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Martin Hilb *Editor*

New Living Cases on Corporate Governance

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The editor is Chairman of the International Board Foundation and most of the authors of the new living cases are Partners of its International Center for Corporate Governance.

Martin Hilb
Editor

New Living Cases on Corporate Governance

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International Board Foundation and its
International Center for Corporate
Governance
St. Gallen, Switzerland

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Preface

The structure of the book *New Living Cases on Corporate Governance* is based on our publication *New Corporate Governance* which is published in 10 languages (Chinese, Japanese, Vietnamese, Spanish, Portuguese, English, French, German, Croatian, and Farsi) and has received a gold medal in corporate governance by the International Academy of Quality in the USA "for the exceptional contribution to the principles and practice of quality in governance".

We have asked the partners of our International Center for Corporate Governance (www.icfcg.org), many of them professors in corporate governance (e.g., at IMD, INSEAD, London Business School) or chairpersons or members of the board of directors, to present a living case on corporate governance which can be used for internal or public board education internationally.

Eighteen partners from 12 different countries have described unique cases they have experienced in their field of board expertise in a specific country or business sector or board function. The names, dates, and locations in all these living cases have been changed to keep confidentiality.

We hope that these living cases will contribute to the development of corporate governance practice.

Many thanks to Otto Strasser for his valuable translations/layout design and Ruth Milewski for her professional publishing.

Note: Except as noted otherwise, figures and tables are compiled by the author.

St. Gallen, Switzerland — Martin Hilb
1 March, 2020

Introduction: New Corporate Governance in the Post-Crisis World[1]

What Is "New"

Based on the results of board evaluations conducted in various business sectors, the following main weaknesses of current corporate governance practices have been identified:

- Most national corporate governance guidelines propose a "one-size-fits-all" approach which is dangerous; it may support good governance, but it does not guarantee that the governance of a firm will become great.
- There is a lack of strategic direction in much of board practice.
- Board selection, appraisal, remuneration, and development often lack integration and professionalism.
- Often there is a lack of in-depth know-how in risk management at the board level.

This chapter presents an integrated corporate governance framework called "new corporate governance," which is based on a reversed KISS principle:

- Situational
- Strategic
- Integrated
- Keep it controlled

[1]This chapter is a revised reprint of "A Global Corporate Governance Forum Publication" by Martin Hilb, issue 16, by International Finance Corporation, Washington CDC, 2010.

This holistic framework for the direction and control of enterprises tries to overcome the above stated weaknesses of corporate governance in the post-crisis world. What is “new,” you may ask?

The new corporate governance framework integrates the interests of shareholders, customers, employees, and the public. The framework comprises four parts which are presented in this paper.

Keep It Situational: The Board as Change Agent

As a result of the many corporate scandals that have taken place around the world, best-practice corporate governance guidelines have been developed in most countries.

This is a positive development, although the following issues should be noted:

1. The Anglo-American model of governance is being promoted as the global standard.
2. Soft laws do not necessarily address the soft dimensions of a firm (in other words, laying down a new soft law does not replace the need for integrity in board relationships and processes).
3. Best-practice guidelines are typically designed for large, publicly listed firms (and hence they are often not suitable for small firms).
4. Good governance guidelines do not guarantee great governance practice.

In adopting corporate governance guidelines developed elsewhere, companies should be aware of the best-practice guidelines for:

Table 1 Keep it situational

Listed companies	≠	Non-listed companies
Large companies	≠	Small companies
Public companies	≠	Family-owned companies
Bank governance	≠	Hospital governance
US companies	≠	British companies

Hence, we base our approach on the principle: keep it situational. There is no “one-size-fits-all” corporate governance approach.

Keep It Strategic: The Board as Value Driver

We propose four main preconditions for success in developing, implementing, and monitoring corporate strategy:

1. A strategically targeted composition of the board team
2. A constructive and open-minded board culture
3. An effective board structure
4. Shareholder- and stakeholder-oriented board measures of success

These four components have to be integrated in a process, as shown in Fig. 1. At each of the different levels, success measures are to be established relating to the important stakeholder groups, and then the responses of members of these

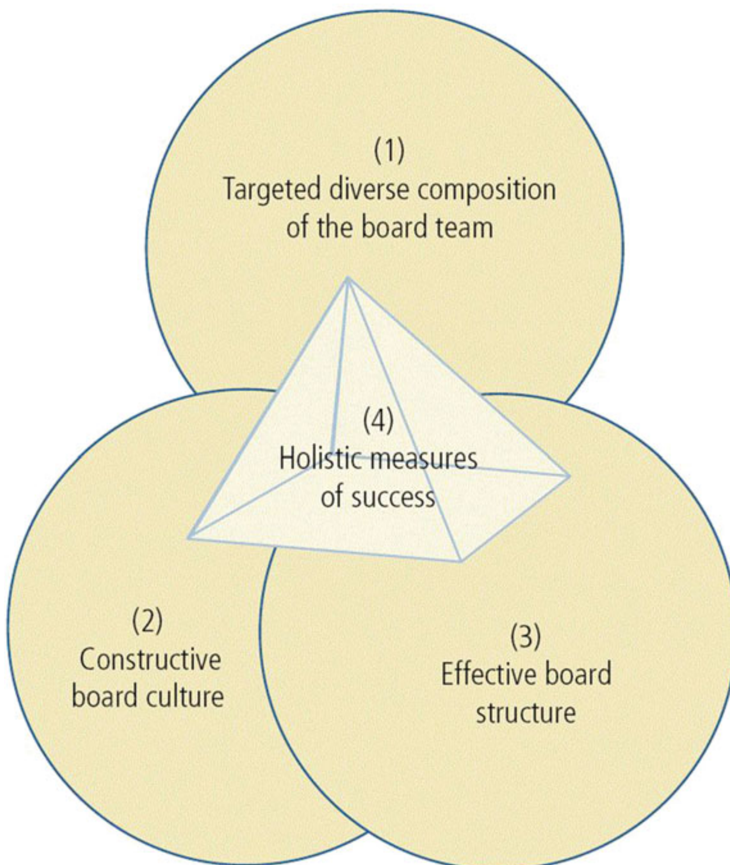

Fig. 1 Keep it strategic

stakeholders' group are to be measured periodically in order to assess the performance of the company leadership.

In the following subsections, each of the four preconditions for successful development and implementation of corporate strategy is discussed.

A Well-Diversified Board Team

Peter Senge asked the question: "How can a team of committed board members with individual IQs above 120 have a collective IQ of 60?" The question could be restated as: "Where do good ideas on boards come from?" In response, Negroponte—Founder of the MIT Media lab—says: "That's simple... from differences."

Together the above quotes are indicative of the fact that differences are an essential part of the strategic potential of a team and that too many boards have failed to create adequately diversified teams. Our suggestion for building differences into board composition is to mix disciplines, team roles, demographic variables, and stakeholder parts.

Well-Diversified Board Teams Consist of Members Representing All Relevant

- Functional competences (e.g., auditing, risk management, HRM, marketing)
- Team roles (e.g., a controller, a critical thinker, a creative thinker)
- Demographic data (e.g., age, gender) and internal and independent members
- Stakeholder "hats" such as customers, shareholders, employees, and society/environment

Each board member has to cover various aspects at the same time, e.g., functional know-how: risk management/team role: critical thinker/membership: independent/social data: very experienced female/stakeholders "hat": shareholders.

A Constructive and Open-Minded Board Team Culture

We suggest that an effective board culture should consist of five factors: an outward, learning orientation; a holistic perspective; a consensus orientation; a constructively open, trusting environment; and a mix of global effectiveness and local adaptability (we refer to this as "glocal").

An Effective Board Structure

Our experience in board management reveals two extreme ways of structuring board teams:

- A large board, operating through a number of different committees (such as auditing, nomination, or remuneration committees)
- A small board of professionals

We Recommend a Third Way
A small, legally accountable, well-diversified board team, comprising a maximum of seven members (including an independent chairperson, independent members, and the CEO). We recommend that the board conducts its activities through only two committees: an integrated audit and risk management committee and an integrated board management committee which is responsible for nomination, feedback, remuneration, and development of the board and top management.

In addition, large public companies can add a large network council (not legally accountable) whose members work in small projects teams, each of whom is coached by one of the independent board members.

Shareholder and Stakeholder Measures of Success

A combined team of supervisory and managing board members need to develop, implement, and evaluate a shareholder—and stakeholder-oriented board vision. Such a vision should:

- Provide a roadmap for future direction
- Generate excitement about future direction
- Instill confidence and trust in leadership
- Offer criteria for success

If corporate success is measured against such a vision, it will necessarily reflect both shareholder and stakeholder measures.

The Following Statement Can Serve as an Example of a Normative Guiding Principle
"The primary role of the board of directors of this company is to help create long-term value for its shareholders, customers, employees and society. The board believes that the company should rank in the top quartile of peer companies in total shareholder return (including the cost of capital), as well as in voluntary loyalty levels of customers, employees and society as measured over 1 and 3 year periods."

This strategic direction function is the basis for the targeted selection, evaluation, remuneration, and development of board members and top management which will be described in the next section.

Keep It Integrated: The Board as A Team

In order to achieve the conditions required for strategic board management described in the last section, four key processes are recommended: targeted selection of members of the supervisory and managing boards, targeted feedback on their performance, targeted compensation, and targeted development (illustrated in Fig. 2).

In the following subsections, we discuss the elements of the figure in more detail, commenting on key principles and practices that can be used in their implementation.

Phase I: Targeted Board Selection

The use of a one-page interview schedule is recommended to guide the specific selection of board members. The interview schedule aims to score the potential of the interviewee on a number of criteria (such as personality, social, professional, and leadership competencies) from the perspective of at least three interviewers (at the level of chairperson, the CEO, and another board member). After the interviewee has been through at least two rounds of interviews, the interviewers hold a short meeting during which they attempt to reach agreement in the score awarded for each item on the schedule. Where a consensus cannot be met, further investigations are to be made

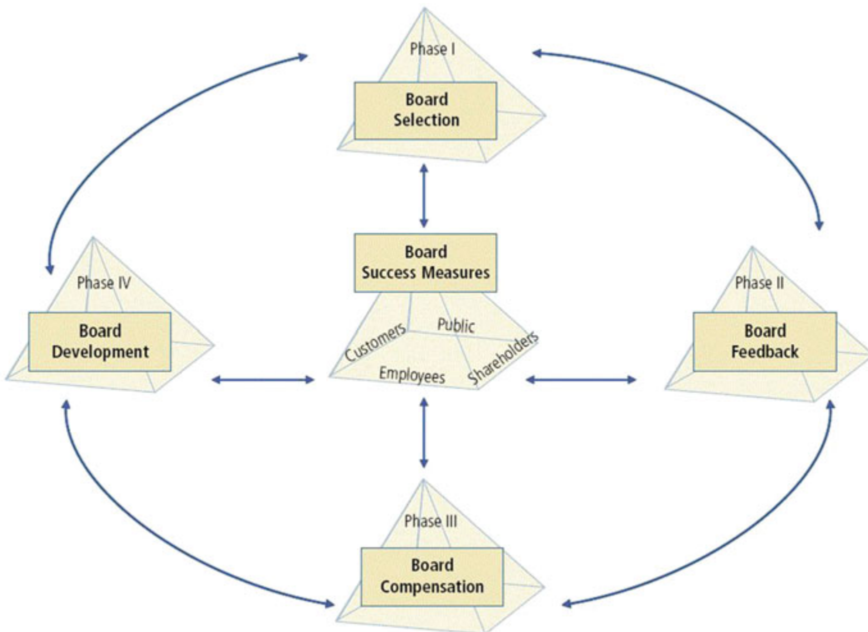

Fig. 2 Keep it integrated

into the nature of the response. A suitability ranking is drawn up on the basis of the final evaluation of each item.

Phase II: Targeted Board Feedback

After board members have been selected, it is natural to introduce an effective feedback program for board members.

We recommend that feedback be linked to the collective performance of the supervisory board and the individual performance of the CEO. In each case, there are a number of dimensions on which the performance can be evaluated.

Targeted board feedback is only suitable if positive performance is rewarded and actions are taken to address development requirements.

Phase III: Targeted Board Remuneration

Board members should be compensated in such a way that they perceive equity based on internal, external, and corporate performance benchmarks.

The total net compensation package of a board member can be divided into fixed (e.g., 40%) and variable (e.g., 60%) components. The variable component can be made up of several measures of performance including:

- Long-term financial performance (3 years)
- Comparative value indices (e.g., 50% EVA, 20 percent customer loyalty, 20% employee satisfaction, and 10% public reputation)
- Functional performance assessments (20% board committee performance, 30% individual board member performance, and 50% corporate performance).

An important guiding principle in board remuneration is that every board member expects financial compensation to be fair. Modifications of the package above or below fair reward are unlikely to result in better performance, since board members are generally driven by intrinsic motivations (Frey 2004). Thus, adequate and fair rewards are important prerequisites for good performance, but motivation is primarily affected through immaterial reward of good performance.

Phase IV: Targeted Board Development

Past board evaluations conducted by us have shown that in quite a number of leading companies, management and board succession planning is not discussed in depth at the board level. The board should ensure that development programs are in place to enable the company to offer 80% (for example) of all vacant key positions in the company to internal candidates. In this regard, the approach of having the CEO and

her/his direct reporting vice presidents present their succession plans to the board once a year has proved successful.

This procedure creates an opportunity for division heads to make a presentation to the board, socially. If an opening arises at the top management level, the board will be well prepared and can use the same form as that used for the targeted selection of external candidates.

Keep It Controlled: The Board as Controller

In this integrated approach, the controlling or monitoring board dimension encompasses the following functions (see Fig. 3).

