The Insider's View on Corporate Governance

The Role of the Company Secretary

Gertrud Erismann-Peyer, Ulrich Steger, and Oliver Salzmann

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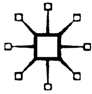

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List of Abbreviations

ADR	American Depositary Receipt
AGM	Annual General Meeting of Shareholders
BIS	Board Information System
CEO	Chief Executive Officer
CFO	Chief Financial Officer
CGO	Corporate Governance Officer
COO	Chief Operating Officer
HR	Human Resources
LSE	London Stock Exchange
NASDAQ	National Association of Securities Dealers Automated Quotations
NYSE	New York Stock Exchange
OECD	Organization for Economic Cooperation and Development
PLC/plc	Public Limited Company
Q&A	Questions & Answers
SEC	Securities and Exchange Commission (US)
SOX	Sarbanes-Oxley Act of 2002
SWX	Swiss Stock Exchange

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We hope that all find the results worthwhile.

Gertrud Erismann-Peyer, Ulrich Steger, and
Oliver Salzmann

Foreword

A book that claims to provide "The insider's view on corporate governance" is making an interesting promise. Who are these "insiders" and what do they tell us – board members, chairmen, CEOs, interested shareholders, and the public at large? As the subtitle of the book specifies: Company secretaries are providing their intimate view on what they are doing, how they are supporting boards at work, and how they are dealing with the increasing challenges of today's corporate governance requirements – requirements that are often driven by political and public pressure rather than by the real needs of the companies and their striving for success. The company secretaries are also talking about how they are trying to help internal and external board members in performing their roles better. And, last but not least, they talk about their dilemmas, their conflicts of interests and loyalties.

A great number of books have been published in the recent past about corporate governance, focusing on areas such as the roles and duties of the boards, the chairman and the CEO, and on board information, board conflicts, checks and balances, internal and external control, and board members' independence. Little research, however, has been done so far on those working with the boards behind the scenes – the people who quite often stay much longer in their function than the chairmen and the CEOs and often even longer than most of the board members.

This in-depth view on board practices in various jurisdictions, industries, and different types of companies allows for a number of interesting conclusions. Why do regulators and corporate governance organizations around the world put enormous emphasis on director's mostly very formally defined independence, whereas nobody seems to care that those supporting these "independent directors" are in no way independent of management? Why are a majority of company secretaries still reporting to the CEO, despite their important role of supporting the board and its work? And why – last but not least – does it seem typical that company secretaries in various jurisdictions have completely different roles and responsibilities, whereas boards are under pressure to become more and more uniform around the world?

Today's definition of "independence" for directors is clearly a result of the US system of a combined chairman-CEO role, whereas in a number of European countries these two top leadership positions have been

bestowed on two different people, thus providing an automatic separation of powers. And where the legal system even provides for two strictly separate boards, one supervising the other, supervisory board members' independence has a different quality. Because the CEO and other members of the executive management have no say in selecting the members of the supervisory body, directors can far more openly express their views, even if the CEO might not like them. In my view, being independent of the company is anyhow much less important than being independent of management and, even more so, having an independent mind. External directors, who know the business due to their former employment with the company can make independent judgments and take independent, well-informed decisions without having to fully rely on what management wants them to know. A strong character and the willingness to express independent views is thus much more important than formal independence qualification. In two-tier board structures, board performance could well be improved if directors, who due to their independent mind and their in-depth knowledge, were allowed to also assume important committee responsibilities even if they were not meeting all of the formal independence requirements. Companies, and first and foremost, all regulators and corporate governance activists, should rethink the real reasons behind the call for "independent boards," which are indeed well-functioning checks and balances through the separation of powers between different corporate bodies. Strict formal rules will not avoid future corporate scandals and failures if the people involved are not able to take decisions based on independent reflections. But inflexible rules, driven by form rather than substance, might hinder companies from achieving better performance.

What is now the role of the Company Secretary in this context? I am convinced that a strong personality, with the clear will to serve the company in its striving for excellence, can add much value. Yet it is crucial that the function becomes more and more independent of management. In my view, company secretaries – and even more so, the "corporate governance officers" as described in the book – should have a direct reporting line with the chairman. They must be in a position to provide independent information to the external directors and they must also be the clear and undisputed confidants of the chairman. If any conflicts arise between board and management, between chairman and CEO, this should not lead to a conflict of loyalty for the company secretary.

The authors of the book, in their conclusions, state that the company secretary role requires a high degree of discretion due to the important

and often sensitive issues involved. And I could not agree more with what they say at the very end of the book: "People matter – not structures. This is true for the boards as well as for the secretary." I hope that this book, which is based on comprehensive research and rich personal and professional experience of the authors, will contribute to a broader understanding of what is really important for companies and their boards' structures and working methods. May it also contribute to an open discussion on the essence of the independence of boards and the support they get from their secretaries!

