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CONCURRENT SESSIONS — **Tuesday 13:30 – 17:30**
KEMPINSKI HOTEL CORVINUS — **Erzsébet tér 7-8, Budapest V.**

SALON REGIOMONTANUS — **Tuesday 15:30 – 17:30**

15.2. CORPORATE SOCIAL RESPONSIBILITY AND SUSTAINABLE DEVELOPMENT I.

Session Chair: ***Györgyi Nyikos****, Ministry of National Development, Hungary*

15.30 The Requirement for Quality in Corporate Governance
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The Requirement for Quality in Corporate Governance

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Abstract

Performance distinctions between competing organizations begin with the strategic direction and policy formulation as established by the Board of Directors while an organization's capacity to sustain long-term success is established by management's ability to assure control using a disciplined approach to daily control based on Board guidance and advice. Recent developments over the past decades have had a sobering effect on Boards of Directors as they recognize their innate responsibility to assure quality of results in both strategic and operational dimensions of organizational performance. An emerging emphasis on quality has been elevated to the level of the Board of Directors as they are being increasingly held accountable for the quality of their organization's operating activities as well as its performance results. This paper briefly traces the development of this new perspective on quality at the level of the Board of Directors and presents an approach to conduct an internal assessment of the performance of a Board of Directors as developed by the International Academy for Quality.

Keywords: Corporate Governance, Board of Directors, Board Responsibility, Total Quality Management, Performance Measurement, Performance Assessment.

The Purpose of Corporate Governance

The first commercial organizations were trading partnerships established by the Phoenicians during a time where commerce most greatly relied on the favor of reigning monarchs. These early organizations (they were recorded as early as 3500 BC) were mostly short-term involving only a few individuals. Most of the wealth during this period lay in agriculture, rather than trade or manufacturing. Prior to 1500 AD the only organizational structure in business was the Guild which existed to develop a particular craft, establish the standards for quality, and protect the interests of the members, rather than organize their businesses.

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During the Imperialist period (1500-1750 AD) chartered companies were established to combine the efforts of government and merchants in exploiting the new world (e.g., the British East India Company and the Hudson Bay Company (established in the 1600s). These companies were structured in a two-tier system with a General Court which included all of the shareholders who had voting rights and a Court of Directors (24 individuals elected by the General Court who were supplemented by management staff and operating committees to run daily operations). The Court of Directors answered directly to the General Court; however, during this time partnerships were still the preferred organizational structure. Until about 1850 state-chartered companies were the only real alternative to partnerships; however limited liability corporations became a reality as France, Britain, and Sweden moved to create joint stock companies. This form of ownership was first experienced in the railroads but it became popular in America following the civil war – just in time to stimulate the industrial revolution with capital to fund expansion. (Micklethwait and Wooldridge, 2003)

Two court rulings in the early 1900s established the current responsibilities for the Board of Directors. In the English Court of Appeal the case Automatic Self-Cleansing Filter Syndicate Co. v. Cunningham [1906] 2 Ch 34 held that the division of powers between the board and shareholders depended upon the construction of the articles of association and that where decision rights and powers were vested in the board, that the general meeting of shareholders could not interfere as "the directors and the directors alone shall manage." Thus as long as the directors are operating within the context of the law then the affairs of the company are vested in them. In a second case, Shaw & Sons (Salford) Ltd. v. Shaw [1935] 2 KB 113 it was found that: "A company is an entity distinct alike from its shareholders and its directors. Some of its powers may, according to its articles, be exercised by directors; certain other powers may be reserved for the shareholders in general meeting. If powers of management are vested in the directors, they and they alone can exercise these powers. The only way in which the general body of shareholders can control the exercise of powers by the articles in the directors is by altering the articles, or, if opportunity arises under the articles, by refusing to re-elect the directors of whose actions they disapprove. They cannot themselves usurp the powers which by the articles are vested in the directors any more than the directors can usurp the powers vested by the articles in the general body of shareholders." Thus, a primary vehicle for control of directors is their election at the General Meeting of stockholders.

