

## **Contents:**

- **Definition of corporate governance**
- **Corporate Governance Theories**
- **Causes of corporate governance problems in co-operatives**
- **Why good Corporate Governance is necessary**
- **Basic tenets of good corporate governance**
- **Principles of good corporate governance**

## **Definition of corporate governance**

Cambridge dictionary defines corporate governance as “the way in which a [company](#) is [managed](#) by the [people](#) who are [working](#) at the [highest level](#) in it.”

Corporate governance essentially involves balancing the interests of the many stakeholders in an entity - these include its shareholders, management, customers, suppliers, financiers, government and the community. Since corporate governance also provides the framework for attaining an entity's objectives, it encompasses practically every sphere of management, from action plans and internal controls to performance measurement and corporate disclosure.

Co-operatives are usually characterized by multiple objectives and are therefore different not only in their organizational forms but also in terms of products, methodologies, social priorities and profit seeking behavior.

## **Corporate Governance Theories**

### **Agency Theory**

Principals (members) delegate the running of business to the management board which in turn hire and delegate authority to the managers.

In agency theory, the agent may succumb to self-interest, opportunistic behavior and falling short of the agreement between the interest of the principal and the agent's pursuits

### **Stewardship Theory**

The stewardship perspective suggests that stewards are satisfied and motivated when organizational success is attained.

In order to protect their reputations as decision makers in organizations, managers are inclined to operate the firm to maximize financial performance as well as shareholders' profits. In this sense, it is believed that the firm's performance can directly impact perceptions of their individual performance.

### **Stakeholder Theory**

A stakeholder can be defined as any group or individual who can affect or is affected by the achievement of the organization's objectives. Stakeholder theorists suggest that managers have a network of relationships to serve, which include the suppliers, employees and business partners.

## **Corporate Governance Theories .....continued**

### **Political Theory**

Political theory brings the approach of developing voting support from the members. Hence having a political influence in corporate governance may direct corporate governance within the Society. Loss of capable cooperative leaders and managers to the political arena worsens the situation. Every person of questionable motives, integrity and competencies who vie for Society leadership can invade the sector. In that way, floodgates for nepotism, corruption, mismanagement and financial indiscipline are opened. In consideration of devolved system of governance, some societies are sprouting in response to government promises of providing subsidized services to members.

### **Degeneration Thesis**

Within a society, there are pressures that are experienced as tensions of different kinds, e.g. over the extent to which surpluses should be retained or distributed to members, over whether OMOV should be upheld but with a restricted membership or modified but with an expanded membership i.e. to open the common bond, or over whether strict equality of members should be maintained or an element of hierarchy allowed. Attempts to resolve such tensions can lead to 'degeneration' hence the "degeneration thesis". Degeneration springs from two main sources: weak internal democracy, where the members are unable to hold the leadership/management to account or have too little stake in the society to influence decision-making processes; and abandoning the principle of member ownership and control (e.g. by allowing external investors to gain a foothold in the society). As the society develops, democracy becomes restricted to the management board and the gap between managers and members increases.

## **Causes of corporate governance problems in co-operatives**

Problems frequently occur in co-operatives due to one or more of the following reasons:

- a) Inadequate Managerial Competitiveness
- b) Failure Of Membership And Boards To Exercise Fiduciary Responsibility
- c) The Borrower Domination Problem
- d) Lack of Clear Rules, regulations and policies combined with Credit Rationing

### **Inadequate Managerial Competitiveness**

Managerial competence requires that management be competitively remunerated. Many co-operative members tend to have lower to moderate levels of income. Salaries that are competitive with those paid by other financial institutions are often criticized by members who compare society salaries to their own. This results in weak administration of the institution, morale problems, and the inability of the society to attract the quality of management that can produce strong results or resist the excessive interference of directors in operational decisions.

### **Failure Of Membership And Boards To Exercise Fiduciary Responsibility**

Members may be tempted to free-ride, that is let someone else monitor or influence the society especially large co-operatives. With limited overview or attention from the membership, the board, manager, and supervisory committee may collude to protect one another's interests at the expense of the institution. Managers may arrange for high salaries for themselves, while the board and supervisory committee members may obtain insider loans for themselves and their friends. This problem occurs particularly where internal as well as external (supervisory) controls are weak.

