THE QUALITY OF CORPORATE GOVERNANCE

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ABSTRACT

The corporatist governing is the system based on which institutions are ruled and controlled. The corporatist administration implies a set of relations between the leaders of an institution, the unions and the economic agents. The corporatist administration also offers the structure according to which the goals of the institution are established, as well as the means to reach those goals and to monitor the gained performances. A good corporatist administration should offer the motivation to achieve the goals which are in the best interest of the institution and the tax payers and should also facilitate an efficient monitoring, thus encouraging the institutions to use the resources sufficiently.

The transparency and permanent informing are the main issues when talking about a real corporatist administration. These allow the unions as well as economic agents to assess the performances of the management with influence over their behaviour. Moreover, the information systems can form managers which will have access to more means so as to rule more efficiently. Last but not least, the transparency and providing information offer the tax payers the opportunity to understand the structure of the institution, its activities and policies so that he can understand the performances and ethical standards on which it is based.

Keywords: *corporate governance, internal audit, development, decisions, performance, management.*

1. INTRODUCTION

The quality of corporate governance is often reflected in the quality of decision making. Public sector bodies must combine reliable information produced by 'hard' systems and processes with the 'softer' issues of openness and integrity to inform their judgment on key decisions. The more open and honest organizations are with themselves about their performance, the more open and honest they can be with service users and the public. This honesty is the foundation for deciding appropriate action to remedy poor performance. Better quality services are then more likely; improved performance and being more open will increase public trust.

The next chapter looks at the quality of some of these aspects of corporate governance across the public sector and at the particular constraints and opportunities that different public bodies face when seeking to improve them.

2. INTERNAL AUDIT AND CORPORATE GOVERNANCE

Standard 2130 - Governance provides:

The internal audit activity must assess and make appropriate recommendations for improving the governance process to achieve the following objectives:

- ♣ Promoting ethical values appropriate to the entity;
- ♣ Ensuring accountability and the effective functioning of the management entity;
- ♣ Effective communication of risk and control information appropriate structures within the entity;
- ♣ Effective coordination of activities and communication of information among management, internal and external auditors and the Council.

2130.A1 - The internal audit activity must evaluate the design, implementation and effectiveness objectives, programs and activities related to ethics entity.

2130.C1 - Consulting engagement objectives must correspond to the values and objectives of the entity.

Internal audit has become increasingly important over the years, and both widening scope and coverage of auditable activities. Interest throughout the world for government in the past 25 years, fueled power internal audit.

Lately, internal audit has evolved a lot because the concept of corporate governance, which influenced and accountable in greater management assessment and risk management.

Internal audit will inevitably be under pressure, since it is the function that can bring an extra transparency. The presence of the internal auditor in this context answer both " corporate governance principles " of all transactions to ensure transparency and management need to bring extra security to allow him to have the courage to implement the strategy of the organization into practice correctly and effective.

Responsible for organizing and implementing internal control system is line management.

Governance is the term used to describe the role of persons entrusted with the supervision, control and management of an entity.

The entity must have a governance structure to enable the Board to exercise a judgment on objective public institutions, particularly independent management.

Structures of governance vary from country to country, cultural and legal reflecting:

- In some countries, a surveillance function and management function are legally separate into two separate bodies, such as a supervisory board (wholly or mainly non-executive) and a management board (the executive);
- In other countries, both functions (supervisory and management) is the legal responsibility of a single unitary council, although it may still be an audit

committee assists that board in its governance responsibilities, relating to financial reporting.

Those charged with governance are responsible for ensuring that the entity usually achieves its objectives regarding:
- Reliability of financial reporting;
- Effectiveness and efficiency of operations;
- Compliance with applicable laws;
- Reporting to stakeholders.

Audit matters of governance interest are those that arise from the audit of the financial statements and the auditor's opinion, are important to the relevant, those charged with governance in overseeing the financial reporting process and disclosure.

Such problems include:
- Uncertainties related to events or conditions that may cast significant doubt on the entity's ability to continue;
- Disagreement with management regarding certain matters, individually or together, may be important for the entity's financial statements or the auditor's report. These communications include specifications for solving or not solving the problem and its importance;
- Other matters warranting attention by those charged with governance, such as material weaknesses in internal control, questions regarding management integrity, and fraud involving management.

Essentially, internal audit can play two roles:

The first role is manifested in the early stages of introducing a sound system of governance, the internal audit is a great opportunity to advise and strengthen leadership in the advantages of introducing best practices and to support its efforts in introducing policies, mechanisms and procedures.

Internal audit can provide advice, training and facilitation. However, audits should assume an executive role in the design or implementation of policy governance - accountability must be clearly attributed to management. Internal audit must also ensure that it has engaged in reaching their own role in corporate governance, providing both assurance and consulting.

The second role internal audit plays when auditing the governance system under which provide assurance on the adequacy and effectiveness and make recommendations whenever necessary improvements in how the implementation or operation of the system. This will bring value not only improving the governance of the public entity, but also issuing a statement supporting sound on internal control in the annual report.

3. GOOD GOVERNANCE SUPPORTS EFFECTIVE DECISION MAKING

The development of a common understanding of corporate governance is generally agreed to have started with the Cadbury report, which identified the principles of good governance as integrity, openness and accountability. The report was the first of several on corporate governance in the private sector, the most recent contributions being the Higgs report on non-executive directors and the Smith report on audit committees. In the public sector, the Nolan Report was particularly important in setting out the principles of public fife. Appendix 2 contains a list of relevant reports on corporate governance.

