roots for any quality outcome. Obviously, if it is part of the board's role to foster the value-based characteristics that make an organization excellent, the board itself should be the first to embody those characteristics. That is what Sonnenfeld's paper seems to imply when talking about "a virtuous cycle of respect, trust and candor….in which one good quality builds another" (ibid.)

To enhance the effectiveness of board assessment, the "soft" aspects (values and real behaviors) should be given great importance. Formal and mechanistic approaches should be avoided and a diagnostic (right-left) approach - starting from past result, focusing on performance gaps and searching for root causes - should be adopted.

External Assessment

Companies that adopt a reliable set of corporate assessments should welcome external assessments (or external audits) performed by acknowledged investor representative bodies. Furthermore, such bodies would certainly consider corporate self-assessment a very useful basis for their work. Figure 2 (right-hand block) represents such an assessment, which is carried out from the shareholder perspective. External assessments of this kind are seldom practiced now, but given their importance for the investors they should grow in the future. Standards & Poor, for example, carry out such assessments involving analysts from S & P's Corporate Governance Services, local law firms and other professionals in corporate governance where appropriate. They use a Guideline that considers four "Components": The ownership structure; Financial stakeholder relations; Financial transparency and information disclosure; Board structure and processes. The audited company–receives a Corporate Governance Score that reflects Standads & Poor's opinion on the extent to which the company adopts and conforms to codes and guidelines of good practices of corporate governance.

External assessments are very useful to the shareholders, while internal assessment, besides being essential for continuous improvement, would also be very useful to all the company's stakeholders.

Conclusions

Corporate governance related self-assessments – like all self-assessments – if properly conceived as part of a corporate PDCA cycle, are crucial for improving company performance, while providing the basis for corporate transparency towards the investors. According to the still diffused mentality "if it ain't broken, don't fix it", the problem of board and CEO assessments has come into fashion only recently, after the well known

corporate scandals. Let us seize this opportunity to move, also in corporate governance, from a "fix it" to a "prevent it" mentality. However, the following recommendation should be made: not to take a shortcut but to allocate self-assessment in the context of continuous improvement of corporate governance, to make the company stronger, healthier, more competitive, and a better place to live in. The complete set of assessments examined in this paper should be implemented in a non-bureaucratic, co-operative way.

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Dr. Armand V. Feigenbaum is President and CEO of General Systems Company, a global leader in implementing greatly improved results in many of the major manufacturing and services companies throughout the world by designing and installing proprietary management operating systems.

Before his position with General Systems, Dr. Feigenbaum was executive for worldwide manufacturing operations and quality for General Electric Company. He holds the Bachelor's degree from Union College and the degrees of Master of Science and Ph.D. from the Massachusetts Institute of Technology. He has received a Doctor of Science Degree from Union College, and has been awarded a Doctor of Humane Letters degree by the University of Massachusetts. Union College has dedicated the Armand V. and Donald S. Feigenbaum Hall, the building that houses its president and vice presidents, in his and his brother's name. University of Massachusetts has established the Armand V. and Donald S. Feigenbaum Distinguished Professorship. He has been awarded the degree of Doctor of Science by the Massachusetts College of Liberal Arts. Armand Feigenbaum has been recognized with the "Outstanding Engineering Alumnus" award by his undergraduate alma mater, Union College.

He is the author, with Dr. Donald S. Feigenbaum, of the book, *The Power of Management Capital*, published in 2003 by McGraw-Hill and setting a new direction for management in the twenty first century not only in industry but also in health care, education, public administration and technology. Reviewers have stated about it that "rarely has one book had the intellect and authority to change business and the way business is approached and conducted" and "it is about the next great wave of corporate dominance – innovation in business management and leadership."

Dr. Feigenbaum is also the originator of Total Quality Management, the approach to quality and profitability that has profoundly influenced management strategy in the competition for world markets in the U.S., Europe, Asia and Latin America. The several editions of his famous book *Total Quality Control* have been published in more than a score of languages including French, Japanese, Chinese, Spanish and Russian, and are widely used throughout the world as a foundation for management practice.

Dr. Feigenbaum was elected to the National Academy of Engineering of the United States in 1992. He serves as the founding Chairman of the Board of the International Academy for Quality, the worldwide quality body. He served two terms as President of the American Society for Quality and one term as Chairman

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In 1988 Dr. Feigenbaum was appointed by the Secretary of Commerce in Washington, D.C. to the first Board of Overseers of the Malcolm Baldrige National Quality Award Program.

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Since 1993 Mr. Watson has provided executive quality consulting services to some of the world's leading firms that include: Nokia Mobile Phones, Hewlett-Packard, DuPont, Monsanto, American Express, Ford, ExxonMobil, ST Microelectronics, and Toshiba. Previously, he was Program Manager for Quality Leadership at Hewlett-Packard, Director of Corporate Quality for Compaq Computer, and Vice President of Quality at Xerox.

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Mr. Watson was awarded the 2001 ASQ Lancaster Medal recognizing his global efforts for promoting the quality sciences and he received the 2001 Association for Quality & Participation (AQP) President's Award in recognition of his career contributions to the quality profession. Also in 2001, Mr. Watson delivered a 50th Anniversary Deming Lecture to the Japanese Union of Scientists and Engineers. In 2000 he was named one of the global "21 voices of quality in the 21st century" by ***Quality Progress*** magazine.