In order to continue as directors, individuals serving in this capacity are expected to act honestly and in good faith (bona fide) in representing the rights of shareholders. Also, they have a fiduciary duty, or a duty of faith, to represent the shareholders in matters of trust and confidence related to finance. Against this historical and legal background we must examine the development of management concepts related to the Board of Directors, Chief Executive Officer (CEO) and shareholders: this is the act of governance whereby one party (shareholders or Board of Directors) grants power to exercise authority or control to another party (Board of Directors or CEO) in return for the right to review and verify performance.

Responsibility for Governance

Chester I. Barnard first perceived of organizations as social systems, where authority is a characteristic of communication relative to the purpose of the organization. An organization's purpose is an executive function which gives meaning to the environment and serves as the organization's unifying principle within cooperative systems. Business policy is the choice and implementation of long-term purpose that affects everyone in the organization and governs how they act in response to the external environment.

Barnard observes that the forces that destabilize organizations are external: physical, social and biological forces which require internal adjustments to processes where the "survival of the organization depends upon the maintenance of an equilibrium of complex character in a continuing fluctuating environment." (Barnard, 1936, p. 6) Barnard speaks of individuals ***inside*** an organization as "participants in specific cooperative systems" so they "are regarded in their purely functional aspects, as phases of cooperation"

(Barnard, 1936, p. 16). This tends to de-personalize the characteristics of individuals and to cause them to be seen in a social situation which enables cooperation. However, ***outside*** a specific organization "a person is regarded as a unique individualization of physical, biological, and social factors, possessing in limited degree a power of choice" (Barnard, 1936, p. 16). This occurs to simultaneously.

For Barnard cooperation results in organizational effectiveness and efficiency and he defines these terms as follows: "we shall say that an action is ***effective*** if it accomplishes its specific objective aim. We shall also say it is ***efficient*** if it satisfies the motives of that aim, whether it is effective or not, and the process does not create offsetting dissatisfaction." (Barnard, 1936, p. 20) But, there are physical and biological limitations in the performance of cooperative systems which arise from the limitations to obtaining knowledge and which affect the way we can learn, know and execute decisions in an organization. Barnard observes that "what you are doing changes physical history, biological history, social history. None of these components can be abstracted from the event either in its origin, its process, or its effects and still leave the event. It is a whole system. It includes many parts that are unknown and for that reason not comprehended." "It is possible that all of the physical components are not known; it is certain that all of its biological components are not known; it is still more certain that all of its social components are not known. But it takes place nevertheless, and the conduct of men is affected thereby." (Barnard, 1936, p. 47) Thus, "we affect the whole through the part." (Barnard, 1936, p. 48)

For an organization to obtain profound knowledge necessary to support its decision-making, it is essential that it understand the limitations hat are placed upon it due to the sources of its knowledge which may be identified as a hierarchical taxonomy which creates its own interpretation problems due to the decreasing intangibility of data and the concomitant loss in confidence that occurs with this increase in uncertainty of the sources of knowledge (Barnard, 1936, pp. 46-61):

Table 1: Hierarchical Taxonomy of Knowledge Limitations

Type of Data	Explanation of Data	Nature of Data
Physical data	Continuous variables (engineering quality data)	Tangible
Biological data	Ergonomic data (time and motion)	Less Tangible
Process data	Timing and attribute data (pass/fail compared to criteria)	↓
Economic data	Approximations (estimates based on probability forecast)	More Intangible
Political data	Leadership and strength of relationship (fixed scale/rank)	
Social data	Interactions or relationship (group norm relativity)	↓
Moral data	Values or personal philosophy (individual relativity)	Intangible

For an organization to effectively plan to deliver a vision of the future state, it must gain knowledge of that potential state. However, this knowledge hierarchy shows that the most difficult kinds of learning are related to the lower types of data: political, social, and moral. This observation calls into question what policies should be used to guide leadership toward an effective allocation of the organization's resources in accomplishment of its strategic intent as these are precisely the issues that must be managed in order to achieve the objectives of good governance – an issue that we must investigate more thoroughly following the current discussion of the concepts of the responsibility for governance.

