CORPORATE GOVERNANCE FOR NOT FOR PROFITS

Thank you for inviting me to speak about Corporate Governance in the NFP sector.

I have grappled with how to make this 20 minutes interesting, useful and perhaps a little challenging to a group of experienced NFP Directors and Officers who I am sure understand quite well the rules, regulations and frameworks that we must all operate under.

I am often asked and indeed often ask myself – is corporate governance different in the NFP sector than the for profit sector. Generally the answer I think is no; apart from what is in my experience a community expectation that NFP’s will be more responsible, more accountable and more ethical than the ‘for profits’.

Whether or not these expectations are met is dependent on how directors, boards and senior management behave and how that behaviour is perceived. So rather than focus on the easy corporate governance issues relating to directors duties, rules and frameworks what I propose to do is to explore the mysterious human dimension of corporate governance.

I define corporate governance as “the way we choose to do things around here”. The way that we, the people, deliberately choose to interpret and use the technical tools, rules and frameworks of the discipline known as corporate governance. The way we work together, the way we make decisions.

For me corporate governance is all about the people and the way in which they relate and behave.

There is a wonderful passage in one of Margot Cairns books that I often reflect on when particularly when things are not going so well:

“The problem with people is that they are hard to get on with. They lie and cheat, and do things the way they want, which is rarely the way I would have them behave.

“People put their own meaning on events, actions and situations. They make their own decisions, have their own value sets and their own agendas.

“They live life to their own standards and relate in their own ways. People have their own weaknesses and their own strengths.

“They perceive me and my actions their way, not the way I would have them do so. People insistently, steadfastly and uncompromisingly go on being themselves.” Cairnes, 1998.

We have to work within the wonderful reality that we are all different, and be committed to helping each other to be the best team players we can be for the benefit of our organisations.
It is not rules and regulations that run organisations and their processes. It is people who design and oversee technological systems and fix them when they break down.

People make all the key decisions and even with the best-of-breed quality control systems in place, major corporate fraud, workplace accidents, and business failures are possible.

The logical extension of this for me, given the responsibilities vested in us as directors, is that corporate governance is all about the way in which we engage in leadership as individual directors and as boards of directors.

**What is director leadership?**
Leaders ask the right questions about strategy and make sure that the right answers are implemented.

“Leadership is about vision and having the courage to do the right thing – different from management, which is all about doing the right thing – even if there is a risk”

“Leadership is of the spirit, compounded of personality and vision; its practice is an art. Management is of the mind… its practice is a science.”

Providing leadership in directorship in my view means using all of our skills and attributes with the best of intentions to make:

- The right decisions
- For the right reasons
- At the right time
- And in the right way.

How we choose to make our decisions is guided by the rules and regulations society puts in place to establish standards and is significantly influenced by our individual values and beliefs and the way we go about the decision making process. The choices we make and the way we behave will determine the standard of our corporate governance and the success of our organisations.

Today I would like to explore how good governance can be achieved through examining new ways of thinking and creating great boards through understanding behaviour and team dynamics.

**Ways of thinking for the future**
The world in which we operate today is characterised by uncertainty and ambiguity, a huge amount of information that is widely accessible, expanding communications pathways and very demanding communities and stakeholders expecting high levels of accountability of people in decision-making roles.

If we are to be successful in this environment I believe we need new/better ways of thinking and behaving.

The neuroscientists tell us that the four pillars of learning and change are:
1. data collection
2. reflection
3. creating
4. testing.

They also tell us that emotion significantly influences how we work through this process. The rational and emotional are both incredibly important to our decision making but we rarely acknowledge let alone discuss the role of emotion and its effect on our thinking and behaviour.

In his book Five Minds for the Future, Howard Gardner, a researcher in psychology, posed the following question, “What kind of minds do we need if we are to create a world in which we would like to live?” I reframe this as, “what kind of minds do we need to create the organisations and boards which are capable of delivering the very best to the stakeholders we serve?”, and where our efforts are "...dedicated toward the acquisition of the appropriate disciplinary knowledge, habits of mind, and patterns of behaviour... to eradicate erroneous or unproductive ways of thinking...and deciding."

His answer is five kinds of minds and I invite you to imagine what your organisations would be like if directors, boards and senior executive were to develop and apply their disciplinary, synthesizing, creative, respectful and ethical minds to their potential.

As I describe to you what he means by each type of mind or way of thinking perhaps you might reflect on how you personally engage with each type of mind and bring them together in your practice as a director.

