ARTICLE

Setting the right foundation

Good governance forms the building blocks to a better future

In the final part of the series, FTI Consulting considers the "G" of ESG and the role governance has to play for management teams, as the cornerstone of business longevity and sustainability.

Whilst environmental and societal best practice will form the pillars supporting sustainable business growth, corporate governance will be the foundation on which such growth is built and realised.

Governments, economies and industries around the world are now tasked with putting the right strategies in place to manage the transition to life in the pandemic. The ability for any organisation to adapt, stay resilient and remain successful will only be as strong as the governing principles and structures guiding them through the transition. As Boards and management teams consider survival post pandemic, they must first ask themselves whether they have the right governance framework in place to enable them to do so.

There has been intense media scrutiny surrounding management decision making – from over-boarding and share buy-backs, to dividend repayments and executive remuneration. For those Boards grappling with these issues right now, some will be more advanced in their response, some will be lagging behind, and others will be in a state of flux as they continue to iterate their approach. However, what is common for all Boards and management teams is the need for all plans, policies and business decision making to be underpinned by strong governance.

Below we offer a broad view of some of the factors at play, highlighting some key considerations for organisations to think about when looking at their governance frameworks.

An effective corporate governance structure will ensure that a Board of Directors understands its individual responsibilities and, via regular meetings, oversee the running of the business whilst ensuring it adheres to a stringent risk management framework. This is supported by a dedicated person, usually a Company Secretary or a legal and compliance representative, who will ensure that all Board protocols are adhered to and that the business is compliant with all relevant jurisdiction rules and regulations, and that all necessary filings have been made to the appropriate authority.

It is the Board's duty to work closely with the management team, provide guidance where needed, and that appropriate decisions are made to ensure the smooth day to day running of the business. The Board is also held accountable by shareholders and a range of stakeholders, which will include regulators for listed businesses, to ensure that the decisions made – as best possible – maintain the best interests of all stakeholders.

Non-executive Board members have a strategic role to play as they help to ensure impartiality and offer an objective perspective on any business decisions or corporate policies. These non-executive Board members therefore bring very valuable insights in terms of ensuring the long-term objectives of the company remain constant whilst providing independent counsel on how strategy or business decisions are likely to impact the company's stakeholders.

Strong corporate governance structures are often recognised by financial markets and investors and rewarded with improved access to capital at a lower cost than organisations with weak governance structures.

With the onset of the COVID-19 pandemic and the subsequent economic downturn, Boards will need to be robust, astute and agile with the appropriate skill sets and expertise in place to address a range of pressing issues. We have seen growing scrutiny around over-boarding, the withdrawal of dividend repayments, rising share buy-backs and executive remuneration. Not to mention new financial reporting metrics (EBITDAC), protocols for raising capital and communicating guidance to the markets.

This scrutiny will not subside anytime soon. With this in mind, Boards will also need the ability to 'deep dive' into their company's financials via in-depth discussion with management teams to fully understand the financial impact of COVID-19 for the short, medium and longer term. Clarity will be needed on pipeline, revenue forecasts and cash balances, and debt obligations. Similarly, strategies will be needed to address any financial challenges which may arise such as the requirement for a cost reduction programme or a debt restructuring. The Boards of listed businesses will also need to assess whether they are making suitably comprehensive public disclosures about the impact of COVID-19 on their business and financial position. In addition, there are numerous financial calendar activities, such as AGMs, financial results and investor roadshows, which will need to be managed in a new way during the COVID-19 era.

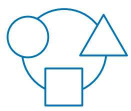
Aligned to this, Boards working closely with their management teams, will also need rolling COVID-19 risk assessment audits for their businesses to identify potential issues or crises, and to ensure there are appropriate structures and mechanisms in place to manage such situations. In effect, these are the building blocks for solid business continuity planning. As part of this, Boards will need to be up to speed in terms of advising on staff deployment levels, team structures, IT requirements to support working from home and the potential business implication of supply chain disruption and the knock on effect on clients' orders, as well as potential business contracts.

One more key component – one which will colour all the above elements – is communications. Any Board will need to oversee a communications strategy which will need to target both internal and external stakeholders. These include (though are not limited to) staff, suppliers, partners, clients, customers, media, regulators and investors – whether private or public, institutional or retail. All communications will need to be bespoke for each stakeholder group, with clear and consistent messaging to ensure key stakeholders can be confident that the appropriate business decisions are being made.

The Board of Directors and the corporate governance structures within which they operate, therefore play a significant role in the resilience, efficacy and financial health of business decision making. The Board, as the key agent of a company's governance framework, needs to engage with management to provide clarity on strategic purpose. Developing and setting a clear strategy, and then implementing it effectively, are vital to any organisation's success.

So what does a good corporate governance structure look like?

This will vary between publicly listed and private businesses. Below is not an exhaustive list, rather six key considerations:



Diversity: Create a Board which is balanced, diverse and has the appropriate qualifications, skillsets and industry experience. The Board should also be reviewed on a regular basis to ensure the appropriate directors/non-executive directors with the necessary experience are in place to support the company as it evolves.

Accountability: Develop a robust monitoring framework which assesses the roles and responsibilities both for the Board as well as key management with clear guidance on accountability. This regular review should also be used as an opportunity to assess the Board's performance and make improvements as and where needed. A benchmark to keep honest and accountable on progress.

Foresight: Ensure effective risk management protocols are in place and that clear 'red flag' reporting frameworks are institutionalised and regularly tested for effectiveness. Added to this a business continuity plan should be in place in case of crisis with a supporting communication strategy for both internal and external communications.

Safeguarding: Corporate reporting should be regular, accurate and safeguarded by external audits of the business. Providing transparency to key stakeholders through both the peaks and dips of a company's financial performance promotes stakeholders' confidence in the business. Full disclosures around related parties' transactions and director's other interests is also essential for complete transparency and trust and avoids any potential conflicts with a director's external financial interests.

Equality: All shareholders should be treated equally with their rights respected and ethical behaviours should be institutionalised and dealt with accordingly when found to be lacking.

Long-term approach: Performance metrics should be focused on long term value creation as opposed to short term gains.

In summary, businesses which view corporate governance as strategically important, and prioritise it as integral to their business operations, will best prepare themselves for future stability. Employing strong corporate governance protocols and setting the right foundation in place will enable organisations to set themselves up for long term prosperity. They will benefit from greater operational strength, increased transparency and more fluid decision making, in line with the needs of their stakeholders of today and tomorrow. Less robust governance structures frequently result in cultures that are both reactive and prone to short-termism where avoidable risks arise.

Governance is not simply a facet of business operations or management considerations which will ebb and flow, rather, it will be the de facto barometer for business health, purpose and success long term.

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