According to Barnard, leadership has two aspects: technical leadership and moral leadership. Technical leadership is: "local, individual, particular, ephemeral. It is the aspect of individual superiority – in physique, in skill, in technology, in perception, in knowledge, in memory, in imagination." It is "subject to specific development by conditioning, training, education; significant chiefly in conjunction with specific conditions; relative; rather easily determinable, comparatively objective; essential to positive action; commanding admiration, emulation." On the other hand moral leadership is "more general, more constant; the least subject to specific development; the more absolute, the subjective; that which reflects

the attitudes and ideals of society and its general institutions. It is the aspect of individual superiority in determination, persistence, endurance, courage; that which determines the ***quality*** of action; which often is most inferred from what is ***not*** done, from abstention; which commands respect, reverence. It is the aspect of leadership we commonly imply in the world 'responsibility,' the quality which gives dependability and determination to human conduct and foresight and ideality to its purpose." This aspect of leadership yields the highest expression of responsibility – "the power of a particular private code of morals to control the conduct of the individual in the presence of strong contrary desires or impulses." So, Barnard defines responsibility as an outcome of moral leadership: "the property of an individual by which whatever morality exists in him becomes effective in conduct." (Barnard, 1936, pp. 260, 263. 267)

Effective leadership of an organization requires as a foundation the relatively easier to develop "technical leadership" while requiring exemplary "moral leadership" to assure that the organization will endure. Thus, a Board of Directors must establish the moral framework for the organization: purpose and long-term vision or strategic direction.

Peter F. Drucker reinforced Barnard's definition by defining the reason for a business as to produce results. In fact Drucker prescribed that: "for full effectiveness all the work needs to be integrated into a unified ***program for performance***." (Drucker, 1964, p. 193) Drucker believed that this program should begin with the purpose of the organization and also include the objectives, plans, and policies that cause the organization to move in a strategic direction. It is essential that such a program for performance look well into the future. "The neglect of the future is only a symptom; the executive slights tomorrow because he cannot get ahead of today. That too is a symptom. The real disease is the absence of any foundation of knowledge and system for tackling the economic tasks in business. Before an executive can think of tackling the future, he must be able to dispose of the challenges of today in less time and with greater impact and permanence. For this he needs a systematic approach to today's job. There are three different dimensions to the economic task: (1) The present business must be made effective; (2) its potential must be identified and realized; (3) it must be made into a different business for a different future. All three have to be carried out with the same organization, the same resources of men, knowledge, and money, and in the same entrepreneurial process." (Drucker, 1964, p. 3)

Drucker's emphasis on results is the cornerstone of business: "Indeed, business can be defined as a process that converts an outside resource, namely knowledge, into outside results, namely economic value." (Drucker, 1964, p. 5) So, the production of results is a critical job of leadership. But, Drucker also warned: "Any leadership position is likely to be short-lived. This is nothing more than a restatement of Schumpeter's famous theorem that profits result only from the innovator's advantage and therefore disappear as soon as the innovation becomes routine." (Drucker, 1964, p. 7) Thus, he concluded that: "Economic results require that staff efforts be concentrated on the few activities that are capable of producing significant business results." (Drucker, 1964, p. 12)

Drucker focused on the need for effective executives – not merely delegation of tasks, but also a specific shaping of the work that they do into an effective use of resources. Effective executives manage their assignment of tasks well – not delegating their work to others, but fully getting rid of "anything that can be done by somebody else so that one does not have to delegate but can really get to one's own work – that is a major improvement in effectiveness." (Drucker, 1987, p. 38) If executives do work that can be done by others, then who will do the work of the executive? **Where is the line between the board and the chief executive?**

In his book ***Management Tasks, Responsibilities and Practices***, Peter Drucker described three functions that must be performed by a Board of Directors:

1. *The Board is a review organ to help management control itself*: "a group of experience people, people

of integrity, people of proven performance capacity and proven willingness to work who counsel, advise, and deliberate with top management." "Somebody has to make sure that top management thinks through what the company's business is and what it should be. Somebody has to make sure that objectives are being set and strategies are being developed. Somebody has to look critically at the planning of the company, its capital-investment policy, and its managed expenditures budget. Somebody has to monitor people decisions and organization problems and has to be the 'supreme court.' Somebody has to watch the organization's spirit, has to make sure that it succeeds in utilizing the strengths of people and in neutralizing their weaknesses, that it develops tomorrow's managers and that its rewards to managers, its management tools and management methods strengthen the organization and direct it toward objectives." (Drucker, 1974, p. 631)

