CORPORATE GOVERNANCE

Seeing Versus Knowing–Why Corporate Governance Has Been Perceived as Failing Lately

The press has been talking about it for a while. If you Google it, you find almost a half million hits. Just try it: corporate governance failure—failure of corporate governance. I've been in the banking industry for almost 30 years, know many bank board members, and just find this to be a strange notion—that they are failing.

The board members I have met are smart businesspeople with a genuine interest in the performance of the bank. Most have invested a significant amount of time in assisting the bank and providing valuable counsel and insight to executive management. So what exactly caused this "breakdown" in corporate governance? Could the answer and solution be based in a very basic (and maybe esoteric) concept of seeing and knowing?

There are approximately 250 business days in a year. At a minimum, these are the number of days management spends on bank business. But how many days does the director of the bank spend? Let's say a non-executive director attends one board meeting per month and one bank committee meeting each month; that director would spend 24 days a year on bank business. That means the board member is involved in the bank about 10% of the time. This is our first hint that the problem may truly be in seeing and knowing.

Two Ends of the Spectrum

Suppose you created a spectrum with one end labeled "seeing" and the other labeled "knowing." At the knowing end are the people who do the work—the ones who spend their time intimately involved with the bank. At the other end are the people who "see." They don't get lost in the details, their experience and skills allow them to quickly look at a report or an event and interpret what is happening. In this seeing and knowing world, the board of directors are the ones who "see" while bank management are the ones who "know." Each exists at opposite ends of the spectrum.

The "people who know" naturally assume that everyone has the same knowledge they have—that everyone understands how borrowers are pursued, loan applications are analyzed, what assumptions are made, and where the weaknesses are. On the other hand, the "people who see" assume the information they are given is an accurate picture of the activities and events at the bank. They also assume that reports, no matter how thick or detailed, tell them what they need to know to fulfill their duties as directors.

Deliver the Right Stuff at the Right Time

What is missing from this scenario, then, is the concept of understanding—right in the middle of the spectrum. Ideally, management (those who know) presents information to the board (those who see) in such a way that they have a perfect understanding of the risks the bank faces. Anyone who lives in the middle of the spectrum is "all knowing and all seeing." But that isn't realistic. Board members will never have the in-depth knowledge that bank management has, nor should they. It is management's responsibility to provide the board members with the information they need to perform their duties. And it is the board's responsibility to make certain that the information it gets is received in a timely manner with enough detail to capture the organization's risks.

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As a consultant, I can attest to the fact that bank management doesn't always subscribe to this thought process in drafting the board packet. I have seen 100+ page reports on every loan included in the packet and writeups that rival War and Peace. In these situations, management has not taken the time, nor has the board required management, to distill the information into a comprehensive, succinct picture of the state of things that is accessible to every board member.

Steps to Bridge the Gap

It is time for every financial institution to sit down and review what is being presented to the board. Can the board grasp the risks the bank faces and make decisions that enable the bank to change course at the appropriate time, to mitigate the risks it faces, and to fill in the gap in corporate governance that has now been identified?

Seeing and knowing may be at the heart of today's corporate governance issues. The beauty is that this is something that can be addressed so that the bank can do a better job of managing through the next expansion and the next crisis.

By John Hurlock

John Hurlock is Director of Risk Consulting Services for Sheshunoff Consulting + Solutions. Sheshunoff Consulting offers management consulting, risk management, technology solutions, and investment banking services and solutions. Sheshunoff's Affiliation programs are known as unique venues for sharing information and peer networking. We are proud of our role in the financial services industry, refined through our many years of service to banks.