Fig. 3 Keep it controlled

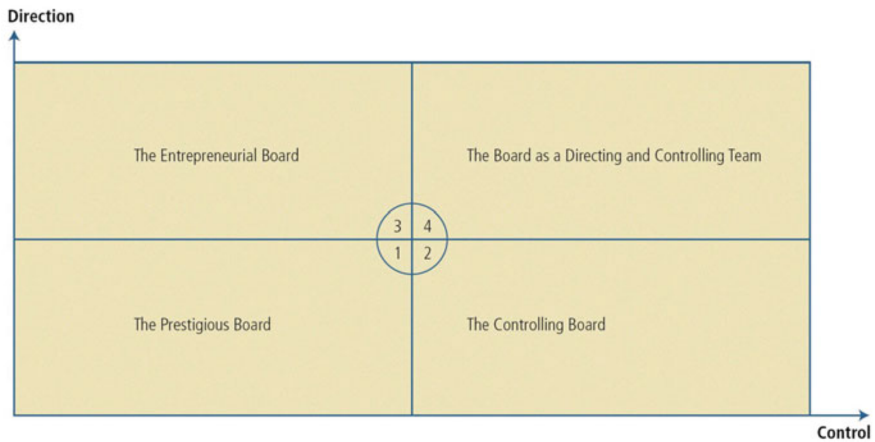

Fig. 4 Levels of boards

It may also be sensible to formulate some essential questions in a board meeting, about which board members should be continually informed (Fig. 4). For example:

- Where is shareholder value being created and destroyed in the company?
- What are the major risks to which the company is exposed?
- What is the level of employee morale and voluntary loyalty compared to competitors?
- What are the threats to customer satisfaction and customer loyalty compared to competitors?
- What is happening to our corporate image?
- How does our strategy differ from that of our competitors?
- How is our stock viewed by the analysts who cover us?

Last but not least, the board has to evaluate board effectiveness on an annual basis.

This paper presents a "both-and" approach called "new corporate governance." The objective of this approach is to overcome the "either-or" thinking that currently dominates corporate governance theory and practice, based on the principle espoused by F.S. Fitzgerald that "The test of a first-rate [board] intelligence is the ability to hold two opposing ideas in mind at the same time, and still retain the ability to function." (Fig. 5):

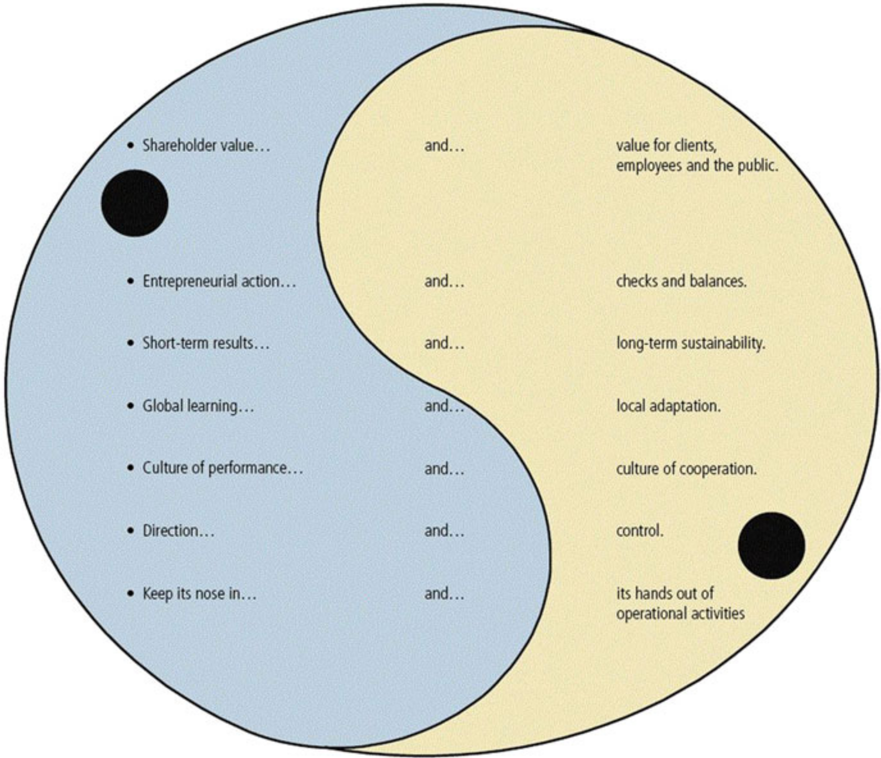

Fig. 5 Balance

An Effective Board Tries to Balance Both

It remains to be seen whether boards have the will and resources to transform themselves into true directing and controlling teams, changing their orientations from corporate administration to corporate *control-preneurship*. The result of this challenge will determine whether companies will be among the winners or the losers in the face of global change and competition.

St. Gallen, Switzerland Martin Hilb

Contents

Part I The Board of Directors as a Change Agent

Family Company Governance Case 3
Martin Hilb

University Governance Case 5
Tudor Maxwell and Stefano Bianchini

Start-Up Investor Governance Case 9
Robert M. LoBue

NPO Governance Case 15
J. Augusto Felício and Ricardo Rodrigues

Part II The Board of Directors as a Direction Body

M&A Governance Case 21
Martin Hilb

Family Company Direction Case 25
Christoph Maier

University Direction Case 31
Mehtap Aldogan Eklund

Board of Directors as a Strategic Sparring Partner 41
Roman Lombriser

Part III The Board of Directors as an HR Governance Body

Reward Governance Case 47
Rolf Dubs

Succession Planning Governance Case 51
Martin Hilb

Owner–CEO Collaboration Case 53
Elena Szederjei

Board–Management Collaboration Case 57
Harry Korine

Governance of Gender Diversity Case 61
Beatrix Dart

A Case of Responsible Restructuring as Good Governance 65
Victoria Maier

Part IV The Board of Directors as a Controlling Body

Subsidiary Governance Case 77
Martin Hilb

Financial Competence on the Board Case 83
Peter Leibfried

IPO Governance Case 87
Jean-Pierre Jeannet

Fraud Governance Case 91
Fred van Eenennaam and Hagar Michel

Afterword: Lessons Learned from the Living Cases and from the Global Financial Crisis 95

Keep It Situational 97

Keep It Strategic 99

Keep It Integrated 101

Keep It Controlled 103

Conclusion: Search for Sustainability and Common Sense 105

Part I

The Board of Directors as a Change Agent

Check for updates

Family Company Governance Case

by Martin Hilb
(Switzerland)

International Board Foundation and its
International Center for Corporate Governance

All names and dates have been changed in this "living" case: Max Meier (61), a "humane" entrepreneur (with a cool head, a warm heart, and working hands), succeeded his father as baker in 1987 in Appenzell, Switzerland, and has over the last 33 years developed the family business into an internationally successful group of companies renowned for its chocolate specialties.

In 2018, the consolidated annual turnover reached *€250 million*. The group of 7 firms, employing 670 people, were acquired by Max Meier over a 20-year period.

Max Meier does not have any designated successor. He is owner, chairperson, president, CEO, and head of the family. His personality is characterized by a rare combination of entrepreneurial flair, creativity, sales talent, and high moral standards. His wife, the only other member of the board, is the financial manager. Together with Max, the couple constitute an ideal private and professional partnership.

Max and his wife have four children:

- Max junior (36) completed an apprenticeship in pastry making and then finished a law degree at the University of Geneva. Now he is responsible for exports in the firm and is based in Geneva.

See Martin Hilb: "New Corporate Governance," 5th Edition, Springer Heidelberg/New York 2016, pp. 26.

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- Monika (34), a Professor of Sociology at the University of Constance, resides in Kreuzlingen (Switzerland, at the Lake of Constance).
- Freddy (32) has a master's in finance from the Wharton School and is CEO of *Schoko Ltd., a* chocolate manufacturing company (acquired 2 years ago), one of the most successful sweets manufacturers in Entlebuch, Switzerland.
- Nicole (28) is an artist based in Paris. After her fine arts degree, she sojourned in Florence and Paris and furthered her studies in Vancouver and Rome.

Six months ago, Max Meier suffered a heart attack. He now asks you, as a competent, trustworthy, and old friend, how he should confront the issues of board composition and management appointment.

How would you advise him?

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University Governance Case

by Tudor Maxwell (Australia)

and Stefano Bianchini (Australia)

WiseTech Global
International Center for Corporate Governance

Ken Dovey (65) had been Director of a Master in Business and Technology (MBT) at a highly regarded university in Sydney, Australia, for 10 years. Under his leadership, the perceived value of the course had improved to the point where it enjoyed the highest student ratings and most engaged alumni of any course offered by that university. But Ken was planning to retire in 2 years, and the benefits of his strong leadership were at risk.

The MBT had been founded (under a different name) as a joint venture between the business and IT faculties, with subjects offered by each department. When Ken took over the leadership of the program, he instituted several changes, notably:

- Stricter screening of applicants to ensure their skill, experience, and commitment were commensurate with the objectives of the MBT (thereby halving the proportion of applicants accepted)
- Tighter controls over the teaching faculty, replacing some academics with industry-based professionals possessing strong academic credentials
- Increasing communication with alumni, students, and teaching staff to build a stronger community around the course
- Cultivating the research culture by focussing a final-year subject on practice-based research (with the option of leading into PhD studies)

While this strategy lifted the value of the course substantially among the students and alumni, it created tension with administrative leadership in the university:

- Course profitability was negatively impacted by the stricter screening of applicants.
- Members of the business school faculty resented the increased reliance on industry-based professionals and threatened to withdraw support for the use of the word "business" in the course title.
- There were no obvious successors for the role of director in the small full-time teaching faculty.

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Without the support of the university administration, it seemed unlikely that the MBT would be allowed to continue pursuing its strategy, risking deterioration in the qualities that had become important to its reputation.

What advice would you offer to Ken?

1 What Actually Happened?

Ken recognized the need for succession planning. He also knew that his strongest support bases were in the alumni and students. He therefore aimed to unlock the latent leadership potential in those groups to augment the leadership he was providing to the course.

Ken described the challenge facing the course to the students, alumni, and faculty. When a student (Stefano Bianchini) stepped forward with a proposal to focus on those challenges as part of a course assignment, Ken provided his full support.

Stefano held informal meetings with selected students, alumni, and faculty to secure their involvement in an advisory board made up of representatives of each of those stakeholder groups. He then convened meetings of those representatives, and together they formalized the board and crafted a strategy focussing on:

- Successful leadership transition from Ken
- Increased financial independence through paid consulting and teaching engagements
- Further strengthening the alumni and student community network
- Marketing the course to support an increase in the numbers of high-quality students

Students and alumni volunteered time to execute the strategy. They were motivated by the opportunities to expand their networks, learn from practical leadership activities, and have fun with their peers. The strong leadership exhibited by Stefano (and then two subsequent leaders from the alumni group) was a critical success factor.

Notable successes from board initiatives included a private-sector sponsored C-level golf day (now in its 5th year), consulting and teaching engagements in three large companies, high-quality community events often featuring strong local and international leaders, and the sustained leadership of a toastmasters (public speaking) chapter.

The board progressively improved its status in the university. Notable evidence included:

- The university administration disregarded the protests of the business faculty and supported the use of the “MBT” name for the course (a dramatic shift over 2 years).

- The administration requested the advice of the MBT advisory board members in an attempt to replicate this model of student and alumni engagement in other faculties.
- The administration engaged MBT board members to provide input on the choice of the director's successor and on how to market the course under new leadership.

New admissions to the course dropped ahead of Ken's departure, as students and alumni anticipated a decline in standards. The new director and administration requested support from the advisory board to use its extensive network to market the course under new leadership. For as long as respect and trust exist between them, the board offers its support willingly. Since it is a voluntary group, though, its support cannot be taken for granted.

2 What Can We Learn from This Case?

- Organizations that have benefited from strong leadership for sustained periods may find themselves in crisis when the leader departs.
- Proactive plans to "distribute" leadership ahead of the departure of the incumbent can increase the chance that the organization successfully navigates the transition.
- There are many ways in which people can be motivated to take on a portion of the distributed leadership of an organization—financial incentives may not be essential.
- A degree of isolation from the parent organization may be necessary for institutional innovation of this type to be able to succeed.

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Start-Up Investor Governance Case

by Robert M. LoBue
(Germany)

ESB Business School, Reutlingen University, Reutlingen, Germany
International Center for Corporate Governance, University of St. Gallen, St. Gallen, Switzerland

It was not until the early 1990s that the Mosaic internet browser made the World Wide Web broadly available to individuals, while in the preceding decade, an innovative California-based start-up designed and sold networking software that was used by large information technology (IT) installations to connect and communicate through the internet. In the classic Silicon Valley start-up manner, the founders of the company had raised money for investment from a United States (US)-based venture capital firm. They also implemented an employee stock option plan (ESOP) as a compensation incentive for the company's employees. As the company had achieved early US and international sales successes, the founders established wholly owned sales and service subsidiaries in Europe, and they also raised capital, less traditionally, from a United Kingdom (UK)-based unit trust.

But by the early 1990s, the founders ran into a serious rough patch in meeting their goals for financial results as well as for the quality of their financial reporting disclosures. They lost the confidence of the board of directors, and the board replaced the founding executives with seasoned industry managers. The new executive team was tasked by the board with three key parallel strategic objectives:

1. Restarting the company to return it to its innovative roots and to operating profitability
2. Sourcing new venture capital to back their new strategy
3. Leading an initial public offering (IPO), the ultimate Silicon Valley start-up experience

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Due to the company's financial difficulties, however, the ownership value of its private shares was significantly reduced to just pennies per share. This was much lower than the value the UK unit trust had paid for the shares in its block. In restructuring the company's equity, its old shares were replaced through a reverse stock split. Apparently, this contributed to a local legal imperative that required the trustee to directly distribute the shares of the software company previously held institutionally by the trust to the many individual investors in the trust, though the trustee did remain as investment advisor to these shareholders. On top of this, dozens of employees had left the company, and some of them had exercised their right to purchase the option shares that had vested to them in the ESOP. This led to the unique situation that a small Silicon Valley software start-up with just over 100 employees and less than US$30 million in annual sales found itself with close to 300 external individual shareholders.

A critical corporate governance risk came into play that threatened the company's ability to achieve its new mission. The Securities and Exchange Commission (SEC) of the US government serves to protect the rights of smaller investors from expropriation and fraud by unscrupulous company founders and overpowerful managers and majority owners. When start-up founders solicit an individual citizen for direct sale of shares in a private corporation, they must collect evidence that the buyer earns a relatively high annual income or possesses a substantial value of overall wealth according to SEC regulations (which are similar to the statutes in most other developed nations). These "accredited investors" are thought to be sophisticated and experienced in financial matters, therefore, able to withstand the risk of this type of investment.