2. *The Board is a disciplinary body to assure management effectiveness*: "An effective and functioning board is needed to remove a top management that fails to perform." (Drucker, 1974, p. 632)
3. *The Board is a representative of the organization's constituency to assure that the results the organization delivers are aligned with their expectations*: "The enterprise needs a 'public and community relations' organ. It needs easy and direct access to its various 'publics' and 'constituents.' It needs to hear from them and to be able to talk to them. The central fact is that the modern enterprise has a multiplicity of constituencies. The shareholders are one. But they are no longer **<u>the</u>** one, as traditional legal theory has it. The employees are clearly also such a constituency, but they are not, as the German trade unions (or the 'industrial community' laws in various Latin-American countries) assert **<u>the</u>** constituency. There are also the communities where a major company has its plants. There are consumers, suppliers, and distributors. All of them need to know what goes on in a major business, what its problems, its policies, and its plans are. The business needs to be understood by them. Top management needs even more, perhaps, to understand what these constituencies want, understand, misunderstand, see, question." (Drucker, 1974, p. 632-633) "The governing board of directors must be a board that represents the basic long-term interests of the enterprise. It must be capable of discharging its function as the review organ and as the supervisor of top-management performance." (Drucker, 1974, p. 267) [Note: The duties that are legally required of the members of the Board of Directors are owed to the company, and not to a specific constituency of the company (Baxt, 2007, p. 35)]

Drucker, in ***The Practice of Management***, distinguishes between the role of the CEO and that of the Board. "The chief executive's job is the biggest and the least explored area for the application of Scientific Management and especially of 'work simplification.'" (Drucker, 1954, p. 167) "What activities must the chief executive do himself? What activities can he leave to others – and to whom? Above all: what activities come first? How much time must be set aside for them no matter what 'crisis' pressures there are? (Drucker, 1954, p. 166-167) "The Board is an organ of review, of appraisal, of appeal. Only in crisis does it become an organ of action – and then only to remove existing executives that have failed, or to replace executives who have resigned retired, or died. Once the replacement has been made, the Board again becomes an organ of review." (Drucker, 1954, p. 179)

Drucker had a superficial approach to defining roles and responsibilities of the Board compared to that of Joseph M. Juran and J. Keith Louden. In his book ***Managerial Breakthrough***, Joseph M. Juran identifies the need for a "steering arm" in the organization that acts with "unity of purpose" based upon the new knowledge that it generates during diagnostics of the organization's performance (Juran, 1964 p. 75-154) At the apex of an organization, this is a role of the Board of Directors. Juran and Louden define three key activities of a Board of directors: (1) setting strategic direction for breakthrough (Juran and Louden, 1966, pp. 46-57) (2) policy formulation, and (3) assurance of control (Juran and Louden, 1966, pp. 130-153). Organizations must identify what they mean by long-term as this identifies the region of specific attention from a Board of Directors. Most organizations define short-term as a period that extends from the current date about three years and many define long-term.as beyond this period. However, some companies are known to have declared long-term as a planning horizon that is 10-25 years from the current date and they

may even distinguish what they focus on within this period (e.g., facility or real estate decisions are made on the 10-25 year horizon, while technology acquisition and partnerships are based on a 5-10 year horizon and new product development decisions are within the 5 year planning horizon). Policy formulation is the act of making explicit the "intent or direction based upon a philosophy or belief that serves to guide the actions of people within the company." (Juran and Louden, 1966, p. 52) "For all practical purposes the Board has no measurement machinery of its own." (Juran and Louden, 1966, p. 142) The Board must assure the integrity of the measurements provided by management and must also assure an independent auditor is used to evaluate from both internal and external perspectives (including the audit of the quality system and all other performance elements affecting materiality in an organization's performance results).

