



The importance of governance in an IPO

‘Corporate governance is also moving away from a tick box exercise which companies endure because they have to. Done well, corporate governance provides companies with an opportunity to add real value to the business, connecting shareholders, boards and management, as well as improving decision-making and reporting.’

Maddie Scrafton

Disaster in the boardroom

‘The message from studying all of these scandals is that boardroom disasters will stop only when every director is trying to “do the right thing for the right reason”. No amount of official rules and sanctions will persuade directors, so regulators, shareholders, employees, and citizens all have a role to play in supporting this goal.’

Gerry Brown and Dr Randall S Peterson

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Disaster in the boardroom

Gerry Brown and **Dr Randall S Peterson** share the highlights of the research they have recently conducted into why boardroom disasters happen and what steps could be taken to mitigate them.

Like death, taxes and the poor, it seems business scandals are inevitable. If noticed at all, most people glance at the headlines but either think little further of it or else don't bother to realise the full extent of the impact upon their lives. Even those whose actual job it is to run, regulate, comment on or understand these numerous business scandals and failures are empowered to do so ONLY after the car has crashed! The predictable aftermath each time sees greater safety requirements, guard rails and crash barriers that address that specific problem just experienced but fail to fully understand and predict the disasters of tomorrow. This failure to address the root causes of the crash is not limited by geography, culture, sector or industry as, despite best intentions, business accidents continue to happen with alarmingly regularity – often at an increasingly dizzying pace.

'These scandals run the gamut from simple theft, fraud, and sexual harassment to the latest data driven environmental, health and safety, and privacy abuses.'

The relentless weekly parade of business failures – worldwide – has so inured us all to business scandals being an ostensible fact of life as the required price we all pay for the systemic wealth creation they offer in return. But what if there was a way to separate the wheat from the chaff? A way to properly see and understand the fundamental drivers and deep-seated causes of all of these business mis-steps and scandals? Researching and deep-diving business scandals worldwide and across the ages, Gerry Brown and Randall S Peterson have developed an innovative but robust metric that identifies, sorts and explains the underlying causes of these scandals.

These scandals run the gamut from simple theft, fraud, and sexual harassment to the latest data driven environmental, health and safety, and privacy abuses. Such scandals happen across all geographies and all times; indeed, no business sector is ever immune. These almost ubiquitous disasters have obvious negative impacts upon shareholders, staff and customers, but also result in disastrous – sometimes recognised, sadly too often not – wider consequences for society. Our book *Disaster in the Boardroom* shines a light on this crucial but rarely properly examined social space and also what is truly needed to improve boardroom culture and promote better director behaviour. We do so by focusing on the underlying psychological causes of board ineffectiveness, and from this analysis provides a range of recommendations for boards, regulators, investors, customers and governments.

The evidence suggests that the governance codes in countries where governance is taken seriously, like the UK, are necessary and do support effective governance. Our research and in-depth case studies (along with 300 years of business history) reveal that they are not sufficient to stop board disasters. This is NOT because the rules are bad or insufficient, but because we are dealing with issues of behaviours and culture that cannot really be directly legislated. Regulatory codes of conduct can only take us so far and, in fact, in most parts of the world have already largely addressed or ticked the existing boxes and necessary areas for compliance. Clearly a significant problem still remains. Indeed, beyond often-performative regulatory environments lies the hidden social and psychological structures that underlie the political power games of the board as both teams and individuals as well as how it approaches and fulfills its managerial and oversight responsibilities.

We tried to broaden our understanding of the drivers of business scandals and disasters to include the social and psychological space that directors also inhabit that, thereby, result in the six dysfunctions found in almost every boardroom, executive or elite team.

These are:

1. Subordination – lack of independence.
2. Imbalance – missing key voices (aka lack of diversity of background, specific required knowledge, etc affects decisions & actions).
3. Distension – the existing cultural intensifies so much that it becomes exaggerated and dysfunctional or misdirected.
4. Bystander – diffusion of responsibility (aka key players refuse to speak up or else point to everyone else about problems; no one take responsibility).
5. Bureaucratic – rule-bound cultures ignore and sideline alternative views, content or ideas.
6. Conformity – group think and identity threat causes elite teams to go along with others and to not raise legitimate concerns.