If the company's individual investors were to lodge enough serious complaints with the SEC, the company's shareholder situation could come under a higher level of legal scrutiny that could trigger an investigation. The SEC would find that the company had no documents showing that the individual shareholders were accredited investors under the regulations. The regulator could decide that the prior actions of the founders and the decisions of the board had been prejudicial to the interests of the minority investors. As a remedy to protect the rights of the hundreds of current shareholders, the SEC could compel the conversion of the company's registration status from a privately held corporation to a publicly traded corporation.

This re-registration would subject the company to all of the burdensome regulations required of publicly traded corporations, such as detailed regulatory disclosure filings and public announcements of financial results as well as strategic decisions, risks, and threats. It would no longer be technically possible for the executives to call the sale of any future shares an official "IPO." Furthermore, the board of directors would have a difficulty in restricting owners from selling their shares in the over-the-counter (OTC) market, which could even lead to an unwelcome takeover by a competitor or corporate raider. This could put the company in a much worse situation with the burdensome costs of regulatory compliance but without the significant benefits of increased financial capital and brand promotional recognition normally gained by an IPO.

What Happened in Reality?

(To be communicated to the board seminar participants after they have discussed the case in small groups and have presented the results to the other groups)

The solution for keeping the shareholders satisfied so that the company could remain private until it could reach its objectives was found, apparently contradictorily, in the public company process realm. The finance team added standard "investor relations" regulated processes to its responsibilities. Most start-ups are so closely held in ownership, and that the large investors backing the company are represented directly by one or more of the elected directors on the board. Directors are direct recipients of management-supplied information. MSI includes financial reports and statements and formal board meeting discussions on regular schedules. Directors also communicate with each other and with management on an ad hoc basis. Just as the company's software engineers were recognized innovators in IT communications technology for their global customers, the finance director designed and implemented a measuredly transparent investor communications regime for the company, in order to engender trust with hundreds of disperse company shareholders.

- After each fiscal quarter, an investor packet was produced for board approval. The finance director supplied a commentary to the financial statements, summarizing the reasons for the results, especially in the categories of sales revenues, operating profits or losses, other gains or losses, cash flow, and business investments. The standard financial statements including profit and loss, balance sheet, changes in equity, and cash flow were also prepared for the packet. The approved packet was mailed by post to all of the shareholders.
- The finance director also took phone calls from individual investors and from the advisor to the shareholders of the former UK unit trust. The finance director had to be careful to restrict answers to questions related only to the company's quarterly packet and other publicly available disclosures and information about the company. Discussing any other items could have risked favoring or prejudicing one owner over the others, or information not yet approved by the board of directors could have been inadvertently disclosed.
- Each year, all investors were invited by the board of directors to the annual meeting of shareholders at the company headquarters. They were allowed to vote on any items under their rights as shareholders, either in person, by mail, or by proxy.

In the mid-1990s, the new management successfully raised an offer for a few million US$ in a private equity placement from a venture capital firm from the Northeast USA. The board of directors informed all shareholders of the impending issuance of this new tranche of shares and of the implications of dilution that this sale would have to their overall ownership. All shareholders were solicited to vote, and they overwhelmingly approved the transaction.

Does This Company Still Exist Today?

The company successfully achieved its IPO during the late 1990s dot-com stock market bubble, in the period former US Federal Reserve Chairman Alan Greenspan described as "irrational exuberance." During the subsequent downward technology

stock price correction, the company was acquired by a midsize publicly traded software company and absorbed into one of its many business divisions. And just a few years after that, the acquiring company was itself acquired by one of the world's top ten software giants who had an unfavorable industry reputation of purchasing rival companies, severely cutting employees and costs of new innovation, and then charging customers higher rates for software maintenance service for many years that followed.

What Can We Learn from This Case?

1. The board of director's and management's responsibilities to owners (shareholders) should be given top consideration at every stage of development of a company. Investors in companies have similar rights, needs, and expectations for fair treatment and transparency whether the company is a small private company or a major global corporation.
2. The currently favored trend of soliciting "friends and family" in an early round of start-up financing could be a two-edged sword. If everything goes smoothly, start-up founders can keep their friends and family relationships intact. If business goes awry, they may not only lose face with their closest allies; they may also find themselves being called to account facing federal government regulators. Having more individual shareholders increases the potential for some to become angry investors registering complaints with the SEC or even filing a securities lawsuit against the board of directors and executive officers.
3. When a company goes through a crisis, especially when that crisis is self-inflicted at the management board or supervisory board level, many unexpected and unwanted repercussions can follow. This could be called "corporate karma." The company had not solicited any of their owners illegally. Nevertheless, the company now had hundreds of individual investors, and there was no way to know whether or not any of them were accredited investors at the point of time they had acquired their shares. The risk was high because the nature and severity of the company's problems could be linked to the same founders who had also originally solicited investments from the unit trust and the employees.
4. The SEC generally defines "penny stocks" as shares in a company that trade for less than $5 in the OTC market, i.e., not in a registered stock exchange. Penny stocks have had a long history of investment fraud and abuse. During the period that the company was founded and restarted, there was a particularly significant level of fraudulent activity regarding sales and market price manipulation of penny stock companies that also involved organized crime. This led to new legislation enacted in the USA, the "Securities Enforcement Remedies and Penny Stock Reform Act of 1990." The SEC also allows that penny stocks could apply to certain private companies whose shares are not intended to be traded, which definitely could have included the company of this case study.
5. Enlisting new leaders to take over a turnaround situation will not be able to shield the company from difficult surprises carried over from past sins. Mature, experienced executives and board members with cool heads, warm hearts, and working hands will need to be called upon to avoid panic, build consensus, and construct solutions to the serious problems that will arise.

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NPO Governance Case

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The demographic shift (rise in average life expectancy and declining birth rate), together with changes in family structure and the recent economic difficulties facing many families, has increased demands on social organizations. These greater demands highlight the importance of social organizations in ensuring social cohesion and well-being. In addition, constraints on public expenditure mean fiercer competition for financial resources and greater difficulties in accessing these resources. Accordingly, some of the burden has fallen upon families to bear the costs of services provided by social sector organizations, which must seek alternative sources of financing.

CAJIL[1] is a nonprofit organization devoted to supporting the senior population in one of the largest parishes in the city of Lisbon (Portugal). Like many organizations that provide similar services[2], CAJIL must cater to the interests of a wide range of stakeholders, including users, CAJIL members, and the government. (1) Users are vulnerable individuals who require the services provided in CAJIL facilities or in their own homes. The amount these users pay depends on their income. (2) CAJIL members aim to provide sociocultural support for the population through CAJIL's work. (3) The government seeks the well-being of the population. Through social security services, the government establishes the rules and allocates the necessary financing to allow social organizations to function. In addition to these stakeholders, the highly specialized professionals who work in social organizations must also be considered. These professionals pursue the goals of career development, remuneration, and stability.

Founded in 1986, CAJIL has been gradually increasing its number of users and the number of services available to these users. The principal limitations in this regard are legislation governing CAJIL's operations and government funding. Since

[1]Center for support to young and senior people of Lumiar.

[2]In Portugal, private organizations in the social sector are generally small, which often means greater proximity to users, and directors usually participate voluntarily.

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1986, the leadership has mostly come from the current chair of the board of directors (either as chair or briefly as vice-chair). The chair of the board of directors is a university professor with extensive management experience, a strong orientation toward CAJIL's development and engagement from top managers and other employees, and wide recognition within the local community. CAJIL's board of directors, elected for 3-year terms, is formally constituted by five directors who carry out their duties on a voluntary basis. CAJIL's board, in particular the chair, oversees operations, the definition of strategic guidelines, including the selection and recruitment of top managers (technical manager, administrative and financial manager, and social marketing manager), and external representation, especially in matters related to social security services.

CAJIL's board of directors is currently implementing a large-scale investment project to build high-quality facilities while increasing the number of services (including services that are scarce in the city of Lisbon) and number of users. Implementing this project exceeds the length of a mandate, and the project's lifetime may exceed 50 years. To support this investment, CAJIL must have a governance structure that assures investors and the implicated public institutions that CAJIL—not just the current board of directors and chair—is capable of completing the project and responding to the management challenges associated with the increase in activity and complexity linked to this investment.

1 What Are the Main Causes of This Problem?

Because of the aforementioned issues, in recent years, the rotation of vulnerable users who access CAJIL's services has grown, although these users and their families are not involved in CAJIL's activities (e.g., participation in general assemblies). Therefore, despite the growing number of users, the membership base, which defines CAJIL's goals through participation in general assemblies and the board, has remained stable. The average age of members is growing, and the membership base is becoming decreasingly dynamic. The amount of time devoted by board members, in particular the chair, has steadily grown because of greater responsibility and breadth of activities, both of which are expected to increase in the coming years. CAJIL therefore increasingly depends on the current chair in operational matters and, specially, in terms of strategic issues. The chair also wants to ensure that his legacy lasts and that his decades of effort and dedication are not wasted.

2 What Do You Recommend to Solve This Problem in an Effective Way?

As well as implementing the project that is currently under development and conducting all other activities, the board should focus on the membership base, mobilizing members and targeting their involvement in CAJIL's activities. A larger

membership base for recruiting board members would enable the identification of individuals who are willing and able to perform their duties as directors, have management and social skills, and command prestige and recognition within the community—a necessary condition to ensure that activities meet users' needs. The board of directors should also create conditions to enable a gradual transition over the next 10 to 15 years, allowing the chair to act increasingly as an advisor to the remaining board members.

3 What Happened in Reality?

The board that was appointed in 2016 for a 3-year term has great diversity in terms of members' education, professional activities (economics, engineering, management, medicine, and nursing), and age, which ranged from 30 to nearly 70. In addition to the chair, the board has members who already have experience on CAJIL's board and others who are appearing on the board for the first time. The main aim is to equip younger members with the necessary skills and experience to ensure the continuity of ongoing activities and projects.

4 What Are the Most Important Lessons Learned from This Case?

Traditional governance mechanisms are not applicable to all organizations. For most nonprofit organizations, remuneration cannot be used to recruit directors who handle operational and strategic issues. Likewise, interests cannot be aligned through remuneration or equity ownership. Finally, although directors perform their duties on a voluntary basis, their professional reputation is under scrutiny. Therefore, their commitment and responsibility must be akin to their commitment and responsibility in professional, remunerated activities.

Unlike in traditional companies where shareholders have financial incentives to monitor company activity, in associations, all members have equal voting rights, so they lack obvious incentives to monitor activity. Consequently, the power tends to shift from the members to the board. Regular elections, however, mean that the board can easily be replaced, although replacing the board fails to guarantee the competence and commitment of the new board.

It is therefore important to stimulate the debate on governance of nonprofit organizations. Nonprofit organizations play a key role in society, so their governance is, by extension, crucial for society. Healthy debate over their governance can provide governance mechanisms that reconcile the voluntary nature of the board members with the dispersion of voting rights and the development of medium- and long-term strategies to ensure that these organizations meet their goals.

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Part II

The Board of Directors as a Direction Body

M&A Governance Case

by Martin Hilb
(Switzerland)

*International Board Foundation and its
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Jacques Ferrier, Chairman of the Board of M-Tec International, is concerned that the aftermath of a recent M-Tec acquisition is threatening to tear his board apart and cause considerable damage to the company.

1 M-Tec International

M-Tec is a high-tech computer company based in Geneva, Switzerland, with a post-acquisition turnover of CHF 320 million, 650 employees, and a 2002 listing on the Swiss stock exchange. The appointment of a new chairman (Ferrier) and CEO (Suter) in quick succession in 1998 proved highly beneficial to the company, and despite the tough market conditions prevailing in 2002, M-Tec shares have traded at values consistently higher than the listing price. The recent acquisition of a rival business of equal size with highly complementary products and markets resulted in an additional, positive movement in the share price.

See Martin Hilb: "Corporate Governance," 5th Edition, Springer Heidelberg/New York 2016, p. 68–71.

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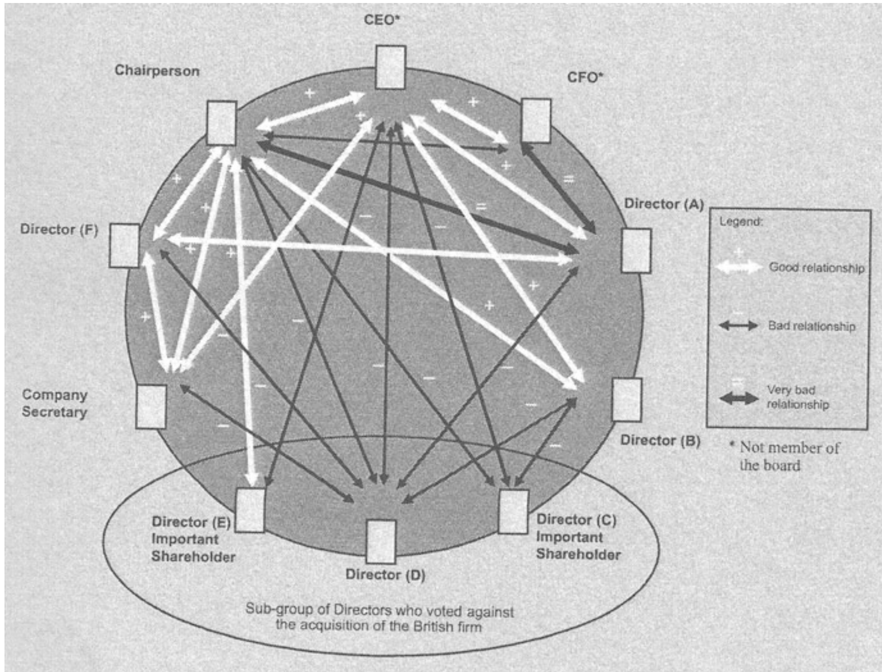

Fig. 1 Current situation

2 The Conflict (see Fig. 1)

Despite the positive performance, however, a major challenge has arisen at the board level. The recent acquisition caused a division of the board into two camps. The chairman, the CEO, and the CFO supported the acquisition. They acted on the advice of a lawyer specialized in business law who studied the acquisition in some detail and who indicated that the acquisition could bring positive value for M-Tec.