Typically, all the various constituencies of an organization are lumped together and called stakeholders. But, some stakeholders have a major financial stake in the company as well as a role in the company. In the case of effective Boards of Directors, Drucker notes that the most effective Boards had both of these components. (Drucker 1992) Thus, whenever the entrepreneurial role of the directors is weak, then the moral motivation toward responsibility of the directors may also suffer weakness. So, what does it take for an organization to have good governance?

Characterization of Good Governance

Some forms of organization are more challenged than others in their exercise of responsible leadership precisely because the "ownership" motivation is missing for the directors (e.g., for public organizations or in the case of outside directors who are financially independent). Here the need for good governance must rely more strongly on moral leadership. For example, in 1994 the United Kingdom Committee on Standards in Public Life identified a set of principles that currently represent the guidelines issued by the House of Commons for public sector organizations. These principles form the basis for development of more detailed codes of conduct within such organizations:

Table 2: The Seven Principles of Public Life [3]

Selflessness	Holders of public office should act solely in terms of the public interest. They should not do so in order to gain financial or other material benefits for themselves, their family, or their friends.
Integrity	Holders of public office should not place themselves under any financial or other obligation to outside individuals or organizations that might seek to influence them in the performance of their official duties.
Objectivity	In carrying out public business, including making public appointments, awarding contracts, or recommending individuals for rewards and benefits, holders of public office should make choices on merit.
Accountability	Holders of public office are accountable for their decisions and actions to the public and must submit themselves to whatever scrutiny is appropriate to their office.
Openness	Holders of public office should be as open as possible about all the decisions and actions that they take. They should give reasons for their decisions and restrict information only when the wider public interest clearly demands.
Honesty	Holders of public office have a duty to declare any private interests relating to their public duties and to take steps to resolve any conflicts arising in a way that protects the public interest.
Leadership	Holders of public office should promote and support these principles by leadership and example.

Behind this set of guidelines stand three related core principles of corporate governance: ownership, stewardship and accountability (Bertin and Watson, 2007, p. 25):

- ***Principle of Ownership*** – Ownership is more than financial, it is a principle that describes the way an

[3] Downloaded from: http://www.public-standards.gov.uk on 27 May 2011.

individual cares for a resource. Owners will establish a system of business control for preservation of capital and risk management methodologies for defining and operating with their personal comfort zone for potential loss of capital (or any owned asset) in order to achieve their desired level of return.

- ***Principle of Stewardship*** – Stewardship is a principle that directs a person to take responsibility for the management of resources that have been entrusted into their care by an owner. Corporate stewardship implies that the value of capital investments is preserved and enhanced by the actions of management. Stewardship impacts all business issues (e.g., social, health and environmental ramifications of the production methodologies as well as the use and eventual disposal of products). The primary roles in assuring stewardship in the life cycle of a product typically involve manufacturers, retailers, service providers, consumers and government. Stewardship acts on behalf of these participating communities to preserve value and exercise due diligence in the management of the organization's resources to achieve is purposeful ends.
- ***Principle of Accountability*** – Delegation of authority and resources from an owner to a designated steward brings accountability for how authority is used and how resources are deployed or consumed.

In a corporate governance structure, owners are the constituents (or stakeholders) while the CEO is the steward. The board of directors provides the mechanism by which owners delegate authority to the steward. How are these three principles integrated into a draft definition of 'good governance' that can be used in a corporate context for quality management? The Organization for Economic Co-operation and Development (OECD), a non-aligned, non-governmental organization that was initially established to help manage the Marshal Plan, has also produced a set of principles that should define good governance:

Table 3: OECD Corporate Governance Principles [4]

Principle	Brief Description
Ensuring the basis for an effective corporate governance framework	*The corporate governance framework should promote transparent and efficient markets, be consistent with the rule of law and clearly articulate the division of responsibilities among different supervisory, regulatory and enforcement authorities*
The rights of shareholders and key ownership functions	*The corporate governance framework should protect and facilitate the exercise of shareholders' right*
The equitable treatment of shareholders	*The corporate governance framework should ensure the equitable treatment of all shareholders, including minority and foreign shareholders. All shareholders should have the opportunity to obtain effective redress for violation of their rights*
The role of stakeholder in corporate governance	*The corporate governance framework should recognize the rights of stakeholders established by law or through mutual agreements and encourage active cooperation between corporations and stakeholders in creating wealth, jobs, and the sustainability of financially sound enterprises*
Disclosure and transparency	*The corporate governance framework should ensure that timely and accurate disclosure is made on all material matters regarding the corporation, including the financial situation, performance, ownership, and governance of the company*
The responsibilities of the board	*The corporate governance framework should ensure the strategic guidance of the company, the effective monitoring of management by the board, and the board's accountability to the company and the shareholders*

[4] Downloaded from: http://www.oecd.org on 27 May 2011.