Marcel Ospel
Chairman of UBS AG

Notes on the Authors

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Gertrud Erismann-Peyer joined International Institute for Management Development, Lausanne, Switzerland (IMD) as Executive in Residence with a primary responsibility for an empirical study on the role of the company secretary, after her retirement as the Company Secretary of UBS AG. She assumed the Company Secretary function of the Swiss financial services group for eight years, after having been in charge as head of the Group Corporate Communications Department with responsibility for media relations, employee communication, investor relations, and marketing communication at Union Bank of Switzerland. Prior to that, she was responsible for the Political Public Relations Department of the Organization for the Promotion of Swiss Economy in Zurich. She holds a Master of Law from the University of Zurich. Since her retirement she also serves as an independent board member for a Swiss medium-sized, internationally active engineering company.

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Executive Summary

Context and research design

Since the mid-nineteenth century, corporate governance rules have always evolved after serious breakdowns in the trust of investors. Financial markets are especially prone to bubbles and when the inevitable burst occurs, the "hangover" leads to government interventions. The individual topics under the aegis of corporate governance change, as do the names of the players involved, but the pattern has remained the same since the modern corporation evolved more than 150 years ago – that is, powerful insiders taking advantage of naive investors for their own financial gain. We owe most of the resulting regulations to efforts that governments have made to restore "investors' confidence" (primarily after stock market turbulences or corporate scandals): accounting rules, external independent certification, stock market listing requirements, reporting, and transparency rules. The "principal–agent" theory provides the underlying conceptual framework for these changes.

The backlash after the 2001 dot-com bubble was extremely powerful. Today, investors are no longer predominately small "retail" shareholders but instead are powerful institutional investors, for example, pension funds or hedge funds with an agenda to be able to look closely into a company without becoming insiders (which would impede their trading ability). For the first time, company boards and their work also became a focus of regulatory intervention. Boards of directors worldwide appointed a majority of independent directors and established independent committees. New responsibilities were added to the boards' rosters (e.g., risk management and control, compensation policy and management performance assessment, corporate responsibility, codes of ethics, board self-assessments). Boards have become more active and involved – they have moved from a "Lap Dog" to a "Watch Dog" style of management supervision.

As the board's workload proliferates – and becomes more elaborate in an effort to meet an increased number of regulatory and capital market requirements – the processes behind the board meetings also become more complex and sophisticated. There has to be someone responsible for "oiling the board machine."

At IMD we have always been interested in the inner workings of the board, its leadership role and the conflicts and dilemmas that it is confronted with. As a result, it was only natural that in 2002 we began to look into the work of those people who keep the board machinery functioning – those primarily referred to as the "company secretary." It is important to be aware, however, that the job was and still is executed under a wide variety of titles. The position's content differs considerably depending upon the country and the company in which the company secretary works. As the importance of these duties grew and the job description broadened, we decided to launch a global research project on the role of the company secretary – a function that is increasingly developing into what we call the "corporate governance officer (CGO)." On the basis of extensive discussions with company secretaries, especially at an IMD Discovery Event in October 2004, we formulated the following key research questions:

- What are the corporate governance drivers and to what extent do they influence the work of the company secretary/CGO in particular?
- What is the profile of such a function (previous job, education, hierarchical position)?
- What is the corporate governance setup with regard to board processes and compositions? What is the job of the company secretary/CGO in terms of responsibility, support structure, activities, and so on?

We conducted 68 in-depth personal interviews mostly in large, global companies and analyzed quantitative data obtained from 330 questionnaires worldwide (for details of the study design and methodology see Chapter 2). In the following paragraphs, we will provide an overview of the main findings.

Corporate governance dynamics and structures

It is not at all surprising that regulation is regarded as the main driver of corporate governance. And there is certainly no lack of new legislation around the world – a lot of it in forms that are "softer" and nontraditional, for example, stock market listing requirements (mentioned as second driver in importance by company secretaries responding to our questionnaire). Public pressure was seen as the least important driver; this may, however, merely reflect a certain short-term view not taking the "history" of many corporate governance laws and regulations into consideration. Public pressure, after all, is very often the trigger for new

or more intensive regulations (see Section 3.1 for more detail on this subject).

One important aspect of corporate governance is, of course, the way boards are organized. Whether the company has a one-tier or a two-tier board is a significant factor, even if decision-making processes are shaped primarily by the composition of the board and the working relations between internal and external, independent and executive directors. In all cases, however, the reporting line of the company secretary tells a great deal about his/her position within the organization and the importance attached to the independence of the secretary function. Company secretaries are often highly ranked within the internal hierarchy with more than two-thirds reporting directly to either the chairman or the chief executive officer (CEO). A reporting line to the CEO automatically places more emphasis on the executive side of the company whereas reporting to the chairman, whether executive or not, can be a clear sign of the board's desire to be more independent of management. Supervisory boards in two-tier systems, however, sometimes do not have any dedicated staff support making it difficult, or even impossible, to have a secretary reporting to the external, nonexecutive chairman. This can potentially lessen the board's overall independence.