Three directors opposed the acquisition based on their conviction that the costs of integrating two companies are frequently underestimated and that the purchase price was therefore too high. All three directors opposing the acquisition were important shareholders in the company.

In order to make the acquisition decision under intense time pressure, the seventh director—himself a pioneering entrepreneur—received a call while on a trip in the United States. He supported the acquisition based on the threat of losing the opportunity to another rival company.

After the split vote, a serious tension became apparent between the two groups of directors. In every meeting, the CEO and board members supporting the acquisition

were challenged with questions about the decision, and they felt the attacks to be unjustified.

One board member opposed to the acquisition was particularly critical, and his comments appeared to provoke emotional reactions that threatened the board's ability to function in the best interests of the company.

3 The Leadership

Jacques Ferrier (65) has an impressive track record as a pioneering entrepreneur. He began his career as an apprentice in a bank and obtained his A levels and then a degree in economics from the University of Neuenburg, Switzerland. He held various sales, marketing, and management positions in an international commercial enterprise with its head office in Lausanne and branches in Rio and New York, and then, at the age of 35, he decided to open his own logistics company. Within 20 years, he succeeded in building up a concern with an annual turnover of CHF 250 million and 480 employees in 8 companies in 8 different countries.

As his two daughters took no interest in the company, he sold his concern to a big German group on good terms in 1998. That same year he took up the position of Chairman of the Board of Directors at Banque Regionale Vaudoise (BRV) in Lausanne and became a member of the board of directors at M-Tec International.

During the first board meetings at M-Tec International, Ferrier was exposed to the unprofessional leadership by Chairperson and CEO, Jean Marmier. When Marmier was dismissed by the three families owning the greater part of M-Tee International, Ferrier was asked to take over his position.

Ferrier undertook two major tasks in his first months as chairman and CEO. He appointed an American consulting firm to do a comprehensive analysis of the company. The results of the consulting analysis were sobering. He also asked an executive search firm from Geneva to find a new CEO. His search led him to Dr. Marc Suter within just 3 months. The company was now back on track again.

Suter graduated with a doctorate in informatics from the EPFL in Lausanne and an MBA from the IMD in Lausanne. After his graduation, he established a successful career with an American producer of computer hardware with offices in Zurich, New York, and Tokyo and finally became director for Central Europe. As part of the executive search process, Suter was given the opportunity to study the consulting report into the state of M-Tec. He was fascinated by the results and convinced the search consultants that he would be able to effect fundamental changes in M-Tec. In fact, over a period of 3 years, and in cooperation with Ferrier, Suter turned the company into a successful high-tech business.

4 Problem Analysis

Ferrier's concern about the viability of the board has led him to contact you for advice on how the conflict should be managed. He has assured you access to all the board members. Through preliminary discussions with both board members and top

managers, the following illustration of relationships among the company leaders has been generated.

1. What are the main challenges facing the board?
2. What would you recommend that the Chairman of the Board propose in the next annual general meeting?

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Check for updates

Family Company Direction Case

by Christoph Maier
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Peter and Richard Schmidtman have been sport enthusiasts for all their lives. Growing up in rural Bavaria in the 1960s, they loved the mountains and every outdoor discipline that came with them.

They were both excellent skiers, Richard even being crowned German champion in the 1962 downhill race. They spent many days and nights together in the Alps, climbing, hiking and trying out all sorts of fancy innovations such as paragliding, mountain biking and abseiling (even though it wasn't called exactly that at their time). They were as close as brothers can be.

After graduating from school in post-war Germany, they earned their money with piece jobs. They were both very good with their hands and popular as builders, carpenters and even mechanics.

The economic boom of the 1960s, the growing market for sports gear and their knowledge of outdoor disciplines provided them with a lifetime opportunity. In 1964, with their rather meagre savings, a little loan from their parents and plenty of passion, they founded "Outdoor Champions"—a little sports retail shop in the basement of their parental home in their small village.

"Outdoor Champions" was a success from the start. In its early years, it catered mainly for the skiing community of the area. Richard was known in skiing circles. He was trusted on his expertise and managed to get excellent deals from his suppliers. Peter became an expert on cycling and other disciplines. Soon, the basement was too small, and the Schmidtmans received a bank loan to build a specialist store in the next bigger city. "Outdoor Champions" grew from strength to strength. In less than two decades, the shop became the "go-to" place for outdoor aficionados within a substantial catchment area.

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Peter and Richard loved their lives. Their hobby had become their profession. They happily worked 16 hours a day, serving their customers on the job floor during opening hours and doing the paperwork at night. Even after employing more than 20 staff and having solid savings in their bank account, they continued to run their business well into retirement age. They proudly watched their sons—each of them had two—following in their footsteps. After completing apprenticeships and college schooling, all four joined the company and worked in rather loosely defined roles, doing whatever was needed.

The sons were different characters though. Staff, business partners and discerning customers could increasingly pick up that the respective brothers were of slightly different stocks. Whilst they all pulled their weight and came to work early and dutifully, their styles and contributions differed. Peter's sons were more the quiet, diligent types, whereas Richard's sons were more boastful, outgoing and sometimes brash. They did not like the less glamorous parts of the job. They lacked the meticulous approach of getting to know new products and brands and tended to be quick in their judgements. Since they had many friends and a good network, they would sell well anyways and saw no need for the more thorough and laborious approach of their cousins. Also, there were not really into repairs and maintenance and preferred lucrative, quick sales. As much as they resisted it, the pairs of brothers drifted apart and started to become resentful of one another.

Probably, Peter and Richard saw it coming early. Yet, they let it happen until one night they agreed to go to their mountain cottage for the weekend and sort this situation out, once and for all. They promised themselves to return with a succession and ownership plan for their company.

What would you recommend to Peter and Richard?

1 What Happened in Reality?

(To be communicated to the board seminar participants after they have discussed the case in small groups and have presented the results to the other groups)

Once Peter and Richard reached the tranquillity of their getaway, they sat down to talk. Without much discussion they arrived at a common understanding of the following fundamental points:

- There is no way that their four sons can remain in and even run the business together. There have been latent tensions and various incidents of friction that the fathers had generously overlooked and probably downplayed. No matter what hierarchies, structures, systems and procedures the fathers would put in place, there will never be an inclusive, constructive and shared organizational culture that would be embraced and lived by the four cousins together.
- The glitches between their sons might not have affected the bottom line of the company yet. In fact, the last years have been excellent years for "Outdoor Champions". However, this will most likely change if the current dynamics remained unresolved. Their gut feeling told them that their business model is under threat.

- The unique selling point (USP) of "Outdoor Champions" has always been the personal touch of the founding brothers and their families. Customers flock to the store because of the knowledgeable, personal and honest service, as well as the anecdotes and storytelling that go with it. For most customers, purchasing at the store without talking to one of the Schmidtmans is inconceivable. Besides, all four sons love the business and are motivated to work in it. Hence, the company should stay in family hands and not be sold or handed over to an external chief executive.
- There is no point in conducting direct and explicit performance appraisals of each of the four sons. With the fathers still present, none of the sons had a clearly defined leadership position. The way the business has been run led to many overlaps in functions and tasks and did not incorporate key performance areas that the individuals could be evaluated against. Obviously, however, both fathers had their personal opinions on the performance of the offspring. They knew these opinions might be biased, but they also knew that sharing them in a transparent forum wouldn't help and most likely cause futile hurt. There must be another, more elegant way of resolving the way forward.
- For both brothers it is time to retire no matter who will be chosen to run the company. They had a great innings and achieved more than they ever dreamed of. Most importantly though, they still respect and love one another deeply. It is a good time to quit.
- Their passion for sports and nature, as well as their business, has always been their very personal, emotional and mutual affair. They always felt they knew best, and they appeared to be right throughout. This dilemma shall therefore be solved by them alone.

Based on that understanding, the brothers agreed that they need to decide which family side, or which pair of brothers, should take over the company. They came up with a very simple plan.

Each brother shall take a little piece of paper and write on it the price he is prepared to pay for the 50% stake that the other brother owns. They will then exchange their papers and open them. The higher price will win. In other words, the brother who offered more will buy the shares from his brother at this exact price. On Monday they will go to the notary to execute the deal.

The brothers each thought about the price for the rest of the day. At dawn on Sunday morning, they had coffee and exchanged the papers. They opened them, hugged, smiled and started their mountain tour together.

Upon their return all provisions were made. The more meticulous, soft spoken and diligent brothers took over the management of the company as Peter had offered more than Richard. Observers, particularly the ones with business savvy, marvelled about the quiet and seamless transition and the fact that the seniors had managed to hand over the business to the "right" set of brothers without any noticeable disruption. Employees were surprised and relieved about the outcome. They would have chosen the same leadership, had they had a say, although they would have preferred that the seniors stay on longer.

Peter's sons worked harder than ever before. They continued in the spirit of their father and uncle. Once, in a moment of exhaustion and weakness, one of them uttered something of "many years of hard work necessary to pay for the shares". Most people actually only heard much later that Richard had sold to Peter.

Richard's sons soon took up jobs in marketing and sales at other companies. They did not have to worry about money and had exciting social lives pursuing various interests, mainly in sports. They remained close to their cousins and would strictly buy all their gear from "Outdoor Champions".

"Outdoor Champions" to this day remains the most successful privately owned retailer in the area by far. Peter and Richard continue to explore the Alps together. Both reached a ripe old age.

2 What Can We Learn from This Case?

1. Be yourself and have courage.
2. When it comes to decisions of ownership, leadership and family, it is good to be quick and decisive. A lengthy process involving lots of people, complicated structures, procedures and bureaucratic protocol can often be detrimental, damaging personal bonds and the reputation of business and family.
3. Great solutions are usually simple. We often lack the courage to commit to them, especially when they are unconventional.
   In this illustrative case, Peter and Richard committed to a simple, unconventional and courageous decision. This way they:
   - Resolved the situation creatively and decisively with minimal noise and cost.
   - Salvaged family unity by taking all responsibility upon themselves and allowing the juniors to save face and remain friends.
   - Made sure that their legacy is preserved in the best possible way.
   - Motivated the new bosses and allowed the business to prosper.
   - Maintained and even grew their love and respect for one another.
4. Have a strong inner scorecard for yourself, your children and family members. From what happened it is clear that both, Peter and Richard, knew accurately which pair of brothers is more suited and shall lead the company. Peter had to make sure his sons get the business. Richard had to get an excellent price so that he could validate his exit and "sell" it to his sons.
5. Since they both worked off the same, strong inner scorecard, their plan worked well.
6. Understand your USP.

Peter and Richard also made mistakes. They should have been more cautious of introducing their sons all at the same time. They should have insisted on clearly defined positions, job descriptions and performance goals. They could have thought about succession planning earlier. However, the moment they sensed that the USP of "Outdoor Champions" is under threat, they stepped in quickly and decisively.

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University Direction Case

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1 Definition and Background

This chapter aims to contribute to the university governance literature with a living case from Bahçeşehir University. The case is supported by the agency and stakeholder theory and the shared university governance models, such as Academic-Business-Corporate (ABC) of University Governance and the Integrated New University Governance (reversed KISS framework). The ABC of University Governance model is a division of resources among academic, business and corporate boards (Carnegie & Tuck, 2010). The framework of reversed KISS stands for 'Situational, Strategic, Integrated, Keep it Controlled' (Hilb, 2012). The shared or integrated governance concept was developed based on stakeholder theory, which shifts the panoptic (shareholder) view to a panoramic (stakeholder) vision (Pesqueux & Damak-Ayadi, 2005). This chapter helps the governing bodies and management authorities in tertiary education gain a deeper understanding of the governance models and evaluate their existing governance structure in the higher education institutions (HEIs).

2 Information on Bahçeşehir University

Bahçeşehir University (BAU) consists of Bahçeşehir University in Istanbul, Turkey (BAU Istanbul) and Bahçeşehir International Universities (BAU Global), such as one in the USA (Washington D.C.), Germany (Berlin), Georgia (Batumi) and the

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Northern Cyprus (Nicosia) (BAU, 2017a, 2017e). These four private universities abroad, collected under BAU Global umbrella, are independent; they have their own rectors, yet they have one shared board of trustees (BAU, 2017c). However, in this book chapter, the university governance structure of BAU Istanbul is analysed in detail.

In 1998, BAU Istanbul was established as a foundation university (FU) by the Bahçeşehir-Ugur Education Foundation. The founding chairman of BAU, Mr. Enver Yücel, is a successful education entrepreneur (edupreneur). BAU Istanbul consists of nine faculties, three graduate schools, one school of languages and two vocational schools. It has 3 campuses, 22,446 students and 1047 faculty members. The university provides more than 100 programs. It aims to be ranked among the top 500 universities in the world by the year 2023. The governing bodies of the university are very good to respond the needs of the twenty-first century, such as digitalization, innovation, entrepreneurship, virtual education, machine learning, cybersecurity, data mining and big data (Ince, 2016; Yalçin, 2017). For the entrepreneurship, BAU in Turkey has the incubation centre in Istanbul, and BAU Global has the centre in the Silicon Valley, USA (BAU, 2018b, 2018c). These centres guide their students to be an entrepreneur and start-up their own companies.

3 The University Governance Structure of the Bahçeşehir University in Istanbul (BAU Istanbul)

Brown (2001, p. 91) expressed that 'the successful universities do have a very successful and strong governance structure'. In this section, BAU Istanbul's unitary governance structure is analysed according to the ABC of University Governance and the holistic and integrated reversed KISS framework (New University Governance). These two concepts are explained and implemented in the living case.

As shown in Fig. 1,[1] the governance organs of BAU Istanbul encompass the following bodies: (1) board of trustees (BOT), (2) rector's office (rectorate), (3) board of directors (BOD) and (4) Senate.