Mr. Watson has an undergraduate degree in liberal studies from Taylor University, a master of science degree in systems management from the University of Southern California, a master of arts degree in legal analysis from Antioch University School of Law and a master of science degree in industrial engineering from Oklahoma State University. He is presently working on his PhD. in managerial economics at the Maastricht School of Management in the Netherlands.

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-Member of the Executive Committee of IAGO (Institute of Directors of Argentina) and of the board of the Latin American Institute for Corporate Governance.
- Chairman of the International Academy for Quality (IAQ).

- Fellow and CO Chairman of the International Cooperation Committee of the American Society for Quality.

- Member of the National Association for Corporate Directors, Washington DC, USA.

- Jack Lancaster Award, American Society for Quality.

- Collaborated with OCDE, World Bank in the elaboration of the Corporate Governance White Paper for Latin America.

- In July 2003, invited by the World Bank to participate in the "Global Corporate Governance Forum", conducted by Yale University in the World Bank Building in Washington DC.

- Guest speaker on Quality and Governance at the International Quality and Business Conferences in the USA, France, Hungary, Israel, Japan, Mexico, Brazil, and Argentina.

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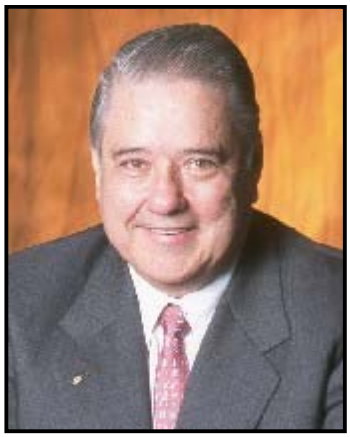

Worked with Hewlett Packard Argentina from 1977 until 2003.
Accomplishments as Hewlett Packard Argentina's CEO:
- Growth: sales from 12M U$S in 1991 to 317M in 1999 (before the spin off of its instrumentation Business Group, now Agilent Technologies) to use comparable data.
- Quality of Management: Hewlett Packard Argentina won the PQA (President´s Quality Award) in 1998. The PQA is a prize with which the CEO of HP Co. recognize the entities that show a consistent high quality management environment, which should, of course, be the key factor to excellent overall results. Hewlett Packard Argentina presented 8 years of consistent performance in all the measured variables (financial results, customer satisfaction, employee satisfaction, key local initiatives, penetration in the local community, etc) The prize was delivered in Palo Alto, Ca, in Feb 1999, by the former HP Co.CEO Lew Platt.
- Training: besides the many and diverse HP courses on Management, TEP (The executive Program) a 6 week Management program, done in June-July 1996 at Darden School of Management (University of Virginia).
- Management of values at Hewlett Packard Argentina: in the year 2002 an image survey of local companies was produced, in which Hewlett Packard Argentina was clearly recognized as the number one in its industry, well ahead of its competitors, with excellent qualifications in all the surveyed areas, and exceptional ones in ethical behavior as well as Management capabilities (Survey Clarín Newspaper, Aug. 2002).

Current and past 'volunteer' positions/roles/accomplishments:
CICOMRA, Cámara de Informática y Comunicaciones de la República Argentina
Founder Member in 1985.- Has been a Board Member since.-
Cicomra represents the interest of the Informatics and Communication business community in Argentina.
FUNDECE: Fundación Empresaria para la Calidad y la Excelencia (Business Foundation for Quality and Excellence).
Member since 1992, elected to the BOD 1993, named President for the period 1995-1997 and re-elected for the period 1997-1999. Presently a member of its Board of advisors.
Amcham: (American Chamber in Argentina).- Elected to its BOD in 1996, until December 2002.
IAQ: International Academy for Quality: elected as a member in 1998.
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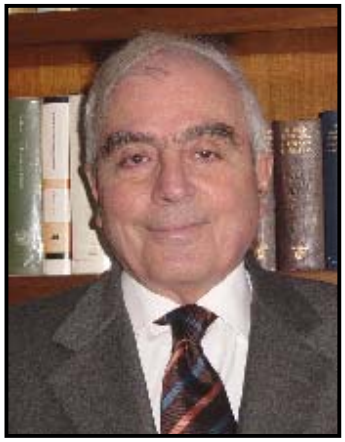

Doctoral degree in Electronic Engineering from the University of Bologna, Italy.

Till 1991 with the Olivetti company, computer and component areas. Major responsibilities: C. E. O. of OLCEA, a subsidiary of the Group developing application specific integrated circuits; Director of Corporate Quality for the Olivetti Group.

From 1987 to 1992 President of UNINFO, the Italian standardization body in the area of Information Technology.

From 1992 to 1994, President of the European Organization for Quality.

From June 1997 to May 2000 President of the Italian Association for Quality

Since 1991 independent consultant in TQM and Organizational diagnosis. Managing partner of OAM (Organizational Assessment Management) s.a.s.

Visiting professor for organizational assessment in different universities.
Member of the Assessment Teams of the Universities: "La Sapienza" in Rome Federico II in Naples.

Member of the Advisory Board of the e-TQM College, Dubai
Vice President of the International Academy for Quality.

Member of the International Editorial Committees of: *Total Quality Management*, Carfax Publ., UK; *European Quality*, Europ. Qual. Publ., UK.; *Internet Journal of Quality*, IQA, UK.

Honorary Member of the European Organization for Quality

Fellow of the American Society for Quality

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