



PRINCIPLES OF CORPORATE GOVERNANCE

ICAEW welcomes the opportunity to comment on the *Principles of Corporate Governance* consultation published by OECD on 14 November 2014, a copy of which is available from this [link](#).

This response of 2 January 2015 has been prepared on behalf of ICAEW by the Corporate Governance Committee whose members are drawn from the business and investment communities. The Committee informs our thought leadership and policy work on corporate governance issues and related submissions to regulators and other external bodies.

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MAJOR POINTS

The intended aim of the revision is unclear

1. The consultation consists of a marked-up draft of the existing Principles of Corporate Governance ('the Principles').
2. The cover page of the consultation simply states the rationale for the review as being to 'ensure the continuing high quality, relevance and usefulness of the Principles taking into account recent developments in the corporate sector and capital markets.' However, there is no explanatory introduction nor related consultation questions. It would have been helpful if the intended aim of the revision had been made clearer.
3. In particular, it is not clear what developments are regarded as fundamental and what changes are proposed in response. Better explanation of this aspect should be made before the Principles are finalised.

The revision process needs more transparency

4. We are aware that the OECD consulted selected stakeholders including business and investment communities as well as its members and non-members in preparing this draft. We also note that the draft is presented as a 'work in progress' prepared by the Secretariat of the OECD Corporate Governance Committee and the purpose of the consultation is to solicit input from business and labour representatives, civil society, and other interested stakeholders.
5. In order to satisfy this purpose, we believe that the consultation should have allowed a longer period than seven weeks, including two weeks of the festive period. Furthermore, more activities, such as outreach events, ought to have been organised in order to obtain genuinely informed, representative and useful feedback. It would be helpful also to have increased transparency over the revision process. As it is, it is not yet clear what perspectives have already been reflected and what additional perspectives the OECD seeks.

The Principles set the benchmark for a wide range of countries

6. The Principles should be as broadly applicable to diverse jurisdictions as possible. In our view, the current draft focuses too much on a legal, regulatory and institutional framework that is more relevant to jurisdictions that have some established corporate governance practice.
7. The assumption that there exists some understanding of both 'soft' and 'hard' regulatory mechanisms, such as capital markets supported by listing rules and the existence of active shareholders, in particular institutional shareholders, may not hold up well in the context of many jurisdictions both within and outside the OECD membership. We encourage the OECD to ensure that the Principles address this issue and enhance their applicability because they are used by major international bodies such as the Financial Stability Board and fund providers such as the World Bank and IMF.

What a corporate governance framework intends to achieve

8. One way of addressing the above issue may be for the Principles to stress what a corporate governance framework should achieve rather than what it should consist of. For example, the Principles recognise that the shapes and forms of a stock exchange can vary. If the Principles set out the effective distribution of resources as a key function of a stock exchange, the framework could focus simply on supervision, regulation and enforcement necessary for such a function. The applicability of the framework will increase as a result, regardless of the shapes and forms of individual stock exchanges, or even in jurisdictions where a stock exchange does not formally exist.
9. Corporate governance is a means to an end, and the end is to enable businesses to be run responsibly and successfully on a sustainable basis. Such businesses will operate better in a transparent, efficient and fair market and facilitate these characteristics of the market as a

whole. In a transparent, efficient and fair market, shareholders, among other stakeholders, are more likely to receive equitable treatment. The corporate governance framework should contribute to this mechanism.

10. What underlies good corporate governance is individual companies running their businesses to be successful sustainably, as markets and stakeholders expect them to be. Law, regulations and institutions should be in place only to facilitate this. The OECD should therefore explicitly recognise the fundamental objective of corporate governance and then define the role that law, regulations and institutions make accordingly. We set out such overarching principles of corporate governance in our paper entitled '[What are the overarching principles of corporate governance?](#)'

Frameworks alone would not achieve better practice in corporate governance

11. For businesses to embrace the benefits of good corporate governance, and for stakeholders including shareholders to participate in facilitating good corporate governance, there needs to be a degree of mutual trust. Stakeholders need to trust companies to demonstrate genuine commitment to good governance and companies need to trust that stakeholders will give them the license to operate as a reward for their behaviour. In our recent paper entitled '[When is comply or explain the right approach?](#)', we argued that the success of 'soft' approaches such as comply or explain depends on two conditions: shared beliefs and institutional arrangements as they are important in establishing mutual trust.
12. Shared beliefs about what constitutes good governance are essential as a basis of good conduct, supported by institutional arrangements including stock markets, patterns of ownership, the role of intermediaries, shareholder rights and engagement, legal and regulatory traditions, and the incentives that all these arrangements create. While important, without shared beliefs, institutional arrangements can become a mechanism achieving nothing more than a tick-box compliance exercise.
13. Currently the Principles appear to presume that shared beliefs exist, and concentrate on the institutional arrangements. In the wake of the global financial crisis where various aspects of corporate ethics and culture are challenged, it is important to rebuild shared beliefs about what good corporate governance means. We called for a wider debate on this in our latest paper entitled '[Who should be covered by codes?](#)'

The role of stakeholders is too narrow

14. We find the contributions of stakeholders defined in Section IV too narrow in the sense that they are primarily seen as a resource for building competitive and profitable companies. Today, stakeholders such as employees, suppliers, customers, and the media are considered to be contributing to the culture and reputation of businesses as well as acting as the gatekeepers of corporate governance. We believe that the Principles should recognise their broader contribution to corporate governance accordingly.