Corporate Governance:
light years behind accountability

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There is no doubt about it: corporate governance is *in*. It has become *the* most fashionable item in business during the last couple of years.

Corporate governance "garments" are flashed in the boardroom, displayed in corporate reports and have taken the top spot on the list of criteria that matter. As with all cleverly designed garments, they also conceal the nasty bulges and other indications that may otherwise show that all is not well. Embroidered cloths also cover the scars on boardroom tables; thick drapes hide cracks in the windows and conceal the ugly view of the reality behind the window panes.

Corporate governance is also big business. It seems more than just coincidence that those who contributed most towards its development, and those who are most actively promoting it, now also profit most from it. Corporate governance compliance audits and the subsequent reports have become a major product of the assurance industry.

Corporate governance has therefore become the darling of the accounting and auditing industry. In the syllabus of the South African Institute of Chartered Accountants, auditing has now become a subsection of corporate governance. Corporate governance is now mainstream. The *Companies Act* is "theory"; corporate governance is "practice". No-one in business likes to theorise. Academics do that. Business people are practical and so *King* takes centre stage.

Who cares what the *Companies Act* requires, as long as we can say we meet the King II requirements? And now II means being advanced – when compared to one. Two is better than one. The *Companies Act* traces its origin to 1973. No-one wants to be in 1973. This is the new millennium. Business is about relevance and today.

The Department of Auditing at the University of Pretoria, in cooperation with the business section of *Beeld* newspaper (*Sake-Beeld*), evaluates all financial advertisements that have to be published in terms of the JSE requirements. Month after month, the project leader reports: "A major shortcoming of these advertisements remains the fact that only a small percentage of companies state that they comply with the *Companies Act*."

When shareholders or other accountability structures call the company stewards to account, ask them probing questions, even in the face of a major corporate scandal it's become the accepted norm for stewards to parade their compliance with *King II* as justification and exoneration. Percentages are quoted: "We are 100% King compliant and we engaged a major international audit firm to verify this." "What more do you want us to do?"

But with *King* having been around for more than a decade (the first King report was published on 29 November 1994) and "110%" implemented, do we actually have Boards of Directors being more accountable; are shareholders better empowered to look behind the scenes and to judge if the stewards have acted responsibly? Is there less corporate fraud now, and management fraud in particular, than before? Are there today fewer cases of directors being paid what seems like unjustified amounts, and do the shareholders today have better information with which to assess such remuneration packages? The current debates, of which executive remuneration is but one, suggest a clear "no" answer.

Has the auditing "profession" under *King* gone from strength to strength? Are South African auditors widely recognised and applauded for their contributions to corporate accountability, or are our auditors today in a state of self confessed crisis?

Whether the architects of the King report did actually intend this to happen remains an open question. However, their persistence in ignoring well researched facts and calls from academia to entrench the audit function as a cornerstone of accountability, and to actually address the "adverse framework within which auditors operate", certainly suggests that they knew exactly what they did.

And this is still where one of the major flaws of the King report lies today. The King Committee missed a golden opportunity to reinstate the role of the auditor as watchdog for society. Instead, it presented the auditing industry with additional privileges which in turn promised additional exclusive business for audit firms. In 1995 the School of Accountancy at the University of Pretoria stated, in a Position Paper on the King report, that: "…the auditing industry may presume that the audit-related recommendations of the King report presents a propitious victory. As this paper has indicated we disagree and state that it adds to the predicament of a *trembling* profession, caught in the whirlpool of the fashionable "business Approach" to auditing and the inability to respond to basic consumer expectations.

Whilst, as the University of Pretoria researchers commented, the audit profession was "trembling" in 1994, it went on to shake a few years later, and then plunged to its biggest crisis ever. This crisis culminated in the Commission of Inquiry into the Affairs of the Masterbond Group of Companies and Investor Protection in South Africa, reporting to our country's President that the profession is "*dishonest and inefficient*". Hereafter the Minister of Finance promised a new Act for auditors, with its main objective to *restore* the public's confidence in auditors by introducing stringent requirements for the conduct and discipline of auditors. The once highly esteemed "profession" is now nervously awaiting the implementation new Act which will herald a process of reorganisation and a new start.

Although additional factors such as the defective process of audit standard setting and the controlling bodies bias towards the protection of vested interests (as opposed to the public interest), have also contributed towards the demise of the audit industry, the King report has undoubtedly contributed a major impetus towards degrading the audit watchdog into a purring lapdog. Whilst evidence from the biggest corporate failures screamed at the King Commission's Audit Task Force that auditors cannot provide non-audit services to the companies they audit without losing their independence, the King report did nothing to address this situation. Even after more damning evidence was

retrieved from the ashes of Enrons, WorldComs and our own LeasureNet like failures, all King II could come up with in this regard was to recommend:

- that the audit committee should set the principles for using auditors for non-audit work (it did not provide these principles – so anything goes);
- that a detailed description (and values) of non-audit services be provided in the annual financial statements; and
- that there should be separate disclosure of audit and non-audit services (no need for that – the Companies Act has required this since 1973).

The two main driving forces behind the King Committee are the Institute of Directors (IOD) and the South African Institute of Chartered Accountants (SAICA). Whilst, as the name suggests, the IOD consists exclusively of directors (the majority of whom are trained accountants), accountants (as opposed to auditors) also make up the majority of SAICA members. Now one thing should be clear: no director wants too much to do with an auditor with real teeth and a watchdog attitude. This could become very uncomfortable for directors and would actually empower the shareholders. From this perspective it may not seem too far fetched to suggest that the King requirements were designed to marginalise the audit function – like the garments mentioned above: something to show off with, but that also hides the real issues.

