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GEORGE COX, ERSTWHILE DIRECTOR GENERAL OF THE INSTITUTE OF DIRECTORS

According to George Cox when he was Director General of the Institute of Directors, in the Introduction to the director's guide to 'corporate governance' [IOD, 2004], "Modern capitalism – the model to which virtually the whole world now aspires – is totally dependent on high standards of governance".

What he means by 'governance' is the overall and rigorous supervision of company management so that business is done competently, with integrity and with due regard for the interests of all stakeholders. And this is important, not for altruistic reasons but because investors wouldn't buy shares in a company (or, rather, they'd insist in a considerable discount) if it wasn't run that way. As Alastair Sim, Director of Strategy and Marketing at SAS, points out in his Forward to the same work [op. cit.], staying competitive involves maintaining investor confidence. The best way to do this is to ensure the transparency of a company's operations to investors and other stakeholders, by supplying them with appropriate and trustworthy information (with due regard to business confidentiality) and this is one of the main concerns of corporate governance, along with the need to comply with applicable laws and regulations.

In the UK, the law is defined by statute; statutory instruments, which implement Acts of Parliament and can materially affect the impact of a statute; and is further developed in the courts by precedent – so determining exactly what the law says is not always straightforward and taking expert advice is often a good idea. We then follow a 'comply or explain' approach to governance. What this means is that, for example, companies with a full London Stock Exchange listing have to state that they comply with, for instance, the Combined Code (the consolidated governance rules promulgated in June 1998) but can report exceptions in certain areas, where they must explain the reasons for their departure from the rules.

The Combined Code [Combined Code, web] places great emphasis on the need to manage risk, which is largely what the financial reports made available to the various stakeholders are used for. As Peyman Mestchian, (Director, risk management practice, SAS UK) puts it "the sensible company takes risks – but not gambles". You must take a holistic and objective view of risk – there is more to worry about than just financial risk. Reputation risk, for example, is frequently overlooked – until loss of reputation starts to affect the financial bottom-line, when it is often too late to mitigate it (a reputation that took years to build can be lost in months). The Turnbull Report guidelines to governance for companies quoted on the UK stock exchange talk about the risk associated with market, credit, liquidity, technological, legal, health and safety, environmental, reputation and business probity issues, as well as financial risk. However, some risk is good – you can't avoid risk without forgoing the business opportunities associated with new kinds of customers, new technologies and new products. In fact, risk avoidance is in itself risky as it limits your opportunities for profit, and doing nothing is frequently the worst possible response to an emerging issue. What is important is that commensurate rewards are associated with the risks that you take, which implies that you have access to reliable information that lets you forecast the rewards and assess the risks with confidence.

Corporate governance ultimately depends on the good functioning of the Board of Directors – and, increasingly, non-executive directors are asked to take responsibility for deviations from good governance. Quoting Kerrie Waring, international professional development manager at the IOD [op. cit.], "A well functioning Board is key to the performance of companies and their capacity to attract capital. A well-established corporate governance framework should ensure that Boards monitor managerial performance effectively to achieve an equitable return for shareholders and uphold the values of fairness, transparency, accountability and honesty."

You could say that the prime objective of IT governance is to help rather than hinder the Board in its governance efforts, as part of a dynamic partnership between business and technology. (Technologists enable business; business rewards technologists.) In many organisations, the IT function is seen as a bit of a loose cannon, subject to different standards, responsibilities and controls to the rest of the organisation; and, in the long term, this isn't going to be good for the careers of those employed by the IT function.

Corporate governance is often talked about in the context of publicly quoted companies, because the shareholders in such companies form a wide and visible set of stakeholders, and because stock markets underlie most economies these

days. However, similar considerations also apply to private companies, of course, since although the stakeholders are different and the legal issues perhaps rather simpler, the owners of the company still need access to reliable information as to its operation.

Regulations in the USA, say, are generally more draconian these days – although even Sarbanes-Oxley seems to be less prescriptive and more in the European style than previous US regulations. This is actually an improvement, as it is harder to merely comply with the 'letter of the law' if you can be assessed both on what you consider to be appropriate internal controls and also on the effectiveness of your implementation of these controls.

International corporate governance rules are also changing, but rules worldwide seem to be generally moving in the same direction. Eventually, it is hoped that the mission statement of the International Accounting Standards Board (IASB) will come to fruition and we will have 'a single set of high quality, understandable and enforceable global accounting standards that require transparent and comparable information in general purpose financial statements'.

Which brings us to Information Technology (IT), since large amounts of information are seldom stored, processed and retrieved manually these days. Your financial reporting is only as good as the quality of the data reported. You must be able to audit the lifecycle of this data from collection through to destruction: you must be able to show where it comes from, who has access to it and that any changes are properly authorised. IT can facilitate this: there is an issue with the transparency of IT (few businessmen are completely comfortable with code analysis) but business policies can be rigorously enforced in unambiguous computer code and any risk of manual error mitigated. Well, up to a point – 'garbage in = garbage out' applies and IT systems only do what they are told to do. This is, of course, a governance issue: the policies embodied in the automated systems must be aligned with corporate policy, the instructions input to the IT systems must be the right instructions, and the accuracy of the translation of these instructions into code must be tested.

IT is also increasingly a major source of risk in companies:

- IT facilitates worldwide access to internal systems, increasing the opportunity for fraud and data theft.
- The scope of impact of IT systems failure can be company-wide.
- IT projects are frequently an enabler for new business; in fact, IT systems are increasingly central to the operation of many companies.

- Despite the importance of IT, according to the Standish Group Chaos Reports [Standish, web], over 80% of IT projects come in late, over budget or wrong (and frequently all three) – over a quarter are cancelled before they are fully implemented.

The Board needs to recognise the risk factors affecting IT projects: very large projects, visible projects, projects crossing geographical or departmental boundaries, projects using new technology projects particularly dear to the Board's heart are all particularly risky.

IT development failures or operational failures are equally matters of corporate governance. When Nick Leeson brought down Barings, there was a real failure of banking governance – essentially, it simply isn't good practice to allow traders to make their own settlements. However, you can equally see this as partly an IT governance issue:

- The technology is available to enforce governance policies including separation of function.
- Positions and limits can be reported transparently to management.
- The calculation of settlements can be removed from the possibility of human error.

What technology can't do, of course, is to inculcate common sense in the Board or counteract complacency or greed. Even so, increasingly, IT is being made accountable for technology-driven business outcomes and a technical failure that is allowed to affect the operation or reputation of a company is being seen as a failure of corporate governance – as, of course, it is.

The next chapter looks at the legal framework underlying governance generally in the context of IT governance specifically.