## **Causes of corporate governance problems in co-operatives.....continued**

### **The Borrower Domination Problem**

The combination of borrower-dominated societies operating in an environment that lacks clear governance rules provides a temptation for improper manipulation of the credit approval and granting process by directors.

### **Lack of Clear Rules, Combined with Credit Rationing**

Governance problems can become crucial when there is excessive and improper manipulation of the credit granting procedures by the board. Society members may actively seek election to the management board or credit committee by promising loans to friends and supporters after the election.

### **Why good Corporate Governance is necessary:**

- a) Attracts customers and investors and assure them that their savings/deposits/investments will be secure and efficiently managed, and in a transparent and accountable process.
- b) Create competitive and efficient business enterprises.
- c) Enhance the accountability and performance of those entrusted to manage entities.
- d) Promote efficient and effective use of limited resources. This in turn creates wealth and employment.
- e) Good corporate governance is a prerequisite for maximization of shareholder wealth.

### **Basic tenets of good corporate governance:**

- a) Accountability-leadership that must be ready to account.
- b) Efficiency and Effectiveness-leadership for results and getting priorities right
- c) Integrity and Fairness-leadership that is honest, faithful and diligent.
- d) Responsibility- leadership that is capable, responsible, representative and conscious of its obligations.
- e) Transparency- open leadership with accurate and timely disclosure of information relating to all economic and other activities of the society.

## **Principles of good corporate governance:**

- a) Authority and duties of members
- b) Leadership
- c) Co-opting of Directors
- d) Strategy and values
- e) Structure and Organization
- f) Corporate Performance, Viability and Financial Sustainability
- g) Corporate Compliance
- h) Corporate Communication
- i) Accountability to Members
- j) Responsibility to Stakeholders
- k) Balance of Powers on the Board
- l) Internal Control Procedures
- m) Assessment of Performance of the Board of Directors
- n) Induction, Development and Strengthening of Skills of Board Members
- o) Appointment and Development of Executive Management
- p) Adoption of Technology and Skills
- q) Management of Corporate Risk
- r) Corporate Culture
- s) Social and Environmental Responsibility
- t) Recognition and Utilization of Professional Skills and Competencies
- u) Recognition and Protection of Members' Rights and Obligations

## **Principles of good corporate governance...Continued**

### **Authority and Duties of Members [or Shareholders]**

Members or shareholders [as owners] of the society shall jointly and severally protect, preserve and actively exercise the supreme authority of the society in general meetings.

They have a duty, jointly and severally, to exercise that supreme authority of the society to:

- a) Ensure that only competent and reliable persons, who can add value, are elected to the Board
- b) Ensure that the Board is constantly held accountable and responsible for the efficient and effective governance of the society so as to achieve corporate objectives, prosperity and sustainability.
- c) Change the composition of a Board that does not perform to expectation or in accordance with the mandate of the society.

### **Leadership**

Every society should be headed by an effective Board that should exercise leadership, enterprise, integrity and judgment in directing the society so as to achieve continuing prosperity and to act in the best interest of the enterprise in a manner based on transparency, accountability and responsibility.

## **Principles of good corporate governance...Continued**

### **Co-opting of Directors**

Co-opting of Directors to the Board should be through a managed and effective process, ensure that a balanced mix of proficient individuals is made and that each of those co-opted is able to add value and bring independent judgment on the decision-making process.

### **Strategy and Values**

The Board of Directors should determine the purpose and values of the society, determine the strategy to achieve that purpose and implement its values in order to ensure that the society survives and thrives and that procedures and values that protect the assets and reputation of the society are put in place.

### **Structure and Organization**

The Board should ensure that a proper management structure [organization, systems and people] is in place and make sure that the structure functions to maintain corporate integrity, reputation and responsibility.