The board of trustees (BOT) is the highest decision-making authority; it represents its legal entity and includes a minimum of seven members. The main duties of the BOT are to direct and control the university, appoint the rector after obtaining the affirmative opinion of the Higher Education Council (YÖK), approve the university budget and monitor its implementation and to make the final decision regarding the resolution of conflicts between various bodies of the university. As of 2018, the seven members of BOT are made up of two internal members (founding chairman and the rector) and five external members with diverse backgrounds. The chairman is elected among the members of the BOT. Each member is appointed for

[1]The figure was derived from Hilb, M. (2012). *Integrierte Governance von Universitäten*: Haupt, p.36 and implemented to the case. In the unitary board system, rector is also the members of university board and Senate, which is opposite to dual board system.

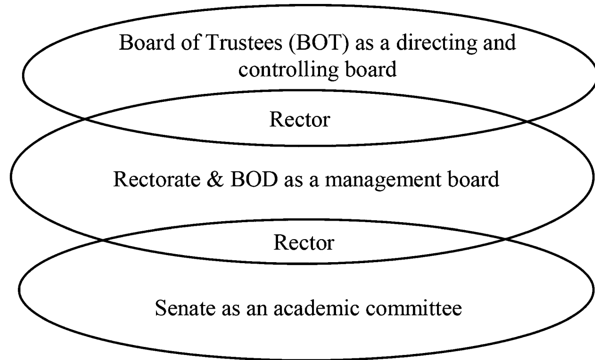

Fig. 1 BAU Istanbul's unitary governance structure

4 years, and they can be reappointed by the chairman. The BOT has to be gathered biannually, and the majority of the members must have a bachelor's degree (BAU, 2018a).

Rectorate (rector's office) is the executive or the management board of the university, and rector is the president of it. The BOT appoints the rector by a plurality of the vote for 4 years. He can be nominated again after completing the period of duty. The rectorate consists of six people (rector, vice-rectors and advisors to rector). The rector and vice-rectors must be a full professor, but the advisors do not necessarily have to be academic. Instead, for instance, the rector's advisor in charge of marketing and communication is a professional who has an expertise in journalism, media and communication. *The board of directors (BOD)* is the authority to assist the rectorate for the executive and administrative matters. The BOD has 13 members with voting rights: the rector, who is also the president of the BOD, the deans of 9 faculties and 3 elected full-time professors at BAU (BAU, 2017b, 2017d; Yalçin, 2017).

The *Senate* is the academic organ of the university, and it gathers at least biannually—the beginning and end of the academic year. It is the organ in charge of the academic decisions and their implementations (BAU, 2017b; Yalçin, 2017). The Senate consists of 27 members with voting rights (rector, vice-rectors, deans of 9 faculties, elected academics, leaders of the institutes, vocational schools and school of languages) and 2 members as an observer, no voting rights (the president of the student council and secretary-general) (BAU, 2018a).

In short, BOD and Senate include only academics working in the university. In line with the unitary (monistic) governance structure, as seen in Fig. 1, the rector is the president of three committees—rectorate, BOD and Senate—and the member of the BOT. The rector acts as a mediator among academic, business and corporate boards. Consistent with the agency cost and information asymmetry assumptions of the agency theory (Eisenhardt, 1989), the unitary governance structure of the BAU Istanbul is advantageous for the stakeholders because the rector can bring university related know-how and information to the BOT, so it decreases the information asymmetry and agency cost. To cope with the disadvantages of unitary board structure, BAU Istanbul has addressed check and balances and conflict of interest

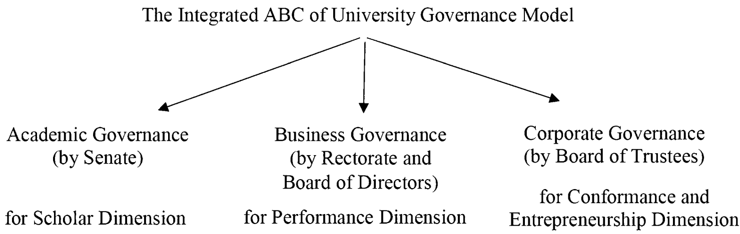

Fig. 2 The BAU Istanbul's the ABC (Academic-Business-Corporate) of University Governance structure

by not allowing the rector to be the chairman of the BOT and by not involving the rector in BOT's meeting when they discuss the issues related to the rector. As a result, it can be concluded that BAU Istanbul's unitary governance structure is successfully implemented and managed.

From the perspective of the ABC of University Governance model, BAU Istanbul has three organs which fulfil the academic governance, business governance and corporate governance as seen in Fig. 2.[2] In other words, BAU Istanbul has integrated/shared or amalgam model which considers the whole stakeholder's interests. Furthermore, the BOT is an entrepreneurial board where various entrepreneurial and innovative decisions are taken and where the incubator centres and the programmes addressing the needs of the twenty-first century are initiated. Therefore, the BOT is a great example of 'corporate university control-preneurship', which was defined as 'controlling, directing, and entrepreneurial board' by Hilb (2009).

From the aspect of New University Governance, Hilb (2005, 2006, 2012) proposed reversed KISS framework articulated into four parts:

Keep It Situational (S) It indicates context dimension that depends on institutional theory. There is no 'one-fits-all' approach available. University governance structure should be modified by considering internal and external contexts (Hilb, 2012). For instance, the governance structures in the examples below should not be the same:

Public University ≠ Foundation University ≠ Private University
Big Scale University ≠ Small-Scale University
Local University ≠ Global University

BAU has differentiated its governance structure by considering the external and internal contexts. For example, its university governance structure is different from the ones at public universities and local universities. BAU Istanbul is way bigger in size than the size of BAU Global universities abroad, and the ambition level of the

[2]Prepared by the author by deriving the concepts from Carnegie, G. D. and Tuck, J. (2010) 'Understanding the ABC of University Governance', *Australian Journal of Public Administration*, 69(4), pp. 431-441, and Hilb, M. (2012). *Integrierte Governance von Universitäten*: Haupt, p.15

BOT at BAU Istanbul is higher than the one at BAU Global. BAU Istanbul is a foundation university; BAU Global consists of private international universities. Therefore, BAU has *kept its university governance situational* (-S) by having two different BOTs for BAU Istanbul and BAU Global, in other words, BOT of BAU Istanbul $\neq$ BOT of BAU Global.

Keep It Strategic (S) It is for strategic direction based on stakeholder theory. The strategic development is a central function of the board, and the board should include competent and exemplary members who act as a role model for both share- and stakeholders (Hilb, 2005, 2006). In our case, the BOT of BAU Istanbul does not act only as a supervisory board, but it also directs, controls and takes strategic decisions. Moreover, the founding chairman selects the members based on their competence. As of 2018, the BOT of BAU Istanbul includes five external members in addition to two internal members (rector and chairman). Mr. Enver Yücel, the founding chairman, and his son (Mr. Ömer Yücel), who will be the prospective chairman, are currently the member of the BOT (Yalçin, 2017). The members have a diverse background, such as politician and professionals from finance.

Keep It Integrated (I) It is related to board management that is derived from resource dependence theory. It means the integrated and targeted selection, appraisal, compensation and development of the board (supervisory board) and the rectorate (managing board) (Hilb, 2012). Consistent with the unitary board structure, at BAU Istanbul, the rector is sitting both in the BOT (supervisory board) as a member and in the rectorate (managing board) as a president, which helps the integration, evaluation, appraisal and compensation processes of the personnel. On the other hand, the rector is not allowed to attend the BOT meeting when they take the decisions about his assessment and compensation. The founding chairman evaluates and assesses the members of the BOT, and their reappointment is depending on their appraisal and evaluation.

Keep It Controlled (K) It is about the strategic control direction built upon agency theory. This dimension is regarding the monitoring and risk management functions of the board. It indicates holistic monitoring of the results from the perspective of stakeholders including shareholders, government, students, alumni, academics, researchers, staff, corporate partners/professionals and the public (Hilb, 2011, 2012). The BOT of BAU Istanbul does also act as a risk committee and takes strategic decisions in the high-risk environment. Risk management is a very important role of BOTs for the global FUs operating in the emerging markets. For instance, although Turkey has experienced unstable economic conditions in the passing years, the BOT of BAU Istanbul has coped with the external risk factors very well due to its successful risk management strategies, so the financial bottom line, education quality and the number of international and national students have not been negatively affected (Yalçin, 2017). For the holistic monitoring, most of the stakeholders are represented in the government bodies of BAU Istanbul. For instance, the appointed practitioners and politician and elected academics and student representative are

involved in the university governance of BAU Istanbul. They aim to bring the expectations of the stakeholders into the Senate or boards to be discussed and fulfilled.

4 Questions

- What are the main strengths of the university direction in this case?
- What do you recommend as areas of development in this case?

5 Discussion and Conclusion

The unitary governance structure of BAU Istanbul is a good example of the ABC of University Governance and the reversed KISS framework (New University Governance model), and it was built upon amalgam governance approaches. Amalgam governance means integrated or shared governance, which includes all of the following governance forms in Fig. 3:[3]

On the other hand, for the areas of development in this case, first, the role of the BOD at BAU Istanbul is assisting the rector in the administration and management decisions and duties (BAU, 2018a). It sounds similar to the management board. The BOD shall be renamed as management board. Second, in addition to the existing members in the BOT of BAU Istanbul, one or two more independent/external members who excel in financial management in the private institutions and corporations shall be appointed to the BOT, so it may help the university to be managed as a university business and increase its income (the financial bottom line) even though making profit is not the main driver of the foundation universities. As Rowlands (2014, p. 273) stated, 'Being an academic leader and doing university

Governance form	
Faculty Governance	→ through Senate
Managerial Governance	→ through Rectorate and Board of Directors (BOD)
Governmental Governance	→ through Higher Education Council (YÖK)
Business Governance	→ through business representatives (practitioners) at BOT
Independent Governance	→ through external members at BOT
Trustee Governance	→ through the Board of Trustees (BOT)
Stakeholder Governance	→ through shareholder/founder, rector, researchers, academics, student council president, politician, professionals in the governance organs of BAU Istanbul

Fig. 3 Amalgam governance of BAU Istanbul

[3]The figure was derived from Hilb, M. (2012). *Integrierte Governance von Universitäten*: Haupt, p.31 and implemented to the case.

leadership are not the same thing (academic leader versus executive leader)'. The contemporary business university governance has more generally shifted to managerialism. 'In the managerialism, the focus is on professional management, performance, management by results, value for money and closeness to the customer or market' (Rowlands, 2014, p. 265). It is believed that the involvement of independent business experts in BOTs shall provide universities with long-term success and benefits. Third, most stakeholders are already involved in the government organs of the BAU Istanbul. For instance, student council president is the observant in the Senate, yet he/she does not have a voting right. It is important that all stakeholders be equally represented in the government organs of universities according to the stakeholder theory. Therefore, it shall be a good idea to appoint the student council representative as a member with voting right in the Senate. Fourth, alumni and public, such as the family members of the students or any interested parties in the education of the university, are not represented in the government organs of the university. For instance, INSEAD Business School and London Business School have an advisory board (Alumni Board or International Council) that includes alumni from various countries and board members or CEOs of international companies. The main objective of the advisory board is to offer innovative advice and dynamic perspectives to fulfil the expectations of the stakeholders. They gather either quarterly or biannually (Hilb, 2012). It is suggested implementing the same concept into BAU Istanbul by setting up an advisory board that is independent of other governing bodies of the university. Fifth, as Hilb (2012) mentioned in his New University Governance model, for the bigger universities, integrated HR committee is suggested to be established to involve in the nomination, evaluation, appraisal and compensation functions of BOT and rectorate. It may also be a good idea for BAU Istanbul to establish HR committee. On behalf of transparency, the assessment and evaluation procedures of the BOT shall be described in the by-laws of the university. Last of all, the CVs or the brief information of each board of trustees should be available to the public on the web page of BAU to increase the transparency and to highlight the level of diversity and independence.

6 What We Have Learned from This Case

1. We have learned the holistic (network or integrated) and New University Governance concepts in the twenty-first century: the ABC of University Governance and New University Governance (integrated reversed KISS) frameworks, which are opposite to traditional top-down approach, e.g. a German chair-based organization system.
2. BAU Istanbul's unitary governance structure is a good example of the ABC of University Governance and New University Governance models. Its long-term academic and financial success mainly depends on the stakeholder (shared governance) approach and the fulfilment of the needs of stakeholders. It proves that 'the successful universities have a very successful and strong governance structure' (Brown, 2001, p. 91). BAU Istanbul's governance structure would be a

good benchmark for the foundation universities which are comparable in the external and internal contexts (keep it situational).

3. There is no such thing as 'one-size-fits-all' model of governance. The governance problems may be comparable in different tertiary institutions. The need is to avoid replicating bad practice while trying to benchmark good practice. Good university governance also does not simply happen. It requires boards of governors to recognize when a governance model is not working and to question why it is not working and how to repair it (Trakman, 2008).
4. The art of being a successful chairperson is to have his/her nose in but her/his hands out (Hilb, 2012).
5. The management in HEIs may refer to the insights and suggested governance models in the book chapter to analyse or improve their university governance structure.

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Check for updates

Board of Directors as a Strategic Sparring Partner

by Roman Lombriser
(Switzerland)

FHNW, Forrer Lombriser & Partner AG
International Center for Corporate Governance

"Light-Tech" is a traditional SME in Northwestern Switzerland. Its major activities are developing and producing luxury lamps for home and office applications. During the last 20 years, the company has been able to establish itself successfully in the high price segment, focusing mainly on traditional lamp technologies such as incandescent light bulbs, compact fluorescent lamps, and energy-saving halogen bulbs.

The emergence of light-emitting diode (LED) lamps poses a possible major threat to the SME.

LED lamps are based on semiconductor material using protons generated as the source of the light. Major new skills and competencies, together with significant investments, would be required to compete successfully in this new segment.

As a preparation for the annual strategy review with the board of directors, the CEO together with his management team updates—as usual—the SWOT matrix. In the threat quadrant, the team mentions the new technology; however, in the strategy proposal for the next 3 years, the managers consider a forced investment in new energy-saving lamps based on the traditional technologies as more urgent and promising.