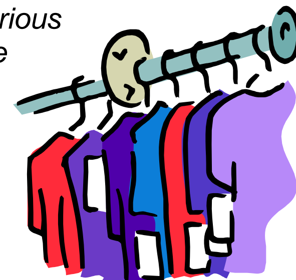
During a recent Company Secretary symposium, Judge Mervin King himself stated that the King report was never intended to become a "weapon of mass distraction" – distraction from the real accountability issues. But this scenario may compare well with the Camp Staaldraad fiasco of Springbok rugby coach Rudolph Straeuli. Of course, it was also never his intention to degrade SA Rugby and the players – but it was bound to happen – as he ignored warnings and well intended advice.

If you still have your doubts as to the issue at hand, (somewhere corporate governance is getting it all wrong) – the following case study (which has been simplified due to space constraints) may explain the problem better:

Have you ever experienced a similar situation?

You have been asked to serve on a committee that functions as part of the entity's corporate governance structures. You do not work for the company in question, but corporate governance principles recommend that a person from outside the company is appointed onto the committee.

Before a particular meeting, you receive an agenda setting out various matters that will be dealt with during that meeting. A perusal of the agenda shows that certain matters that you consider of vital importance in relation to the ones under discussion have not been listed on the agenda. At the previous meeting, the Chair promised that certain matters would appear on the next (this) meeting's agenda, but these have also not been included. You approach the Secretary and point out these omissions. You are



told that this will be given attention. Arriving at the scheduled meeting, however, the same original agenda is tabled. Your objections fall on deaf ears.

During the meeting you mention, at numerous occasions, that you would like your objection to certain matters to be minuted. When other matters are considered, and you try to contribute, the Chair does not allow you to do so, citing as reason that the discussion has carried on for long enough and that the meeting needs to "move on". After the meeting you receive the minutes and after reading them, you ask yourself if this was the same meeting that you attended. The minutes do not reflect the proceedings at all and more specifically, the matters that you asked to be minuted have not been included. Again, you approach the Secretary and point this out. You are told that this will receive his immediate attention. A few days after your visit to the Secretary, you receive a letter from the Secretary thanking you for your inputs to improve the minutes. The minutes are, however, never changed and are circulated to members and other stakeholders as is.

Let us subject the above case study to the typical corporate governance evaluation.

The above is a concise example and therefore only five corporate governance criteria apply.

- Agendas should be drawn up for every meeting
- Agendas should be distributed to all committee members before the meeting
- All items on the agenda should be dealt with during the meeting
- Minutes should be drawn up in respect of all meetings
- Minutes should be distributed to all committee members

After the evaluation, the corporate governance score card is completed as follows:

CORPORATE GOVERNANCE SCORE CARD **Governance aspect**	✓ or ✗
Agenda drawn up	✓
Agenda distributed *before* meeting	✓
All items on agenda dealt with	✓
Minutes drawn up	✓
Minutes distributed	✓
Final corporate governance score	100%

Based on the corporate governance score card, the organisation scores a cool 100%. In real corporate governance fashion, the management now asks a firm of auditors (preferably an major international firm) specialising in corporate governance matters to "audit" the above score card.

Not only do the auditors find the score sheet a true reflection of the reality, and the 100% score providing evidence of the entity's seriousness to implement important corporate governance principles, but they also point out that the written acknowledgement of inputs by the Secretary in fact exceeded best principles and were indeed praiseworthy (the score is actually 6 of out of 5 or 120%!). They also recommend that this practice be continued in spite of the obvious cost implications that it has. The audit firm furthermore offers to conduct a full corporate governance investigation and to recommend possible areas of improvement. This offer is accepted by management and the audit firm recommends, amongst others, that the company develops a manual that documents the procedures relating to the scheduling of meetings, starting with the drawing up of agendas, the distribution thereof, the minutes, etc. Such manuals, they recommend, could then be distributed to all members of the various committees to assist them in their participation.

"*Meeting, and in fact exceeding corporate governance principles are bound to be ultimately rewarded by the market and reflect in higher share prices and greater investment confidence*" the audit firm concludes in their corporate governance report.

When your complaints about the company being unaccountable, non-transparent, implementing unfair practices, etc. are leaked to the press and are raised at a shareholders' meeting, the Chair responds by pointing out that the entity had subjected itself to a voluntary corporate governance audit and reads the full corporate governance audit report to the shareholders present. This quickly settles the matter. As previously pointed out: a weapon of mass distraction…

Parallel to the corporate governance evaluation, a short but telling accountability score card was drawn up. Let's look at the results:

ACCOUNTABILITY SCORE CARD Aspect	✓ or ✗
Are the systems and structures open and transparent?	✗
Are the processes inclusive?	✗
Are the processes fair and equitable?	✗
Is the organisation accountable?	✗
Final accountability score	0%

The corporate governance fans will point out that the above exercise (of using a score card) degrades the concept and is therefore invalid or unacceptable. But you see, we also "downgraded" accountability to a score card and yet the results are profoundly different.

Be that as it may – high score or not – I would not invest my money in the company used in the above case study. Therefore if you ask me, I chosoe accountability anytime – all the time – because unlike corporate governance, accountability is in the heart…