1. **The disciplinary mind.** All directors bring some disciplinary expertise to the table but the disciplinary mind also involves a way of thinking and is capable of distinguishing between subject matter and discipline. In the area of subject matter, large number of facts, formulas and figures will have been committed to memory but the discipline part represents a distinctive way of thinking about the world. For example, one does not confuse correlation (A occurs before B) with causation (A caused B); In applying the disciplinary mind you are aware that current consensus is subject to challenge based on evidence – in fact you look for and invite the challenge.

2. **The synthesizing mind** is competent at selecting the crucial information from the copious amounts available. It has the ability to integrate ideas from different disciplines or spheres into a coherent whole and to communicate that integration to others. Narratives or stories and powerful metaphors, images and themes will be used. Powerful communicators will link different kinds of synthesis with different learning styles:
   - a linguistic mind would favour a story
   - a logical mind would be interested in some kind of equation or theory
   - a spatial mind would flavour a chart, drawing, diagram, etc.

Synthesis is becoming increasingly important now that data overload prevails and synthesizing the current state of knowledge, incorporating new findings, and delineating new dilemmas is part and parcel of the work of any director.

3. **A creative mind** involves breaking new ground. In this mode of thinking you have a capacity to put forth new ideas, pose unfamiliar questions, conjure up fresh ways of
thinking, uncover and clarify new problems, questions and phenomena with unexpected answers. The creative mind goes beyond existing knowledge and syntheses to pose new questions, and offer new solutions. This is the mind that is engaged in formulating new direction and vision.

The difference between synthesizing and creating minds is that “... the synthesizer’s goal is to place what has already known into the best, useful and illuminating a form as possible. The creator’s goal......is to extend knowledge, to ruffle the contours of the status quo, to guide a set of practices along new and hitherto unanticipated directions. The synthesizer seeks order, equilibrium, and closure: the creator is motivated by uncertainty, surprise, continual challenge, and disequilibrium.” As directors we have to recognise and manage these conflicts.

4. **The respectful mind** involves welcoming differences and having an understanding, awareness of and appreciation of differences among human beings and human groups. In a world where we are all interlinked, intolerance or disrespect is no longer a viable option. The respectful mind is essential to seeking to understand others on their own terms, extending trust to and working with others who are different and avoiding as much as possible, thinking in group terms. “Respect emerges as time- and situation-specific, rather than as an assumption that governs our human relations... respect should not entail a complete suspension of judgment. When a person consistently acts disrespectfully toward others, that person should be called to account.”

5. **The ethical mind** involves understanding and recognizing your responsibilities as a citizen of a group, community, region, nation and the world, i.e. striving to serve purposes beyond self-interest. Ethics is about relationships:

   - It's about struggling to develop a well-informed conscience
   - It's about being true to the idea of who we are and what we stand for
   - It's about having the courage to explore difficult questions
   - It's about understanding risk accepting the cost of decision making

The ethical mind is engaged whenever we make decisions; when we ask - what ought one to do? This is a question that is extremely difficult to avoid. Indeed, the only sure way to do so is to be a creature of unthinking habit who goes about life doing things “because everyone does it” or because “that's just the way we do things around here” or because “it seemed like a good idea at the time”. This sort of unthinking custom and practice is a real threat to good decision making'. An ethical mind is fundamental to good governance.

Bringing our five minds individually and collectively to the board table should allow us to make confident technical contributions, exercise sound judgement, create the vision, build great relationships and earn respect.

If only it were so simple. So how do we bring our minds together to create a high performing team exercising exemplary corporate governance in the boardroom?

**Board dynamics and behaviour**
Most directors and senior managers start their careers in technical specialties, such as engineering, accounting, or law. Initially, their work concentrates on specialised aspects of their field with little emphasis on people skills and human behaviour.

So while they are capable of valuing and safeguarding intangibles such as a brand or professional reputation they are less capable of dealing with human behaviour. Rules and regulations are clearly understood – the nuances of values and beliefs and their importance in behaviour and decision making around those rules and regulations are a bit of a mystery.

Our values and beliefs are the key internal drivers of our behaviours and emotions – we use them to make sense of reality.

If we have a belief that good governance deals only with visible, measurable facts and a board member interrupts proceedings to ask questions because they have an intuition that something is not right, but are unable to prove their suspicions, we are likely to see them as a nuisance.

If we believe that emotions are uncomfortable, or even dangerous, we unconsciously punish someone who openly voices an opinion or emotion that causes us discomfort.

In comparing boards that failed with boards that succeeded, Jeffrey Sonnenfeld found that there was no significant difference in the formal aspects of governance between good and bad boards. What brings boards and companies down is not tangible, visible, and measurable. What brings boards and companies down is dysfunction within their social system.