The relationship between the chairman and other board members, in addition to the overall internal organization of the board, are other key factors when it comes to defining the company secretary's role; they determine how much support the secretary gives to the board as a whole or just to the chairman as an individual. Furthermore, the full board's meeting frequency, in addition to the number of board committees (both of which have gone up in recent years), hold significant importance. Both factors are "multipliers" of the secretary's workload (there are more details about this in Section 3.2).

Background, career opportunities, and challenges for the company secretary

Given their past and current role, it is no surprise that an educational and professional background in legal affairs is the predominant experience for company secretaries. More surprising, nearly half of our respondents were recruited externally to fill a job where confidence is key and networking across the company a must. We can only conclude that in many cases no adequate internal talent existed (probably especially true in smaller companies). The widespread perception of the function being a rather technocratic, legalistic administrator might

further reduce the chances for internal recruiting on a high level. Future career advancement also seems to be rather restricted. Few of the secretaries have experience in line management and would therefore not easily find an adequate business function within the company. Moving to another, probably larger, corporation as a company secretary may be a good solution. Owing to the secretary's broad experience in corporate governance, assuming a board seat in other medium-sized companies after early retirement might be a promising and challenging move but it is not yet a common one.

Both job duration and job satisfaction are high for company secretaries; factors which serve as indications of the job's "richness" and importance. It became clear through our interviews and questionnaire responses that the job of the company secretary is often fairly unstructured. There is significant discretion in terms of how to fulfill the task. The interpretation of the role is shaped by the personality of the office holder, how he/she is networking, building relationships, and so on. This should not be surprising because the issues that the secretary has to deal with are generally not the chairman's or the CEO's (to whom they primarily report) favorite topics. The chairmen and CEOs are generally happy to leave the complicated, sometimes boring, but important legal and compliance "stuff" to someone they trust and who will take care of it competently. This paves the way to a pretty influential job ("éminence grise") as long it is done with discretion and tact. Ultimately, of course, the board makes the decisions, not the secretary.

Life can be difficult for the company secretary. In most cases, at least outside of the United States, the roles of chairman and CEO are assumed by two different individuals. Secretaries, however, are often accountable to both the chairman and the CEO. This can result in a variety of demands both in process and in overall job assignments (some of which, of course, are legally mandated). During "normal times" this dual accountability is not a problem but it can become a significant challenge for the secretary in the case of fundamental differences between the chairman and the CEO and/or between the board and management. Loyalty conflicts are the unpleasant result of these situations (see Section 3.3.3 for more about this topic).

Tasks and responsibilities

Both the company secretaries who were interviewed and those who responded to our questionnaire reported having a wide variety of tasks and responsibilities (Chart ES.1).

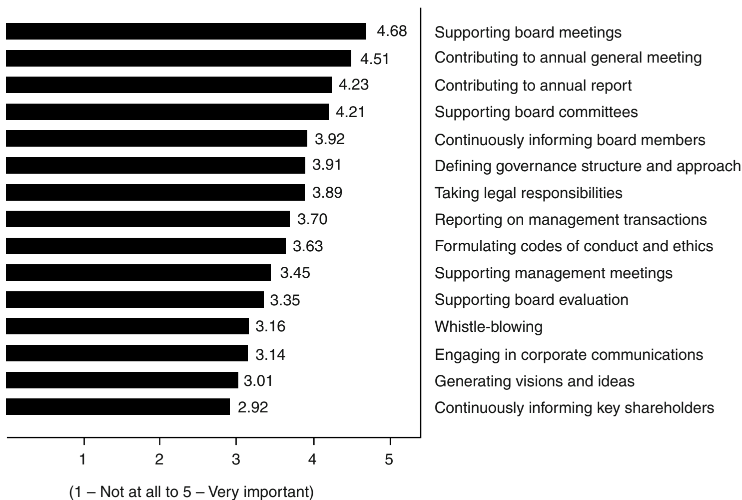

Chart ES.1 Importance of tasks and responsibilities

Providing support to the board of directors is, of course, one of the primary tasks of the company secretary. But the way that support is executed in terms of intensity and priority differs widely. The company secretary is involved in setting the board's agenda to varying degrees. Most secretaries have to ensure that the documents for the board book are ready on time (requiring considerable "herding" efforts). Some set specific criteria for the necessary papers, edit the texts, and/or add additional information (to help the outside directors understand the topic). Other secretaries simply compile the necessary paperwork that has been delivered to them. The only commonality is that electronic distribution of board papers is not widely utilized (it is employed by only 10 percent of respondents).

We know from the results of a previous study that there is significant room for improving board information management (Steger and Amman, 2008). Basically, board information is too often seen from the perspective of a "rear view mirror" and remains internally focused; examining more external and forward-looking information (e.g., regarding competitors, industry trends, and technology dynamics) is desirable. However, few boards take the trouble to clearly define what information they want and need. This can leave management guessing and adding information "organically" as requests come up. Over time, this results in a growing information flood without becoming more