In September, the board of directors and the top management team met for a 2-days strategy seminar off-site. The chairman and several of the other directors, who all were experienced strategist and successfully led several companies for many years, had bad feelings about the issue of technology replacement. Contrary to the top management team, the board of directors were not convinced that the break-through of the new LED technology in the market was still far away.

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Preparing for the September seminar, the chairman was wondering how to lead the strategy discussion without demotivating the management team by imposing too strongly his view on the executives while at the same time fulfilling the obligation of warning top management about critical threats.

Question: What do you recommend the chairman to do to solve this issue in an effective way?

1 What Happened in Reality?

Together with the executive team, the board of directors performed a scenario analysis for about 3 hours. In this analysis, the team varied two main external drivers of change:

- **Customer acceptance of the new technology:** very fast vs. gradual vs. slow adoption of the new LED technology by the main customer segments
- **State-funded financial subsidies** for the new LED technology: high vs. medium vs. low (as today)

In the subsequent evaluation, the board assessed the likelihood for the most probable scenario, the "gradual change scenario" at around 50%. The more pessimistic scenario (fast acceptance of the new technology, strong funding by the government) received a probability of still 30%. The following discussion of the implications in the case of the pessimistic scenario becoming reality revealed that the company could not afford the risk of not preparing for this threat.

The board requested the top management team to formulate a precautionary strategy which much better prepares the SME for the pessimistic scenario. Four months later, in the January meeting, the board approves a plan, submitted by top management, that asks for a continued investment in the traditional energy-saving lamps, yet not with as much funding as the top management team was originally planning for. Instead, the plan also included measures to push the implementation of the new business segment for LED products, in cooperation with an external partner.

2 Results

- Two years later, the pessimistic scenario reveals itself as reality. The replacement of the traditional products by the new LED technology occurs much faster than most top managers expected.
- Thanks to the more robust strategy as consequence of the collective scenario analysis, the SME can establish itself successfully in the new LED segment.

3 Key Lessons Learned

- By performing a scenario analysis together with the top management team, the board of directors were able to play an important role as strategic partner, without interfering too much in operative details ("constructive sparring partner").
- Developing different scenarios of the future and coming up with possible strategic answers can help to prevent dangerous "one-way strategies" and opens up the strategic perspectives of both the board as well as of top management.

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Part III

The Board of Directors as an HR Governance Body

Check for updates

Reward Governance Case

by Rolf Dubs
(Switzerland)

University of St. Gallen
International Center for Corporate Governance

At present a lot of writing takes place about sustainable management (ESG, environmental, social and governance issues). But many members of the supervisory board still have a hard time to deal with it.

The supervisory board of an enterprise in the food sector with approx. 1500 employees was represented by president and 6 members, of whom a woman had the following agenda item on their spring meeting—**annual financial statement**:

4. Acceptation of the annual financial statement:
   4.1 Discuss the financial report and the management letters from the auditing firm.
   4.2 Request to the general meeting about the distribution of profits.
   4.3 Discuss the distribution of bonuses, proposed by the corporate management.

1 Target: Resolution

Turnover and profit were way beyond the conservative budgets of the previous year.

Whereas paragraphs 4.1 and 4.2 did not provoke any discussions, paragraph 4.3 led to a lengthy and fierce discussion which evolved as follows: The HR manager

Reference: Dubs, R. (2015). Normatives Management (normative management). A contribution to sustainable corporate governance (3rd edition). Bern: Haupt.

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explained the process of officialized bonus determination and substantiated the proposed solution. Contrary to the processing of this topic in previous years, Carl Müller demanded the word and asked:

> How many of the 1500 employees will receive a bonus this year?

After an instant of hesitation the HR manager announced that 60 cadre employees, including corporate management, would benefit thereof. Following that, Carl Müller proposed a motion to comprehensively revise the bonus regulations for the years to come and if good profits occur to provide bonuses for all 1500 employees. He argued as follows:

> We have to perceive social responsibility, enterprises should—within their means—contribute to a reasonable social compensation—In other words perceive social responsibility and provide fair potential earnings for all employees.
>
> This means to concede bonuses to all employees, then they all contributed to the success. Furthermore the existing understanding of bonuses fosters the society separation in elite—which sets itself progressively apart—and the simple folks; this is on the long run a dangerous trend. For this reason the bonus policy has to be scrutinised.
>
> We would be badly mistaken to believe that we would have done enough for sustainable governance with our environmental measures and thoughtful sponsoring.

Two of the executive directors reacted quite fiercely: One meant that the enterprise would already invest substantially for a good working atmosphere, which would contribute much more significantly to success than “a little more money for the employees”. The second relegated to the legally required compliance with minimum wages, which the company—in spite of cost trends—since years would fulfil in an exemplary manner. For this reason our company perceives the social responsibility sufficiently clear.

Which opinion would you represent on the Board of Directors and what would be your reason?
And how would you vote on the application?

2 What Happened in Reality and How Did the Vote Turn Out?

- The motion was passed unanimously. It was most supported by the vote of a board member who unexpectedly asked how the individual members of the Board of Directors would finance the non-resident study of a child, with a minimum wage of CHF 4000. This remark led to some embarrassment for individual members. Another member was surprised because he had never dealt with such a question at a board meeting.
- The corporate management immediately started work on the new regulations. In doing so a challenging problem occurred: How can incentive pay be distinguished

from bonuses—particularly in case of employees without executive functions—as undifferentiated compensations would lead to social injustice between "highly performing employees" and "minimalists".

- The following options were discussed amongst the Board of Directors:
  1. General elimination of the bonuses, as it is scientifically proven that bonuses are not a significant motivational factor.
  2. A general, appropriate increase of cadre wages, because a wage differentiation by cadre level is taken for granted. The bonuses are distributed proportionally to all working groups of all levels as a total amount—with the task to decide on the distribution to their group members autonomously. In this way, the "high performers" can receive a little more, whereas the "minimalists" in the following year rather will strive for better performance, as attempts with this wage plan have already proofed.

The decision is still pending.

3 What Can We Learn from This Case?

1. Procedural: One should refrain from spontaneous applications to the board meeting, unless one is also willing and/or able to present feasible ideas for implementation.
2. In view of the many problems and conflicts of aims in today's corporate governance and its implications for corporate and social development, normative management (sustainable corporate governance) must be incorporated into strategic thinking in boards of directors.
3. Unlike many board members, corporate management is now increasingly interested in normative management, but does not dare to implement it in because many members of supervisory boards are not yet involved in it and/or they fear resistance of shareholders. Without the role model of the Board of Directors, the combination of strategic and normative management often fails.
4. The consideration of normative management, which—besides environmental issues and sponsoring—must also include social issues and governance, should not be dismissed as a "social visionariness", but its implementation should continue to give due weight to the economic issues. Honest economic constraints remain a limitation of many normative management ideas. However, a paradigm shift should be achieved, which I no longer focus on the short term, ruthless principle of profit maximization but on the goal of a profit under constraints.

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Succession Planning Governance Case

by Martin Hilb
(Switzerland)

International Board Foundation and its
International Center for Corporate Governance

Michael Miller is the founder of a successful international high-tech company in the medical field. His company operates worldwide and has annual sales of 910 million Euros. The headquarters is located in Zurich, and total staff includes 3500, 90% of which are outside Switzerland.

In 2002, Michael Miller's company was successful in acquiring Phamtex International, another family-owned company, headquartered in Fort Worth, Texas.

Phamtex was the biggest competitor with similar sales and headcount figures. The owner had no successor and therefore wanted to sell the company.

Miller offered the CEO position for the new merged company to John Kennedy who was the successful former CEO of Phamtex.

Kennedy accepted the offer under the condition that he remained in Fort Worth and suggested to manage the organization 1 week from Fort Worth and 1 week from Zurich.

Miller agreed with this and the merged company continued to be very successful.

Suddenly, Michael Miller realized that he had no successor for John Kennedy in case of his leave. This was a great risk, because it takes at least 1 year for an outsider to get familiarized with the sophisticated high-tech products of the company.

Michael Miller asks for your advice. What would you recommend to him?

See Martin Hilb: "New Corporate Governance", 5th Edition, Springer Heidelberg/New York 2016, pp. 88–89

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Owner–CEO Collaboration Case

by Elena Szederjei
(Switzerland)

CND, The Swiss Data Center
International Center for Corporate Governance

1 The Pros and Cons of an Owner–CEO Combination

The entrepreneur Alexander Manberg founded and successfully developed an IT company over 30 years ago. He managed to do this from scratch using no external financing whatsoever. At the time he decided to plan for the company's succession, the company employed 40 persons and had an annual turnover of six million Swiss francs.

Once aware of the importance of planning for a succession, Alexander Manberg approached this task with considerable thoroughness. He not only wanted to be rewarded for his past efforts but wanted to ensure the long-term existence of the particular brand he had created. For the latter reason, he blocked all proposals for selling the company to any competitors and instead looked for an independent successor that had similar competencies to his own, viz. strong technical skills, a capacity to bear the many difficulties that are bound to arise when managing a company, and an awareness of quality that is typical of operations in Switzerland.

In the end, he was able to persuade a senior engineer within his company (albeit very talented and technically skilled) to become his successor and to take over the company. The deal involved external financing and this new owner was also appointed as the CEO.

Several months after his appointment, the new CEO recognised the need to adjust the company's strategy to the rapidly changing market conditions in the IT branch.

However, having little managerial experience and overestimating his responsibility, the new CEO blocked himself by fears of making unsound decisions. Finally, he was not able to believe in his own success and in the success of the business itself. This resulted in a negative impact on the company's overall performance.

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2 Questions

- What was the reason at the Board level for the company's negative development?
- Was the decision to look for a successor with the same personal profile a good one?
- How could the situation be improved?

3 What Happened in Reality?

The Board recognised that the new CEO was considerably deficient in financial skills. It had also recognised that an increased number of employees required professional guidance and control and this could not be executed by a person with strong technical skills alongside to his client servicing and strategic direction activities.

The Board decided to appoint an independent CEO. This decision released the tension of fears and restored a positive trend in company's development.

4 What Can We Learn from This Case?

1. Planning for a succession in a company is as a chance to strengthen that company by broadening its corporate knowledge and professional network. Market conditions are considerably different from what they were 30 years ago. Try to consider candidates with different skills! When the new successor has very similar skills to his predecessor, it could well be a good idea to support that person by employing a new CEO.
2. When starting from the size of 30 people, an independent CEO is recommended to increase the efficiency of operations and to free the resources for other activities.
3. An independent CEO can also be the solution when a company or the company's owners are facing financial pressure. This is likely to keep any awareness of business risk at a sound level, thereby seeing that any new opportunities are taken advantage of.

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Board–Management Collaboration Case

by Harry Korine
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An international NGO dedicated to research and project work has seen the amount of unrestricted funding it receives decline precipitously over the last 3 years. In an environment of declining budgets, both public and private donors have sought to earmark the funding they provide to specific research programs or project outcomes (e.g., restricted funding). As a result, the NGO has been forced to cut back on some of its work and reduce staff. Overall, headcount has declined from over 250 to 200. Just as importantly, the nature of the work has changed: whereas for the first 20 years of the organization's existence, researchers and project workers could count on a steady flow of centrally generated funding, they now have to spend a lot of their time preparing proposals and applying for external funding.

While a majority of staffers have taken to the new challenges positively, quite a few have reacted to the changed conditions with disbelief and anger. The Director whose term has coincided with the changes has come in for particular criticism. He is said to have been unnecessarily blunt and, at times, to have acted in a threatening manner in implementing the new policies. Several senior staffers have made use of their ties to individual members of the NGO's Board of Trustees to make personal complaints about the Director. In the absence of regular communication between the Director and the Chair of the Board, mistrust has been allowed to fester.

The NGO Board is made up of respected scientists, career non-profit professionals, and experienced business people from around the world. The Board is self-constituting, independent, and unpaid, with members chosen for a maximum of two 3-year terms and a change of Chair every 3 years. In addition to teleconferences for committee work, the Board meets twice a year in person, for

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2–3 days per meeting, receiving management's recommendations and deciding upon the major issues facing the NGO.

Under the influence of the complaints of several senior staffers to individual Board members, the Board decided at its last meeting to give the Director a contract extension of only 1 year (rather than the 2 years that he had asked for) and require that he undergo professional coaching as a condition for the extension. This decision came as a surprise to the Director and to his management team. They feel that they have done their best to steer the NGO through turbulent waters, and the results, both in terms of quality of work done and new funding obtained, bear this out. In response to the Board's decision on the Director's contract, the management team has written to the Chair of the Board in strong support of the Director, asking the Board to give him an unconditional 2-year extension.

The new Chair, who only took over after the last board meeting, asks an independent consultant for advice. Specifically, (a) what should be done about the contract extension for the Director—should he the Chair ask the Board to go back on its decision; (b) what should be done to strengthen the collaboration between the management and the Board; and (c) what should be done to restore confidence in the organization and its governance?

1 Analysis

Comparing the experience of the NGO in the case to that of other "not for profits" (NPFs) is a good starting point for the analysis. The situation described is dramatic, but the context is not unusual. In fact, many NPFs have experienced similar challenges in recent years, specifically the decline of unrestricted funding, the reduction in headcount, and the need for staffers to become more entrepreneurial. Also, it is not uncommon for the staffers of NPFs, particularly those with a research focus, to work around hierarchical channels of communication and take personal complaints directly to the top. Finally, a significant knowledge gap between all-volunteer Board and professional management is a feature of many NPFs. In short, the NGO in the case can learn from the experiences of other NPFs.

