ACCA

POLICY PAPER

# Corporate Governance and Risk Management Agenda

## INTRODUCTION

This Agenda sets out the corporate governance and risk management principles and aims which inform and guide the work of ACCA's Corporate Governance and Risk Management Committee. The Agenda is designed to be applicable internationally so as to reflect the global reach of ACCA. It aims to provide the policy framework to be used by the Committee, and ACCA more generally, in:

- developing ACCA's specific policies on corporate governance and risk management for different sectors and regions
- enabling ACCA to respond coherently on corporate governance and risk management issues as they arise.

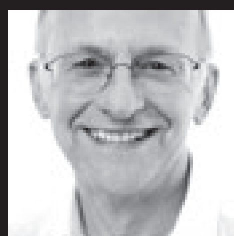
The Agenda is in three parts: Part A sets out ACCA's view of the purpose of corporate governance; Part B contains 10 principles which ACCA considers fundamental to all systems of corporate governance and risk management; and Part C sets out the Committee's aims for guiding ACCA's activity in these areas.

We see this document as being a statement of intent that will be refined and developed over time as knowledge and understanding improve generally. To this end, further research providing empirical evidence of best practice in corporate governance and risk management is needed. There is too little evidence to support many of the generally accepted tenets of corporate governance. These tenets should be questioned in an open and constructive manner and evidence sought to justify, improve or refute them.

The main body responsible for corporate governance within an organisation, can be known by a number of different labels: eg board, supervisory board, management board, council, authority, and committee. Similarly, the members of these bodies are also known by different labels: eg director, trustee, senior manager, member, governor and officer. In some organisations, more than one body shares responsibility for governance: eg large German listed companies have a supervisory board and a management board and UK Foundation Hospital Trusts have a board of governors and a board of directors. For consistency and simplicity, this Agenda refers to the bodies with responsibility for directing and controlling the organisation as 'boards' and members of these bodies as 'directors'.

**Professor Andrew Chambers**
Chair, ACCA Corporate Governance and
Risk Management Committee

**Richard Aitken Davies**
President, ACCA



This paper was commissioned by the ACCA Corporate Governance and Risk Management Committee, which exists to contribute to improving knowledge and practice in corporate governance and risk management, and to guide and shape ACCA's global strategies and policies in these areas. The Committee, chaired by Professor Andrew Chambers, comprises experts from business, the public sector, academia and ACCA Council.

For more on ACCA's work in this area visit **www.accaglobal.com/governance**

## A. THE PURPOSE OF CORPORATE GOVERNANCE

Fundamental to this Agenda is ACCA's view of the purpose of corporate governance. Our research suggests there is a divergence of view: some see corporate governance as improving effectiveness, some see it as protecting stakeholders while, unfortunately, a number regard corporate governance as a compliance exercise with little intrinsic value.

ACCA's view is that there are three complementary main purposes of corporate governance.

- To ensure the board, as representatives of the organisation's owners, protects resources and allocates them to make planned progress towards the organisation's defined purpose.
- To ensure those governing and managing an organisation account appropriately to its stakeholders.
- To ensure shareholders and, where appropriate, other stakeholders can and do hold boards to account.

We use the word 'appropriate' as clearly not all stakeholder groups have equal rights or responsibilities. These different rights and responsibilities will be addressed in ACCA's policy positions on specific sectors.

Although none of the above purposes refer explicitly to it, we regard effective risk management as fundamental to good corporate governance.

## B. ACCA'S CORPORATE GOVERNANCE AND RISK MANAGEMENT PRINCIPLES

The principles set out below are matters that ACCA believes are fundamental to all systems of corporate governance that aspire to being the benchmark of good practice. They are intended to be relevant to all sectors globally, and to any organisation having a significant degree of separation between ownership and control. Many of these principles are also relevant to organisations where ownership and control lie with the same people.

### 1. Boards, shareholders and stakeholders share a common understanding of the purpose and scope of corporate governance

There should be a clear understanding of what corporate governance is for. ACCA's view is stated in section A above.

### 2. Boards lead by example

Boards should set the right tone and behave accordingly, paying particular attention to ensuring the continuing ethical health of their organisations. Directors should regard one of their responsibilities as being guardians of the corporate conscience; non-executive directors should have a particular role in this respect. Boards should ensure they have appropriate procedures for monitoring their organisation's 'ethical health'.

### 3. Boards appropriately empower executive management and committees

Boards should set clear goals, accountabilities, appropriate structures and committees, delegated authorities and policies. They should provide sufficient resources to enable executive management to achieve the goals of the organisation through effective management of day-to-day operations, and monitor management's progress towards the achievement of these goals.

### 4. Boards ensure their strategy actively considers both risk and reward over time

All organisations face risk: success in achieving their strategic objectives will usually require understanding, accepting, managing and taking risks. Consideration of risk should therefore be a key part of strategy formulation. Risk management should be embedded within organisations so that risk is considered as part of decision making at all levels in the organisation. To avoid creating a risk averse culture, risk should be about both threats and opportunities. Boards need to understand the risks faced by the organisation, satisfy themselves that the level of risk is acceptable and challenge executive management when appropriate.

### 5. Boards are balanced

Boards should include both outside non-executive and executive members in the governance of organisations. Outside members should challenge the executives but in a supportive way. No single individual should be able to dominate decision making. It follows that the board should work as a team with outside members contributing to strategy rather than simply having a monitoring or policing role. Boards need to comprise of members who possess skills and experience appropriate for the organisation. All board members should endeavour to acquire a level of understanding of financial matters that will enable them to participate in decisions regarding the financial direction and control of the organisation.