It's difficult to tease out the factors that make one group of people an effective team and another, equally talented group of people a dysfunctional one; well-functioning, successful teams usually have chemistry that can't be quantified. They seem to get into a virtuous cycle in which one good quality builds on another. Team members develop mutual respect; because they respect one another, they develop trust; because they trust one another, they share difficult information; because they all have the same, reasonably complete information, they can challenge one another's conclusions coherently; because a spirited give-and-take becomes the norm, they learn to adjust their own interpretations in response to intelligent questions.

Sonnerfeld concludes that if a board is to truly fulfil its mission it must become a robust team-one whose members know how to ferret out the truth, challenge one another, and even have a good fight now and then – in other words develop effective social systems with a virtuous cycle of respect, trust and candour – employing the five minds.

Exercising your five minds and engaging a Portfolio of Roles at the board table is critical to building a robust social system. When board members don't challenge one another, individual directors' preferred roles - the ruthless cost cutter, the damn-the-details big picture guy, the split-the-differences peacemaker - can become stereotyped or rigid. Effective boards encourage and support their members to play a variety of roles, in some cases dipping deep into the details of a particular business, in others playing the devil's advocate, in still others perhaps serving as the project manager. Playing different roles gives directors new perspectives, a wider view of the business and of the alternatives available to it.

So how do you recognise and judge when and how a board is dysfunctional? Surely all of our boards are robust social systems?
What are some of the signs that might indicate otherwise? If you answer yes to any of the following questions you may need to think about the conversations and actions that are needed to redress the dynamic.

- Are there dominant personalities who override others?
- Are there directors who struggle to exercise their voice?
- Is dissent discouraged?
- Are questions encouraged?
- Are decisions sometimes hurried and based on inadequate data?
- Do things that could adversely affect the company’s image and affect staff morale get covered up?
- Is the board swamped with information at short notice?
- Is meeting time used up on trivial matters and more important matters rushed through at the end of the meeting because of lack of time?
- Are particular stakeholders or interests favoured?

It is often very difficult to speak up even when your gut tells you that things could work better. Human beings are social animals, genetically programmed to live and to work in communities. Human group behaviour reflects a deep desire and a need for group acceptance. We struggle between meeting our need to be individual, and our desire for socialisation and acceptance in society. Socialisation generally demands behaving in a way acceptable to those around us. This is core to the human psyche and a great challenge for those striving to achieve great corporate governance – if you can’t build a board culture with a that virtuous cycle of respect, trust and candour that I discussed earlier then you are at risk of group think.

In our organisations, the stated rules typically consist of laws, regulations, the company constitution, board charter, values, and ethics statements. These stated rules can however be undermined or negated by covert rules, such as those that support group think.

All groups have norms, the rules about what is required to be a member of, and accepted by the group. While these norms will differ from group to group there is one rule that is invariable: breaking the norms can lead to group censure and perhaps exclusion from the group. Intelligent and highly ethical people will often comply with group norms even if doing so demands from them behaviours they would normally avoid.

When group think is operating, a group colludes on a subconscious level to maintain the stability of the group and to avoid change. Invisible, subconscious, collusive forces dissuade group members from asking embarrassing questions, outshining each other, or “rocking the boat”. I think we would all agree that this is unlikely to lead to good corporate governance.

It takes skill and personal courage to challenge the rules or norms, stated or not stated, by which the group operates. Regardless of the level of personal discomfort, directors committed to sound corporate governance need to create group norms that foster problem solving, critical review, constructive feedback and honest, open discussion.

In my experience good corporate governance requires directors who are skilled at recognising and dealing with human behavioural systems and who provide leadership in embracing norms that make it safe for directors to use people skills and intuition when dealing with social systems and their intangible elements.
Developing a healthy functioning board culture takes effort, skill, time, and commitment – in other words; leadership. Some of the practical things steps that can help create this type of culture include:

- Working out what kind of board culture you want.
- Assessing the current board culture and your progress over time, seeing outside assistance if necessary.
- Including building a healthy, functioning culture as an ongoing board agenda item, even if some directors think that the board culture needs no improvement.
- Developing norms to support good governance.

In his analysis of what makes of highly effective boards Jeffrey Sonnenfeld concluded that there are five behaviours that distinguish the best:

1. They create a climate of trust and candour
2. They foster a culture of open dissent
3. They use a fluid portfolio of roles
4. They ensure individual accountability
5. They evaluate performance.

In conclusion I believe that the secret to good governance in the NFP sector is not the rules and regulations or what the board says it is going to do, but what it does and how it does it. As some famous person once said, “it’s not rocket science – it’s much harder”.

Let me leave you with a question – what can you do to better engage in the human dimension to create governance behaviour that adds real value to the endeavours of the organisation?

References

- AICD. Boardrooms that work. A guide to Board Dynamics.