Finally, the United Nations Economic and Social Commission for Asia and Pacific (UNESCAP) have also defined good governance. UESCAP begins by defining "governance" as "the process of decision-making and the process by which decisions are implemented or not implemented." The concept of good governance is appropriate for many of the institutions of society (including its commercial and business organizations) and is characterized as possessing eight attributes: it is participatory, consensus oriented, accountable, transparent, responsive, effective and efficient, equitable and inclusive and follows the rule of law (http://www.unescap.org/pdd/prs/ProjectActivities/Ongoing/gg/governance.asp).

The Meaning of Quality in Governance

However, quality in governance has to do more with two specific aspects: the process of governing and also the content or result of the governance outcome. In its previous work the International Academy for Quality (IAQ or Academy) has defined good governance as:

> "'Good governance' describes quality in terms of the response of the organization to its guiding principles and strategic direction: does it do what is right, reliable and responsible to assure the desired performance within a context of holistic oversight that is provided through the system of business controls? Good corporate governance must focus on ensuring that corporations take into account the interests of a wide range of constituencies (stakeholders such as customer-consumers, investor-owner-shareholders, employee-associates, legal-regulatory, and communities in which it operates) and that the board of directors is accountable to both the company and its constituents." (Bertin and Watson, 2007, p. 18)

Thus, "good governance" must specify both the targeted outcomes (results to be managed) as well as the process by which it will obtain these results (business operating methods). While the Board does not specify the specific content of the process, it should be held accountable to assure appropriate methods are used to determine "what and when" the organization will respond to the "why and how" of its policy. Perhaps the biggest implication of this observation is that any commitment towards improving the quality of management in an organization must include improving the quality of its moral leadership and this must begin with the Board itself and its establishment of the cultural foundation that is deployed as the spirit of the organization.

Emerging Interest in Governance Quality

Why has the interest in governance emerged? Over the past twenty years two periods of crisis have faced business – the first due to the ethical and moral shortcomings of Board of Directors and the second due to the emergence of the financial crisis. These issues have been written about extensively and have created the current focus on governance by a variety of organizations: United Nations, World Bank, Business Roundtable, Global Corporate Governance Forum (IFC), OECD, NACD, etc. However, we can draw some observations about what are the "forcing factors" behind this attention:

- The tendency to increase government regulations gradually becoming global
- More demanding consumers who expect higher levels of performance
- Global customers requesting global standards that include transparency and governance
- Investment, rating agency, and pension funds Governance requirements
- Due to the companies concentration in their core business there is a growing need to develop, integrate and motivate suppliers located around the globe
- Growing awareness of the need for companies to have sound social responsibility programs
- The need of companies to align the interests of all constituents to assure the necessary well-

motivated diversity that is essential for innovation, growth and profitability

IAQ Governance Quality Initiative

The Academy was established in 1966 as a cooperative effort among the American Society for Quality (ASQ), the European Organization for Quality (EOQ) and the Union of Japanese Scientists and Engineers (JUSE). The original purpose of the IAQ was three-fold: to coordinate attention to technical problems in quality; assure the broad dissemination of the results of such work to the greatest benefit of those concerned; and promote recognition of the role and importance of quality in other disciplines as a concept and as a decisive factor in stimulating success in all disciplines. Today, the Academy carries out its work through dedicated quality improvement projects, Think Tanks focused on specific quality improvement initiatives, as well as the individual contributions of its members.