2 Consultant's Advice

In a first, immediate step, the consultant had to help the new Chair decide what to do about the contract of the Director and the letter of the management team. Given the Director's record of good performance under difficult conditions and in view of the fact that the negative information on the Director was limited and potentially biased, the consultant asked the Chair to decide if he would be willing to personally support the Director, not only in extending his contract against partial opposition on the Board but also in working with him closely to make sure that the Board and the management would be able to go forward on the same page. In the process of addressing management's letter in support of the Director and reconsidering the contract extension decision, the new Chair made his commitment absolutely clear to

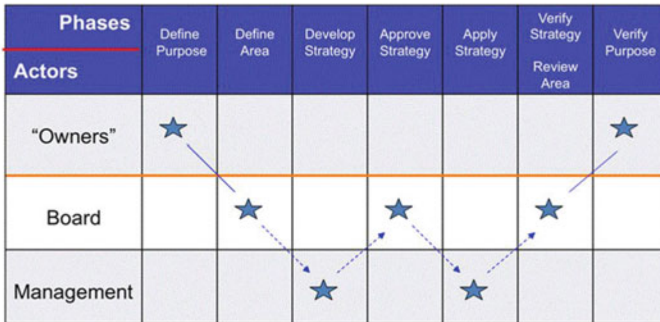

Fig. 1 Board as integrator

both Board and management. Faced with a Chair resolved to lead, the Board member who had been most closely connected with the information against the Director resigned, and, after several teleconferences, the other Board members agreed to reverse their previous decision and grant the extension.

In a second step, the consultant worked with the Chair and the Director to prepare a workshop on Board–Management collaboration. It was agreed that the workshop would be one part education and three parts work. In the educational part, both Board and management would learn about best practice in the governance of NPFs, with a particular focus on the different roles of board and management. In the work parts, Board and management would rethink the nature and role of the Board, develop new processes for working together, and agree on how to channel two-way communications between staff, management, and the Board. Preparation for the workshop was intense, with a three-way personal meeting, multiple trans-continental telephone conferences, and numerous drafts of workshop content. It was important to the consultant that both Chair and Director contributed to and bought in to the recommendations for action to be presented and put into action at the workshop.

The key ideas presented at the workshop can be summarized in two slides (Figs. 1 and 2), as follows.

3 Workshop and Board: Management Resolutions

At the workshop, the consultant helped Board and management understand how the changes in the context required them to collaborate much more closely than they had in the past: to be able to respond to the twin challenges of unstable, restricted funding and rapid transformation of the business model, Board and management could not go on in the "old" way, but needed to adopt the "new" way outlined by Taylor, Chait,

Fig. 2 Teaching new ways

Teaching an Old Board New Ways

OLD	NEW
• Approves/monitors	• Joint problem solving
• Territories set in stone	• Domains set as needs
• Structure and routine	• Strategy and flexibility
• Process driven	• Content driven
• Collective of stars	• Collective capabilities

New Issues → New Behaviors

Source: Taylor, Chait, and Holland, The New Work of the Nonprofit Board, *Harvard Business Review*, 1996

and Holland and summarized in the second slide above. Once that was understood and agreed upon, Board and management resolved a series of concrete actions:

(a) To organize future board meetings around specific themes, as dictated by needs
(b) To constitute mixed Board/management work groups to address issues of strategic importance on an ad hoc basis
(c) To ensure that all board agenda items were presented by management as either for information or for decision and led to specific next steps
(d) To establish and reinforce clear channels of communication from the Chair and the Director to the staff and from the staff to management committees and hence to the Board and to close down any unauthorized communication to the Board

It should be noted that the consultant also took part in the first board meeting after the workshop and intervened on several occasions to actively reinforce the "new" way of working. This allowed Board and management to see their agreement in action and adapt the model to their circumstances.

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Check for updates

Governance of Gender Diversity Case

by Beatrix Dart
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The six board directors of Minefield Company, a publicly traded mining company with a successful 40-year international track record and revenues in excess of $12 billion dollars, have been locked in a heated debate over the last few board meetings. The board chairman, John Miller, has been visibly frustrated by the lack of agreement what criteria they should use to add a new board member to their currently all-male board. Since Jim's retirement from the board, the position has remained vacant for over 9 months now. The CEO of Minefield, Barry Goodman, has been adamant that they should be adding a woman to their board, citing that it is "the right thing to do given that we are in the twenty-first century."

Peter Conway, who at the age of 61 is one of the "younger" board members, has repeatedly pointed out that investors have started to ask more specific questions about their board composition—all white male, with an average age of 69 years—and their lack of tenure limits. Gender diversity has been brought up by one of their largest shareholder as a proposal to enhance their diversity of thought on the board, which is considered as too homogenous.

However, Gordon Dey, one of the longest-serving board members, feels that this is the wrong way to go about adding diversity to the board. His argument is that first of all it shouldn't be based on gender, but on merit—"who wouldn't want the most qualified and experienced person on their board, and should it happen to be a woman—great (!), but let's focus on qualifications first. So who knows a former CEO with mining industry experience in their network?"

Charles Jenkins, a former senior accountant, is not sure which might be the best approach. Clearly, there are hardly any female CEOs in the mining industry, but if the investors are pushing for more women on boards, shouldn't they make it their first priority to find one? And how would one go about doing that?

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Board member Brian Copper thinks the only fair approach would be to develop a rigorous board skill matrix, identifying the exact skills gaps they have on their board (he believes it is in technology), and then look for the best available person to fill that board seat—male or female.

Finding the discussions all a waste of time, Bill Murton points out that he has a perfectly good candidate for the board seat, Tom Watson. He knows Tom from another board they serve together, and he can vouch that Tom is an experienced board member who will fit right into this board as well. On top of that, Tom has great connections in the exploration business, which could be very useful for the Minefield Company.

What would be your recommendation how to solve the disagreement?

1 What Happened in Reality?

- Investor pressure was seen as important by the CEO and by most of the board members, and there were concerns of negative PR at the next shareholder meeting if no pro-active gender diversity policies were presented.
- The board members did come around to prepare a board skill matrix that emphasized new skills they felt they were lacking as a board. They also included attributes such as "independent thinker," "intellectual curiosity," etc. which opened up the field of candidates further, and didn't limit themselves to industry experts.
- None of the board members had a suitable female candidate in their immediate network. They therefore agreed to each reach out to professional connections and to share the skill matrix with the request to bring forward names of female candidates.
- To their surprise, they had over 20 names for women within a 2-week period. A few phone calls and lunch meetings led to a short list of three outstanding female board candidates. They decided to add one of them immediately and to keep the other two names on an "evergreen list" as they might be facing further board vacancies in the near future.
- Board meetings changed. There were more discussions on governance and risk measures, and overall the board felt that their decision-making process had improved dramatically.
- A year later, a second woman was added to the board of Minefield as Gordon Dey retired.

2 What Are the Most Important Lessons Learned?

- Diversity of thought certainly goes broader than gender diversity, but gender diversity is a good place to start to bring fresh perspectives to the board table.

- Merit-based arguments are welcome and make good *sense if* there is an equal playing field. However, in most countries without a gender quota for board positions, women have been historically under-represented and under-valued. Therefore, a corrective action is required to establish an equal playing field.
- Finding qualified women to serve on boards requires a conscious effort to expand the network of board members and senior executives. There are other sources such as trusted advisors, lists of board-ready women, executive search firms, etc. which can be tapped. It is not a supply issue, but a demand issue!
- A board skill matrix should not be limited to previous senior position, but also contain desirable attributes of board candidates. Many male board directors started out on a board because somebody took a chance on them—the same should hold true for female board appointees.
- Rigorous board evaluations should take place at regular intervals to assess the performance of each board director and find the right time to bring in a replacement. Ideally, this would eliminate the need for age limits or tenure limits.
- In the best case scenario, boards have an "evergreen list" of desirable board candidates they are keeping an eye on, so that in the event of a vacancy, it can be acted upon quickly.

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Check for updates

A Case of Responsible Restructuring as Good Governance

by Victoria Maier
(Switzerland)

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First established in the late 1800s as the US subsidiary of Dumont SA, a French-based pharmaceutical and chemical company, NTC Pharma grew steadily through the 1950s and 1960s to become a global, research-based pharmaceutical firm which in 1971 merged with Imogen Inc, a worldwide manufacturer of consumer products. The end result was the NCI Corporation, and the merger proved fruitful: Only a decade later, the company's sales had grown four times by focusing 70% of its products in pharmaceuticals and 30% of its products in widely known household name brands. In fact, NCI's breakthrough products enabled the company to outgrow its parent in size and expand rapidly into Europe, Africa, the Middle East, Asia, and South America.

So although flourishing at the onset of the new millennium, US conglomerate NCI was determined to remain a world-class player on the market. One of the company's policies was to collaborate with business consultant McKinsey to monitor and adopt best practices for organizational development. As a result of this partnership, NCI's senior and top management all became well acquainted with McKinsey consultants Robert Waterman's and Thomas Peters' *In Search of Excellence,* which said that a company's headquarters should have no more than 50 people total.

This fifty-person model, along with other management standards noted in the book, soon became a benchmark for an internal, company-wide study to find out how NCI's management practices compared with best-in-class companies. The findings indicated that many departments—even whole divisions—did not measure

Based on a living case in Switzerland.

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up to the companies discussed in the book. For NCI's top management, the message was clear: Reduce any regional head offices that were larger than the ideal fifty-person headcount.

René Renz, Personnel Executive for NCI's European Headquarters in Geneva, Switzerland, was well versed in the details of the internal study. *In Search of Excellence* had been widely read throughout all corners of NCI and so had the negative results of the internal study. Renz knew change was brewing on the horizon, and when Michael Sauderman, the top HR man at NCI's headquarters in the United States, called to set up a meeting, Renz was not surprised. "Book a nice, quiet room at some hotel for the entire weekend where we can talk confidentially," said Sauderman. Renz did not know exactly what to expect, but he knew that whatever was taking Sauderman across the Atlantic would not be pleasant news.

1 Saturday Morning: The News

Only a handful of people were present at the weekend retreat in Montreux, Switzerland, and Renz did not miss the fact that Renz's own boss, Marc Adler, President of the European Division, had not been invited. A new man had been chosen to head up the European Division instead of Adler, and he had come with a few of his advisors—also new—to the retreat, making for a total of just five participants that Saturday morning.

Sauderman got right to the point: "The fact is, René, that we have to slim down. Our admin and management is much too high. Our European Division Headquarters alone has 110 people where it should have 50 or less. We just can't afford to ignore this situation. We've devised a reorganization which will reduce Europe's management levels from four to two and our headcount to 50, and I need you to figure out how to implement our plan. We need you to begin and complete rollout on Monday."

Sauderman showed Renz the new organizational plan as well as a list of the departments—and people—to be phased out. Even Adler was on the list of people leaving.

Renz's mind reeled. NCI was simply too large and integrated into the Geneva community to be able to effect this kind of organizational change without impacting large numbers of people above and beyond those in the company. In addition, times had been good at NCI. Growth had risen steadily from year to year; this reorganization did not come as a result of need. In fact, NCI was considered a choice employer with rich resources and payback that attracted the best of the best to come work for the company. Many people were going to find it hard to understand that this radical change was being undertaken because the organization's top management had changed its strategic direction.

> When the top management has made a decision like that, there is nothing you can do, really, but implement it. But you can decide how to implement it in the way you think is right. (René Renz)

There would, on the one hand, be emotional repercussions in the company. Those who were not cut would be burdened by the implications of their former colleagues' sheer absence. Efforts would have to be doubled; employees would take on larger loads—willingly or not—and extra strain as a result of fewer hands at the till. The sense of insecurity from the cuts would make the company's remaining employees feel like survivors, and this emotional weight would have to be dealt with.

However, there was also the question of the people being asked to leave. It seemed like a lose-lose situation. On the one hand, the organization had invested in these people and in the department, and now, just as the investment was beginning to bring returns, it was being liquidated. No matter who he asked to leave, their exit from the organization would invariably constitute a major loss of star talent with which the organization might never again have contact. On the other hand, the individuals leaving the organization would have to work extremely hard to find a situation that not only matched, but also furthered, their considerable talents. As ironic as it would perhaps seem, it appeared that making the change happen also revolved around getting people to come to terms with and accept their own dismissal.

Renz felt personally responsible to these people, who had given the company so much of their trust and worked so hard for NCI. The company had been blessed with extremely talented and capable employees, several of them experts with world-class reputations, in point of fact.

There was the option of simply leaving the company and leaving the problem to others. On the other hand, if he stayed, how could he, in less than 48 hours, just get rid of people who had done so much for the company? What tools lay at his disposal for doing the thing right? What pitfalls had to be avoided? What should his next steps be?

Decision Point #1 Renz has Saturday evening and Sunday morning to decide about his role in the process of downsizing NCT's European Headquarters from 110 to 50 on Monday. How do you think he should proceed?

2 Saturday Afternoon: The Decision

The feeling of shock sets in later. At that moment, you just start taking action. (René Renz)

Renz decided that he owed it to the extraordinary people in his unit to stay and implement the change properly.

It was one of the worst days of my life, but leaving would have been an act of cowardice. The only thing to do was make the best of things. (René Renz)

Having made this decision after the meeting on Saturday afternoon, Renz began to think about what to do. It just so happened that he had taught a course on HR management practices and policies at one of the local universities, so he had had

plenty of exposure to the theory on the process of transferring talent and expertise from one company to another due to downsizing. This process also included outplacement, a hot topic which had trickled over from the USA back in the 1980s, and Renz had made good use of it in individual cases in the past to counter people's sense of shock and disorientation at the news of their dismissal.

> There are two things you have to consider in a situation like this. There's the tangible aspect of the matter—the severance package—and that has to be at least adequate. But then there's the intangible aspect. If all you do is offer people a severance package—even a generous one—they're going to feel like they're being treated as things, not people. Compensating people solely in material ways sends the message that people—and their lives—can be bought and sold. (René Renz)

Renz's practice in these cases had therefore been to treat the people leaving the organization in the same way he himself would want to be treated. One aspect of this meant doling out severance packages which were as fair as possible. However, although the the executive management in the United States had authorized Renz to be generous in this regard, Renz also wanted to make sure that these talented people would know what the next step in their career was after their time with NCI had ended.

> If you can show people what their future holds, it cushions the blow they feel after this kind of a shock. I mean, when you're asking these individuals to leave the company, you're not just asking them to make changes but also their families as well, and sometimes these are people from other countries, and often these factors aren't in mind when you make this kind of decision. You shape people's lives by hiring them, but when you let them go, you have a long-term impact on them as well, and that's why it is very important for a responsible company to take care of people just as well when they are leaving the company as when they are entering it. (René Renz)

> ***Decision Point #2*** What considerations does Renz need to make to ensure the successful implementation of the restructuring? What tools should he make use of and what measures should he avoid? What resources does he have to be able to offer people options beyond that of a severance package?