### 6. Executive remuneration promotes organisational performance and is transparent

Remuneration arrangements should be aligned with individual performance in such a way as to promote organisational performance. Inappropriate arrangements, however, can promote perverse incentives that do not properly serve the organisation's shareholders or other principal stakeholders.

Disclosures of director and senior executive pay must be sufficiently transparent to enable shareholders or other principal stakeholders to be assured that arrangements are appropriate.

### 7. The organisation's risk management and control is objectively challenged, independently of line management

Internal and external audit are potentially important sources of objective assessment and assurance. Internal and external audit should be able to operate independently and objectively, free from management influence. Neither internal nor external auditors should subordinate their judgement on professional matters to that of anyone else. A key part of internal and external audit's scope should be assessment of the control environment including such aspects as culture and ethics.

Internal audit should be able to report directly to the board and should be properly resourced with staff of suitable calibre to work effectively at all levels of the organisation including the board.

### 8. Boards account to shareholders and, where appropriate, other stakeholders for their stewardship

In acting as good stewards, boards should work for the organisation's success. Boards should also appropriately prioritise and balance the interests of the organisation's different stakeholders. In a shareholder owned company, shareholder interests are paramount but their long term interests will be best served by considering the wider interests of society, the environment, employees and other stakeholders as well.

The type of organisation, its ownership structure and the culture within which it operates will determine how boards should account to their owners and/or significant stakeholders. No single model of accountability will be appropriate for all organisations in all regions. A universal requirement, however, is to disclose sufficient, appropriate, clear, balanced, reliable and timely financial and other information to those to whom boards should be accountable. Such information should cover the organisation's objectives, performance, prospects, risks, risk management strategy, internal control and governance practices.

### 9. Shareholders and other significant stakeholders hold boards to account

Owners and, in some cases, other significant stakeholders need to take an interest in the organisation and hold the board to account for its performance, behaviour and financial results. ACCA recognises that in many societies, the owners of organisations will have to take other stakeholder interests into account. As in Principle 8 above, the mechanisms required to enable this will depend upon the type of organisation, ownership structure and culture.

Toward this end, a fully independent external audit process, overseen by an effective audit committee, is an important component of good governance. The membership of audit committees should have sufficient financial literacy and at least one member should hold an appropriate accountancy qualification.

### 10. Corporate governance evolves and improves over time

Organisations in different sectors and across the world operate in diverse environments in terms of culture, regulation, legislation and enforcement. What is appropriate, in terms of governance, for one type of organisation will not be appropriate to all organisations.

A voluntary 'comply or explain' approach to governance, which allows organisations flexibility to innovate and improve as well as enabling stakeholder pressure to enforce good governance practice, is preferable to legislation providing it results in satisfactory standards of corporate governance. Legislation is rigid whereas more flexible systems allow innovation and improvement but at the risk of allowing poor practices to continue, particularly if Principle 9 cannot be upheld.

To assist innovation and improvement in corporate governance and in risk management, there should be flexibility in practices and structures. Corporate governance and risk management will never be fully evolved and may always be improved upon. It is important, therefore, that requirements do not create a straightjacket which prevents innovation and improvement in the ways organisations conduct themselves.

## C. AIMS OF THE CORPORATE GOVERNANCE AND RISK MANAGEMENT COMMITTEE

The ACCA Corporate Governance and Risk Management Committee's aims for its work on corporate governance and risk management are as follows.

1. To ensure that ACCA is a respected influence upon corporate governance and risk management developments in the UK, regionally and globally.
2. To ensure that ACCA influences UK and non UK legislators, regulators, investment fund providers and others so that corporate governance and risk management develops to best serve the emerging needs of society internationally.
3. To ensure that ACCA uses its influence to promote balanced, clear and understandable periodic reporting.
4. To ensure that ACCA is a significant player in appropriate harmonisation of corporate governance internationally.
5. To ensure that ACCA members have the encouragement and the means to be key players in corporate governance and risk management within their organisations and as representatives elsewhere.
6. To encourage the development of corporate governance and risk management best practice for entities beyond companies.
7. To promote the development of sector-specific guidance on corporate governance and risk management.
8. To work with others to promote the positioning of ACCA as a concerned party on corporate social responsibility issues.
9. To better define the boundaries and purposes of corporate governance and risk management.
10. To encourage the development of effective use of narrative reporting which is concise and readily understandable.
11. To contribute to the enhancement of internal audit's assurance and consulting roles with respect to corporate governance and risk management.
12. To encourage conceptual and empirical research in corporate governance and risk management and the development of innovative approaches.

## ABOUT ACCA

ACCA (the Association of Chartered Certified Accountants) is the global body for professional accountants. We aim to offer business-relevant, first-choice qualifications to people of application, ability and ambition around the world who seek a rewarding career in accountancy, finance and management.

We support our 122,000 members and 325,000 students throughout their careers, providing services through a network of 80 offices and centres. Our global infrastructure means that exams and support are delivered – and reputation and influence developed – at a local level, directly benefiting stakeholders wherever they are based, or plan to move to, in pursuit of new career opportunities. Our focus is on professional values, ethics, and governance, and we deliver value-added services through our global accountancy partnerships, working closely with multinational and small entities to promote global standards and support.

We use our expertise and experience to work with governments, donor agencies and professional bodies to develop the global accountancy profession and to advance the public interest.

Our reputation is grounded in over 100 years of providing world-class accounting and finance qualifications. We champion opportunity, diversity and integrity, and our long traditions are complemented by modern thinking, backed by a diverse, global membership. By promoting our global standards, and supporting our members wherever they work, we aim to meet the current and future needs of international business.

## CONTACT

For more information, please contact:

**Paul Moxey**, head of corporate governance and risk management, ACCA

+44 (0)20 7059 5794

paul.moxey@accaglobal.com

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