### **Corporate Performance, Viability and Financial Sustainability**

The Board should monitor and evaluate the implementation of strategies, policies and management performance criteria and the plans of the society. In addition, the Board should constantly review the viability and financial sustainability of the enterprise and must do so at least once every year.

## **Principles of good corporate governance...Continued**

### **Corporate Compliance**

The Board should ensure that the society complies with all relevant laws, regulations, governance practices, accounting and auditing standards.

### **Corporate Communication**

The Board should ensure that the society communicates with all its stakeholders effectively.

### **Accountability to Members**

The Board should serve the legitimate interests of all members and account to them fully.

### **Responsibility to Stakeholders**

The Board should identify the society's internal and external stakeholders; agree on a policy or policies determining how the society should relate to, and with them, in creating wealth, jobs and the sustainability of a financially sound society while ensuring that the rights of stakeholders (whether established by law or custom) are respected, recognized and protected.

### **Balance of Powers on the Board**

The Board should ensure that no one person or group of persons has unfettered power and that there is an appropriate balance of power on the Board so that it can exercise objective and independent judgment.

## **Principles of good corporate governance...Continued**

### **Internal Control Procedures**

The Board should regularly review systems, processes and procedures to ensure the effectiveness of its internal systems of control so that its decision-making capability and the accuracy of its reporting and financial results are maintained at the highest level at all times.

### **Assessment of Performance of the Board of Directors**

The Board should regularly assess its performance and effectiveness as a whole and that of individual members, including the Chief Executive Officer. A summary of the major findings together with a statement confirming that the Board has carried out a self-assessment exercise should be made to the annual general meeting.

### **Induction, Development and Strengthening of Skills of Board Members**

The Board should recognize the need for new members to be inducted into their roles and for all Board members to develop and strengthen their governance skills in light of technological developments, changing corporate environment and other variables. The Board should accordingly organize for the systematic induction and continuous development of its members.

### **Appointment and Development of Executive Management**

The Board should appoint the Chief Executive Officer and participate in the appointment of all senior management, ensure motivation and protection of intellectual capital crucial to the society, ensure that there is appropriate and adequate training for management and other employees and put in place a succession plan for senior management.

## **Principles of good corporate governance...Continued**

### **Adoption of Technology and Skills**

The Board must recognize that to survive and thrive it has to ensure that the technology, skills and systems used in the society are adequate to run the society and that the society constantly reviews and adopts the same in order to remain competitive.

### **Management of Corporate Risk**

The Board must identify key risk areas and key performance indicators of the society's business and constantly monitor these factors.

### **Corporate Culture**

The Board should define, promote and protect the corporate ethos, ethics and beliefs on which the society premises its policies, actions and behaviour in its relationships with all who deal with it.

### **Social and Environmental Responsibility**

The Board should recognize that it is in the enlightened self-interest of the society to operate within the mandate entrusted to it by society and shoulder its social responsibility. For this reason, a society does not fulfill its social responsibility by short-changing beneficiaries or customers, exploiting its labour, polluting the environment, failing to conserve resources, neglecting the needs of the local community, evading taxation or engaging in other anti-social practices.

## **Principles of good corporate governance...Continued**

### **Recognition and Utilization of Professional Skills and Competencies**

The Board should recognize and encourage professional development and, both collectively and individually, have the right to consult the society's professional advisers and, where necessary, seek independent professional advice at the society's expense in the furtherance of their duties as directors. [This is in addition to and not a substitute to their personal duty to acquire competence, training and information that would help them make informed, independent and astute decisions on issues relevant to the society.]

### **Recognition and Protection of Members' Rights and Obligations**

Members of the society have a right to receive any information that would materially affect their membership, participation in any meeting of members and participation in the election of directors and be facilitated to fully participate in all other resolutions of interest to them as members.

### **The attention of the Boards of Directors is increasingly being drawn to the need to ensure :**

- a) The governance framework takes account of gender and youths and the special needs of disabled and/or handicapped citizens.
- b) The society promotes the interests, rights and welfare of host communities.
- c) The society protects and preserves the environment.
- d) Adherence to prudential standards.

**END**

**THANK YOU**