EFFECTIVE CORPORATE GOVERNANCE

Theory and Best Practices

Kirimi Barine

David Minja

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To the students, practitioners and experts of Leadership and governance.

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Section I:
Theory

1.

Introduction to Corporate Governance

The last two decades have seen the evolution of governance from a mere concept to a more fundamental discipline in social and economic circles. Avellaneda (2010), in a paper titled, "Good Governance, Institutions and Economic Development: Beyond the Conventional Wisdom," and presented at the *Forum de Recerca, Department de Ciencies Politiques I Socials, Universitat Pompeu Fabra*, Barcelona, observes that a growing literature stresses that governance, broadly defined as the traditions and institutions that determine how authority is exercised in a country, matters to economic development.

According to the Good Governance and Human Rights Organisation, there is no single and exhaustive definition of "good governance," nor is there a delimitation of its scope that commands universal acceptance ("Economic Rationality," 2009). The term is used with great flexibility; this is an advantage but also a source of some difficulty at the operational level. Depending on the context and the overriding objective sought, good governance has been said at various times to encompass: full respect of human rights, the rule of law, effective participation, multi-actor partnerships, political pluralism, transparent and accountable processes and institutions, an efficient and effective public sector, legitimacy, access to knowledge, information and education, political empowerment of people, equity, sustainability, and attitudes and values that foster responsibility, solidarity and tolerance (UN, n.d.)

WHAT IS CORPORATE GOVERNANCE?

Corporate governance is the system by which companies are directed and controlled (Cadbury et al., 1992).

Thus, governance is a system based on a set of practices to facilitate the development of enterprises that are accountable (McNamara, n.d.). Furthermore, governance includes the relationship between the exercise of power and the management of socio-economic resources for a welfare society. In the contemporary world of political pluralism, the concept of governance has become crucial and attracted great interest. Governance forms a significant component of the balance maintained between the quest for equity and order in society, effective production and distribution of goods and services, accountable exercise of legitimate power, respect for human freedoms and rights and finally,

promotion of a socially and economically viable corporate environment that is accommodative to everyone's contribution (Monks & Minow, 1996).

The term "corporate governance" was first used in 1960 by Richard Eells in his attempt to define how corporate polity is structured and functions. However, the concept of corporate governance existed as early as the start of the 20th century, especially in finance textbooks. Moreover, the origins of this concept form the core basis of the definition of corporate governance. The constituents of corporate governance include processes, customs, policies, laws and regulations stipulating how enterprises should be administered or controlled. Equally important, corporate governance outlines the way stakeholders should relate and lays out corporate goals. Key corporate decision-makers include shareholders, management, and the board of directors. Stakeholders in the corporate governance structure consist of the workforce, suppliers, customers, financial institutions, and regulators, as well as the surrounding community.

According to Cadbury et al. (1992), corporate governance consists of the systematic control and direction of enterprises. Furthermore, corporate governance can be described as a set of management practices adopted by companies in the process of separating ownership and core business operations. The benefits of corporate governance are best experienced in the presence of core values of transparency, accountability, fairness, and responsibility. This is critical in reaffirming the confidence of investors, stakeholders, and the wider community. Corporate governance provides a plausible arena for different players to meet and relate while reflecting on the principal goals of the enterprise. Corporate governance is the way different participants relate in the process of charting the direction and performance of an enterprise (Blair, 1995).

Blair (1995) further states that corporate governance consists of a composite of legal, cultural, and institutional procedures that outline the functions of public corporations, who and how to control them, and finally, the risk-to-reward ratio in their operation. This further implies that corporate governance exists in an environment with an established legal, economic, and institutional framework that makes it possible for any enterprise to thrive and give value to shareholders while ensuring sustainable development that is human-centred and responsive to the expectations of stakeholders, the environment, and the wider society.

The figure below shows the relationship between owners and people who benefit from an organisation, its board, and management.

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