We believe this six dysfunctions framework is applicable to ANY group that makes consequential decisions. Groups that are making high stakes decisions, where they feel the stress of being responsible for the outcomes of their decisions, and where there are many stakeholders with interests in what the group is doing, all fall prey to these psychological blind spots and errors. All 'elite teams' share similar challenges: for example, to be representative of those they represent (ie, missing voices); or where culture can interfere with information sharing within the team and distort their decision-making.

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It is easy to find these boardroom dysfunction errors often cropping up elsewhere. Whether these debates are public – the UK or EU Parliaments, for example – or privately held behind closed doors – in American or Russian Presidential suites or UK Cabinet meetings, for example too – there is also always groupthink, bystander groups, diffusion or responsibility, rule bound cultures, lack of independence etc to hamper and distort effective decision-making despite everyone believing otherwise.

Finding out what has gone wrong is one thing but what are some of the authors key recommendations?

Ensure culture is a core activity of the board. Boards need to actively measure, question and interrogate their own culture as well as that of the organisation to search for existing (or emerging) evidence of any of the six dysfunctions. Many boardroom scandals and disasters could be avoided by planning for cultures that serve the entire organisation rather than enabling powerful sub-groups to conflict or allow dysfunction to run unchecked.

Director certification, education, and continuing professional development. Independent directors are assumed to be 100 per cent competent and qualified from the very moment they are appointed. Aside from our observation of the data revealing that this is simply untrue, this core but flawed assumption of common existing management practice and most of the literature and research has at least three interrelated and negative externalities:

1. It limits the diversity of background directors can have to a small talent pool of mostly former executives who are plausibly ready.
2. It encourages boards to be extremely conservative in who they appoint to directorships.
3. It is backward rather than forward looking so directors are not encouraged to engage in further development once appointed.

We believe that this is where most regulators have under-emphasised their direct role in building and maintaining boardroom culture. We recommend the compelling need for a system where we assume those appointed are not qualified, until they provide evidence otherwise of their experience. Or else gain certification via some kind of professional exam – much as lawyers, engineers and many charities boards use – along with the expectation of annual continuing professional

development as – again – many other better regulated professions require.

The message from studying all of these scandals is that boardroom disasters will stop only when every director is trying to ‘do the right thing for the right reason’. No amount of official rules and sanctions will persuade directors, so regulators, shareholders, employees, and citizens all have a role to play in supporting this goal. Regulators can encourage better director education, assessors can ensure that boards measure and discuss their culture, citizens should stop normalising business disasters, and so on. We all have a role to play in making these disasters a thing of the past.

We found that to really improve the cultural dimension of board effectiveness that there are a handful of strategies that have solid research backing as effective means for changing culture. These include measurement – there are effective measures to look at culture, such as whether it is competitive or co-operative along with being pre-emptive. Think about your culture BEFORE you engage organisational change, will it help or hurt this change? Obviously, we should continue to hold individual directors to account for their behaviour.

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Though no-one should need reminding that boardroom culture really matters, in a nutshell corporate governance is closely linked to culture which is about what you want to do and how you want to do it. You cannot legislate to ‘do the right thing for the right reason’. You can try, but what is right for you is not right for me; what is right in one situation is not right in another; what employees value in my business might very well be different in your business. And yet when I ask you whether your board does the right thing for the right reason you probably know exactly what that means for your business ... that is culture. It tells us what is important and valuable. We shouldn’t need reminding that corporate disasters and scandals are symptoms of a deeper cultural dysfunction that oftentimes has its roots at the board level or, at the very least, are the responsibility of the board. Board dysfunctions do not appear from nowhere. They evolve out of weak, poorly defined cultures where board members do not actively engage to shape the culture of their board and organisation.

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Designed and printed by WithPrint
Riverside Studio, Gills Lane, Rooksbridge, Somerset, BS26 2TY
www.with-print.co.uk

ISSN 1358-5142

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