The Audit Commission has developed its understanding and in this report defines corporate governance as:

The framework of accountability to users, stakeholders and the wider community, within which organizations take decisions, and lead and control their functions, to achieve their objectives.

Good corporate governance combines the ‘hard’ factors – robust systems and processes – with the ‘softer’ characteristics of effective leadership and high standards of behavior[1]. It incorporates both strong internal characteristics and the ability to scan and work effectively in the external environment. The internal combination of ‘hard’ and ‘soft’ characteristics involves:

- **Leadership** that establishes a vision for organizations, generates clarity about strategy and objectives, roles and responsibilities, and fosters professional relationships;
- **Culture** based on openness and honesty, in which decisions and behaviors can be challenged and accountability is clear;
- Supporting accountability through **systems and processes**, such as risk management, financial management, performance management and internal controls. They must be robust and produce reliable information to enable better decisions to be reached about what needs to be done in order to achieve objectives;
- **External focus** on the needs of service users and the public, reflecting diverse views in decision making, producing greater ownership among stakeholders and maintaining clarity of purpose[2].

Externally, an effective and **strategic regulatory regime** can promote better corporate governance, with appropriate targets and freedoms and flexibilities for organizations based on comprehensive information about their performance and capacity.

How well the internal characteristics are balanced is important: public sector organizations operate in complex legislative, political and local contexts, in which they have to make difficult decisions. Well – governed organizations balance their different responsibilities and use information to decide where to allocate effort and resources to meet competing demands. Good governance supports effective decision making; poor governance is often seen (in hindsight) as creating the climate, structures and processes that lead to poor decisions.

Decision making always involves risk, but this risk is reduced when an open culture exists in which challenge is accepted and supported. This challenge and openness must be underpinned by robust performance, financial and information management systems, the effective use of risk management and an accountability framework that is based on a clear communication and understanding across the organization of roles and responsibilities.

The importance of effective leadership in ensuring good governance is clear from inspection reports and from other reports generated across the public sector.

Ultimately, leaders are responsible for achieving the right balance of hard and soft factors and are accountable for the decisions they take, or fail to take. They set the strategy for organizations and give it a sense of direction and purpose. The relationships between those carrying out executive and non – executive roles are fundamental to setting the tone for the cultural aspects of organizations that can never be codified or set out in detailed guidance, but which are immediately recognizable to those who work in or deal with them.

The Audit Commission, in conjunction with the Improvement and Development Agency (I De A) is currently investigating the topic of leadership and will report later in 2003.

Increasingly, public sector services are delivered through contracts between public, private and voluntary sector organizations and through more informal collaborations with a range of partners across all sectors.

Organizations are unlikely to be able to ensure that partnership and contracts are effective unless their corporate governance is effective. How corporate governance affects the quality of partnership outcomes and how partnership affect organizations' own governance arrangements are both important issues that this report does not address in detail. The Audit Commission plans to carry out further work to specifically address the issues relating to governance of partnerships and multi – agency alliances[3].

In this report, the key governance roles are described in terms of the responsibilities of executive directors and non – executive directors (or N E Ds), following terminology used in the NHS and in the private sector. These terms are understood differently across public sector organizations, particularly in local government, reflecting the democratic foundations of local authorities.

To avoid confusion, the terms 'executive' or 'executive director' should be taken to mean the corporate management team in local authorities – that is, the chief executive and senior service directors. The term 'non - executive' or 'non – executive director' should be taken to mean those roles carried out by elected councilors. In policing, executives are the chief constable and his or her senior management team; the non – executive function is filled by members of the police authority. In probation, all board members except the chief officer are non – executives; the chief officer and his or her senior management team are the executives.

Organizations with good corporate governance have the capacity to maintain high – quality services and to deliver improvement. Poor corporate governance has contributed to serious service and financial failures. The growing debate about corporate social responsibility and corporate manslaughter bring this issue into stark perspective.

The quality of governance also affects levels of trust in public services:

"Trust is at the heart of the relationship berween citizens and government. It is particularly important in relation to services which influence life and liberty – health and policing. But it also matters for many other services – including social services and education. In these cases, even if formal service and outcome targets are met, a failure of trust will effectively destroy public value"[4].

Corporate failures in the private sector can have a catastrophic effect on public trust, leading to falls in share values, investor confidence and in the general public's trust in the stewardship and state of the economy. MORI's research for this study shows that public sector corporate failures also undermine trust. Nearly two – thirds of those asked (64 per cent) said that high – profile incidents, such as the death of Victoria Climbie or the Alder Hey organ retention scandal, had adversely affected their level of trust in public services.

Loss of trust will damage the Government's aim of modernizing public services. The public and service users can disengage, either by choosing other service options (where feasible), or by not wanting to participate in public service delivery. They might decide not to vote, fail to respond to consultation, or, more significantly, withhold information or participation that enables public services to be delivered effectively for the wider common good.

4. CONCLUSIONS

Trust in public bodies is principally affected by two things: the quality of services that individuals and their families receive; and how open and honest organizations are about their performance, including their willingness to admit to and learn from their mistakes. The public does not generally rate public bodies highly on the second of these attributes: only one in eight (13 per cent) believes that their local hospital, council or police service always admits when it makes a mistake; and only in four (22 per cent) believes that such organizations learn from the mistakes that they make.

Research for this study shows that public bodies fare badly on the 'negative' drivers of trust: having poor leaders and managers, and being uninterested in peoples' views.

Poor leadership and management is associated with poor communication, echoing research previously carried out for the Audit Commission that showed that the public believe: it is in the interest of the service provider to present figures and spending in a positive light.

5. REFERENCES

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