The development of the Governance Quality Think Tanks is a good illustration of how IAQ operates. It was the insight of one academician that initiated this effort after several years of individual research and personal effort. In 1996, Academician Bertin delivered the first paper that identified quality in governance as an issue that should be pursued (Bertin, 1996). Subsequent to this speech he continued his research and in 2002 the Academy initiated a project to investigate this subject which resulted in the publication of a research report on governance quality (Bertin, 2005) which was later turned into a book that was endorsed by the Global Corporate Governance Forum and the Governance practice of PriceWaterhouseCoopers (Bertin and Watson, 2007). In 2009, the Academy established the Governance Quality Think Tank, lead by Academician Bertin to increase its activities in this area. In recognition of his pioneering work in this area, the "Marcos E. J. Bertin Corporate Governance Quality Medal" was established by the Academy in 2008. This medal is awarded in two categories: one to a practitioner of governance quality (e.g., the chairman of the board of a company) and the second to an individual who has advanced the governance quality body of knowledge. Perhaps the most important development of the IAQ Think Tank has been the development of a methodology for evaluating board performance by Academician Bertin with fellow Argentinian Academician Hugo Ricardo Strachan. This method will be described in the next section of this paper.

IAQ Method for Evaluating Board Performance

Academicians of the IAQ developed a matrix that may be used to evaluate the performance of a Board of Directors. The matrix has two dimensions: assessment categories and four levels of performance maturity that are used to assess the current state of performance for these categories. The assessment categories are:

- Mission and Principles
- Board Structure
- Board Operating procedures
- Board and Management
- Board and Shareholders
- Board and Community
- Board Contributions

Each of these categories is operationally defined by using four levels of maturity that are anchored by specific examples to describe levels of practice in each of the categories. Each category is scored with the following grading scheme to indicate the degree of maturity achieved by the organization:

- Level 1: Understanding (qualification: 0-1)

Board understands the need to improve Corporate Governance in the respective point or area.

- Level 2: First steps (qualification >1 to 3)
  Board has taken concrete steps towards establishing best practices in the respective point or area.
- Level 3: Implementation (qualification >3 to 7)
  Board has implemented improvements to Corporate Governance in the respective point or area.
- Level 4: Leadership (qualification >7 to 10)
  Board has reached the best achievable improvements to Corporate Governance in the industry for the respective point or area.

The relative value of each category is signified by a weight based upon the relative importance of its contribution of the categories to the results of the company (the sum of the weights is 100). Thus, when the point values are multiplied by the weighting the maximum total value that may be achieved on this assessment is 1000 points. The results are then displayed in an evaluation matrix (see table 4).

The Power Point version of this paper will describe in detail these seven assessment categories.

Table 4: Example of a Board Evaluation Matrix

BOARD EVALUATION MATRIX

LEVEL	Scores for LEVEL	Board Mission & Principles	Board Structure	Board Operating Procedures	Board & Management	Board & Shareholders	Board & Community	Board Contributions	TOTAL Evaluation (Max.1000)
1	0-1						1		
2	>1 to 3				3				
3	>3 to 7		7	6		5		6	
4	>7 to 10	10							
	Score	10	7	6	3	5	1	6	
	Factor	20	7	7	10	10	6	40	
	TOTAL	200	49	42	30	50	6	240	617

Current Issues in Performance Measurement of Corporate Governance

A follow-on development to this IAQ Assessment methodology is planned by developing a system for strategic performance measurement. In 2010 the NACD released a report on performance measurement for the Board of Directors (NACD, 2010). However, report presents a methodology that is biased toward factors that merely count activities rather than measure performance. Indeed, there is a general bias in the field of performance measurement based on the timeframe of the planning horizon. The NACD report is only a starting point in the conversation that Boards must engage in order to understand how to assure the integrity of their measurement systems. The Academy believes that it is important to develop a sound system of measurement for the Board that eliminates bias and is helpful for providing insight into the way that the organization is operating. For this reason the Academy's Corporate Governance Think Tank is working on this issue as a priority project for 2011.

Conclusion

The future investigations of the IAQ Governance Quality Think Tank will focus on three immediate projects: (1) Analysis of board constituent Issues applying the method of Quality Function Deployment (QFD); (2) Analysis of enterprise risk management and the suitability of quality methods for addressing the identification and specification of risks; and (3) development of a White Paper to address a general approach to performance measurement for application at the level of the Board of Directors.

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