

## Of Head Offices and Foot Soldiers

### Corporate Governance – Responsibility Rests at the Top



*Prof. Dr. jur. Monika Roth: „The attitude of management and functions are a reflection of the sanctions and control within the monitoring environment. This attitude can affect value creation.“*

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One of many descriptions of corporate governance goes as follows:

Corporate governance is the sum of shareholder-oriented principles that promote transparency and a balanced relation between leadership and supervision, while maintaining efficiency and decision-making capability at the highest corporate level. (Swiss Code of Best Practice).

While hardly a new topic, corporate governance has gained in importance since the accounting scandals and stock market slides between 2000 and 2002, which were followed by a wave of bankruptcies and a severe loss of confidence. These developments had their roots in conditions

that had been developing since 1980 and which were marked by a decline in ethical standards. This decline was evident in the total lack of self-restraint displayed by certain key figures.

Today, corruption, bribery, and corporate criminal liability are subjects of increasing public scrutiny, and official sanctions brand them as not merely improper but illegal. This change in perception signals the end of the days when “anything goes” for corporate management. Today, the quality of a corporate organization is directly linked to a meaningful ethics policy and the firm’s overall corporate governance.

A criminal investigation serves as a sword of Damocles, both encouraging and even forcing intrinsically less motivated companies or the individuals comprising them to address questions of leadership and organization, of rules of behavior, and

of supervision in a different way. In addition to compliance as a function and a behavioral concept, proof of compliance plays an important role, meaning that firms must document their efforts in this sphere.

The following discussion will concentrate on compliance as a behavioral concept rather than as a function. Such a behavioral concept is largely implemented from the top down and constitutes an important aspect of corporate governance. And for good reason: as the saying goes, a fish rots from the head first.

The behavioral concept may be described as follows:

- Laws, ordinances, regulations, circulars, professional codes of conduct and business principles that are or should be generally acknowledged must be complied with by the company as a whole, by management, and by all employees.
- Relationships with customers and other stakeholders should be characterized by ethical standards such as honesty, fairness, transparency, decency, and trust.
- Conflicts of interest should be avoided. If they cannot be, they must be disclosed to create transparency and facilitate a fair resolution.

This implies, among other things, that a comprehensive understanding of compliance goes beyond merely adherence to the letter of the law. The law undergirds integrity but does not define it completely; that takes more. Monitoring and supervision play an important role in this context. Clearly, it is preferable that the values of compliance are internalized, but a system of monitoring remains essential.

The monitoring environment, which encompasses the work environment as a whole, encompasses the attitude of management and top corporate officers and bodies toward monitoring and sanctions. This environment must be defined by integrity and ethical values, the distribution of authority and responsibility, personnel

and promotion policies, and professional expertise.

The attitude of management is a particularly important element in the monitoring environment. The key here is not a focus on apportioning liability, but concentration on the desired market success and the element of trust. The quality and timeliness of information, as well as a climate in which critical scrutiny is seen as creating value. These contribute to a well-functioning monitoring environment.

It is important that those with responsibility do not permit a “code of silence” to reign and allow “minor peccadilloes” to be swept under the rug. Problems must be addressed by asking the right questions. What this means may be illustrated by the role played by those team doctors in professional cycling who were responsible for illegally supplying athletes with performance-enhancing drugs.

“A doctor working with top athletes must answer two questions before dispensing medications or other substances: Are they illegal? And are they detrimental to the patient’s health? In practice, though, the problem has been formulated completely differently: Can the substances be discovered through doping tests? And can the risks be controlled with professional supervision?”

So top management individuals and bodies bear an especially great responsibility. It is their task to recognize and point out the organization’s strengths and its weaknesses. They should question and consciously shape their own role within the system while applying a healthy dose of self-reflection. They must live up to their function as role models and provide evidence that a companies’ daily operations reflect their values.

Without this individual and authentic role-model function, there can be no healthy, functioning monitoring environment. Instead, it will be precisely those employees

who abide by the rules who will feel duped, and lose faith in the organization.

The monitoring environment must also be defined by a “zero tolerance” policy toward rule violations. It should be communicated clearly and implemented without regard for rank or position. It should also be recognized that nonverbal communication by company leadership is very important. Nonverbal behavior, such as facial expressions and gestures, is largely involuntary. If the content of verbal pronouncements is perceived to conflict with the speaker’s tone and expressions, mistrust and exasperation result. The credibility of the messenger is impaired and, with it, the credibility of the message

<sup>1</sup> JÖRG HAHN, Radsportärzte, Frankfurter Allgemeine Sonntagszeitung, 27 May 2007, p. 10.

## **\*On this and other questions,**

see Monika Roth, Good Corporate Governance, Compliance als Bestandteil des internen Kontrollsystems, Dike Verlag, Zürich 2007 (ISBN 978-3-03751-035-0) ([www.dike.ch](http://www.dike.ch), and for other publications by this author: [www.roth-schwarz-roth.ch](http://www.roth-schwarz-roth.ch))

## Conclusions

In summary, firms must ensure that their internal operations adhere to certain essential maxims, without which the behavioral concept of compliance will not be able to meet the expectations it creates of good corporate leadership:

1. Standards must be formulated, communicated, and implemented. Either they will apply to everyone, or to no-one.
2. Monitoring and transparency must be ensured.
3. Sanctions must be implemented without regard to position; this practice must be universally known.
4. In public companies, the supervisory board must receive regular reports of any violations, as well as their consequences for individuals or organizational units.
5. Accountability extends to all within the company – there is no “inner circle” beyond reach of the rules.
6. There are no ends that can justify violations of the rules.
7. Successful avoidance of legal and/or moral imperatives is not a sign of special skill, and will never be rewarded.
8. Arrogance and self-satisfaction are not acceptable proof of correctness.
9. Management encourages open discussion and questioning, and creates procedures and institutions to ensure that criminal violations are quickly discovered (whistle blowing).
10. Criminal charges are preferred quickly and impartially, regardless of the rank of the perpetrator.