3 Gearing up for Monday: Devising a Solution

First, Renz compiled all 60 people's names, age, qualifications, and job function in a list. This gave him an overview of which employees were qualified for what position. The next thing he did was to create an action plan for implementing the change on Monday. The rollout would have to be timed well so that, among other things, Renz would have enough time to speak privately to every individual affected before communicating the news to other stakeholders. In addition, an information plan had to be set up so that the news would be communicated properly.

> I was really on my own. I had to make sure that people heard things at the right time and that they would keep what they knew in confidence. (René Renz)

He also drafted a budget of direct and indirect costs associated with the implementation which included considerations, such as sums paid out for helping people to move house or losses incurred as a result of change in leadership. The budget also included a severance package for each person affected. An employee received a certain amount of severance pay based on age and length of tenure in the company. However, the package also covered the cost of outplacement support, which would be flexible and given on a case-by-case basis: Individuals who needed more assistance with finding a new placement at another company would receive it.

After Renz had clearly outlined what had to happen on Monday, he turned to the more immediate need of helping people with the next step in their career. A successful career in Switzerland required the acquisition of a personal network of contacts, and Renz had accordingly spent several years networking with HR executives and managers within and beyond Switzerland. He knew many people in the Geneva area as well as renowned colleagues in HRM in 18 other countries. Though by no means a common practice, Renz called individuals from this network—although many came from NCI's biggest competitors—and explained the situation to each person confidentially, as well as his desire to be able to offer each person leaving NCT a viable next step in his or her career.

> I explained right away that this was all emergency and that I only had Monday to tell everyone and that we had a win-win situation all the way around. I'd be giving my HRM network colleagues great talent which NCI could no longer employ; they'd fill the position at minimal expense, effort, and time invested; and the people leaving NCI would have a seamless next step in their career to look forward to. (René Renz)

That his colleagues would see the immediate benefits of this approach and respond positively to it was to be expected: Hiring an executive search consultant would cost a company up to 40% of the salary offered for any position to be filled, and even just placing an advertisement in a noteworthy publication cost approximately CHF 5000. Soon, Renz's network connections had faxed Renz a description of all the positions open at their companies, in total over 80 from over 15 competitor companies.

Renz then looked at his original employee qualifications list and compared each job description with each employee's previous experience, qualifications, and education and assigned them jobs that might be of interest. Renz's final list had three columns: One for each person's name, one for his or her professional qualifications, and a third showing the positions open for which each individual seemed qualified. After he had assigned at least one position to each person, he removed each candidate's name from the list and faxed it to his network colleagues for their review. As a final thought, Renz built in a contingency plan. Some of the individuals to be phased out were qualified to take on certain internal positions which were being hired for at that time, so Renz planned to offer these individuals the option of an

internal transfer first. This alternative would also mean a smaller loss of talent to the company.

> Of course, this process took up the rest of Saturday and went on Sunday before and after I presented my game plan to the corporate representatives, but by late Sunday evening, I'd organized new jobs for almost all of the people leaving NCI. (René Renz)

> ***Decision Point #3*** What do you think will be the most difficult aspect of the rollout? What do you think Renz should do to make the most of the strengths and backup/safeguard against his weaknesses in his action plan? How should he frame the news to each person? How will the way he frames the news impact the organization and the change effort?

4 Monday: Game, Set, and Match

It was clear that if the information was disseminated improperly, people would take the change badly. In the mid-1990s, Switzerland remained one of the least legalized countries in the western world: People could be hired by means of a verbal agreement, without a written document. Trust was the backbone of business—why create laws to regulate something when a handshake sealed a business deal just as well?

However, trust was as fragile as it was crucial. Renz knew that it had to be preserved as the basis for collaboration with all the stakeholders in the restructuring process. Misunderstanding and miscommunication were luxuries that NCI simply could not afford. For one thing, the news of this scale of dismissals in one of Geneva's largest sources of income and employment could easily sour relations between NCI and the Swiss government if improperly communicated. The Geneva city government would have to receive the news directly from the company, not just read about it in the paper. And if employees got wind of the news prematurely, insecurity and worry could overtake the organization in almost no time.

Monday went by in a whirlwind of activity. Renz scheduled an appointment of seven minutes on average with each person being asked to leave the company to walk through the restructuring and severance process and explain what would happen next. He began with top-level managers first and worked his way down.

> People want to know what is going to happen. I didn't waste time telling people that they were going to lose their job, but I also assured them that it wasn't because of their performance. When you're meeting with someone to let them go, the meeting has to be short. You have to explain that it isn't your doing, that you want the best for them and that they will find a job that's at least as good as what they have now, and that the material aspects of the change will be fair. And we knew we could be fair, because the company was doing well and because even with the generous severance pay that people were given, the restructuring was going to pay itself back. (René Renz)

Many of the people Renz spoke to that day had expected some measure of this nature to arise as a result of Peter and Waterman's study. Many at NCI's European Headquarters felt that American companies tended to be restructured more

frequently based on trends and best practices, which could mean lower employment security compared to working for a Swiss firm. However, this expectation did little to alleviate people's disappointment and upset at losing their jobs. As more and more people became informed, the tension in the atmosphere became more and more palpable. Renz knew that people would still need an explanation that would allow them to digest their feelings on the matter.

> I said to people, 'We all know that when you work at headquarters, you're in the most comfortable, highest place in a company, and that's in a city with one of the highest standards of living in the world. The problem is that people stay put because there is no place to be promoted to internally, and since a lot of people are slow to look for new assignments outside the company, we have a build-up here that has to be broken down.'

Renz also reserved an hour to inform employees who would be staying with NCI of the restructuring because these individuals would also need an opportunity to digest their feelings about this restructuring effort. So Renz invited everyone to a meeting in which he asked them to work together to help NCI into its new, improved, leaner future. Thereafter, he met personally with the government to talk about the dismissals. He rounded up the communication process by making an announcement to the press.

> You have to tell the people close to the change. The local community is invariably affected by this scale of change, and they deserve and need to be the first ones to know. (René Renz)

However, Renz's day did not end with the press conference. The news had indeed spread like wildfire, and people began to contact Renz to find out if they, too, were on the blacklist.

> I had to answer their questions immediately, of course. People were worried. One person had called me just as he was leaving Switzerland, and I had him paged at the airport when his plane landed so that I could reassure him that he wasn't going to be asked to leave. This is the kind of thing you have to do, or things will get out of hand as people talk and speculate. (René Renz)

The initial meeting was followed by an in-depth discussion of the severance package and procedure between one of Renz's direct assistants. This offered individuals an opportunity to express particular concerns and ask questions regarding the process. Renz also scheduled a personal follow-up with each individual as a third meeting to find out how things were moving forward and to help solve potential problems. Toward this end, Renz also hired an external outplacement consultant to help individuals needing—or wanting—extra support in the weeks to come.

By 7:00 p.m. on Monday, Renz had indeed removed 60 individuals from NCI—most of them management level—and put the company's European headquarters in line with the best practices of the day, with fewer leadership levels and a broader span of direct manager control in the ranks. In financial terms, this change meant no less than a permanent reduction of 50% in the overall budget at headquarters.

Decision Point #4 René Renz has now reduced NCI's European leadership structure by more than 50%. How do you think this restructuring effort will benefit NCI over the long and short terms? How do you think the restructuring effort could harm NCI over the long and short terms, and what do you think the company should do to counteract or safeguard against such negative impact?

5 Stepping into the Future: A New Frame of Mind

The financial benefits of the restructuring were yet to come, but there were immediate takeaways. To begin with, NCI found itself experimenting with new ideas about how to develop as a company. The restructuring had been executed by choice rather than need, and even though almost every employee left NCI with a job in hand, the process—short-lived though it was—had still been challenging at different levels for everyone involved. The company could not afford to constantly lose and rebuild its talent pool as a result of downsizing; ongoing fluctuation would take its toll on the employees, without whose full focus and innovation the company would not flourish. However, increased changes in the global pharmaceuticals market invariably meant more change at NCI, too. To NCI, developing the company responsibly and effectively over the long term now meant strategically developing its people resources so that when hard times hit, downsizing would not be a must.

NCI therefore decided that in future, it would keep its headcount low on a long-term basis. This meant streamlining human resources constantly, before cost-cutting became an ultimatum. For example, whenever a position became vacant, NCI went through a preselection process to analyze whether or not the job could be integrated into other internal functions or whether indeed externals should be invited to apply for the position. The tasks and functions associated with each position were divided into three categories—category I, vital and interesting; category II, vital but boring; and category III, not vital and boring. HR offered category I tasks and functions to internal employees wherever possible and then found solutions for automating category II tasks and functions to subsume them in pre-existing organizational structures and processes without additional expense or effort. Category III tasks and functions were simply phased out of the work structure altogether.

> If you want to out-innovate your competitors, you can't surgically remove excess in one fell swoop after your company has gotten 'overweight.' You can't wait that long to make choices regarding your company's development and your people strategy. Building companies doesn't happen through restructuring revolutions but rather through a dynamic, step-by-step process which never ends. Toward that end, you have to have as few fixed costs as possible. You need companies which are lean, fit, and happy, all the time. 'Sinful indulgence' when times are good and then purging when times are bad isn't the way toward long-term excellence and sustainability. (René Renz)

In addition, humanely restructuring by covering both the tangible and the intangible aspects of a change meant that former employees still wanted to work with NCI, even as externals. The company thus found itself better connected than ever, with increased access to a network of expertise and skill that went beyond its internal

and subsidiary borders. Some of the individuals asked to leave even applied for jobs at NCI years later.

> Our major achievement was that people came back. Years after they had built up a career with other companies, they still wanted to work for NCI. There is no greater marker of success for a downsizing process, no greater compliment to a company, than when you see the people you let go returning to work for your company. (René Renz)

Decision Point #5 What do you think is the relevance of this type of downsizing solution is in a recessive economy? Which elements of NCI's approach do you think were critical for the success of the restructuring effort and its long-term impact? How do you think other companies can make use of NCI's approach and what, if anything, would you change?

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Part IV

The Board of Directors as a Controlling Body

Check for updates

Subsidiary Governance Case

by Martin Hilb
(Switzerland)

*International Board Foundation and its
International Center for Corporate Governance*

You are the newly appointed Vice President for Europe of Computex Corporation, a San Francisco-based computer manufacturer.

This morning you received the following letter signed by six (out of ten) members of your sales force team in the recently established Swedish subsidiary, located in Gothenburg.

Each group has to analyse the situation and to develop an action plan (based on the attached form) to solve this problem in a fair and effective way.

1 Original Letter:

Mr. Peter JONES
Vice President-Europe Computex Corporation
San Francisco/U.S.A.
Goteborg, March 30, 2018

The writers of this letter are the headcount of the Sales Department of Computex Sweden *NS,* except the Sales Manager.

See Martin Hilb: "Glocal Management of Human Resources", 2nd Edition, LIT Zurich & Berlin 2009, pp. 181–184

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We have decided to bring to your attention a problem which unsolved probably will lead to a situation where the majority among us will leave the company within a rather short period of time. None of us want to be in this situation, and we are approaching you purely as an attempt to save the team to the benefit of ourselves as well as Computex Corporation.

We consider ourselves an experienced, professional and sales-oriented group of people. Computex Corporation is a company which we are proud to work for. The majority among us have been employed for several years. Consequently a great number of key customers in different areas of Sweden see us as representatives of Computex Corporation. It is correct to say that the many excellent contacts we have made have been established over years; many of them are friends of ours. Short background because we have never met you. What kind of problem forces us to such a serious step as to contact you? Problems arise as a result of character traits and behaviour of our General Manager, Mr. Miller. We are more convinced that we are tools that he is utilizing in order to "climb the ladder". In meetings with us individually, or as a group, he gives visions about future, how he values us, how he wants to delegate and involve us in business, the importance of cooperation, communication, etc. When it comes to the point, these phrases turn out to be only words.

Mr. Miller loses his temper almost daily, and his outbursts and reactions are not equivalent to the possible error. His mood and views can change almost from hour to hour. This fact causes a situation where we feel uncertain when facing him and consequently are reluctant to do so. Regarding human relationship his behaviour is not acceptable, especially for a manager.

The extent of the experience of this varies within the group due to our location. Some of us are seldom in the office.

Secondly we have experienced clearly that he has various means of suppressing and discouraging people within the organization.

The new "victim" is our Sales Manager, Mr. Johansson. Because he is our boss, it is obvious that we regret such a situation, which to considerable extent influences our working conditions.

There are also other "victims" among us. It is indeed very difficult to carry through what is stated in our job descriptions.

We feel terribly sorry and wonder how it can be possible for one person to ruin a whole organization.

If this group had consisted of people less mature, many of us would have left Computex already. So far only one has left the company due to the above reasons.

From September 1, two new Sales Representatives will be joining the company. We regret very much that new employees get their first contact with the company under the present circumstances. An immediate action is therefore required.

It is not our objective to get rid of Mr. Miller as General Manager.

Without going into details, we are thankful for what he has done for the company from a business point of view. If he could control his mood, show some respect for his colleagues, keep words and stick to plans, we believe that we can succeed under his leadership.

We are fully aware of the seriousness of contacting you, and we have been in doubt whether or not to contact you directly before talking to Mr. Miller.

After serious discussions and considerations, we have reached the conclusion that a problem of this nature unfortunately cannot be solved without some sort of action from the superior. If possible, direct confrontation must be avoided. It can only make things worse.

We are hoping for a positive solution.

Six of your Sales Representatives in Sweden

ATTACHMENT 2:

STRICTLY PERSONAL/CONFIDENTIAL

A C T I O N   P L A N

STEP	WHOM?	WHAT?	WHEN?	WHO?	HOW?	WHERE?	FOLLOW-UP	ACCOMPLISHMENT (PLEASE CHECK)

CASE GUIDE

Arriving at home, Peter Jones wrote the following action plan:

Case guide

STRICTLY PERSONAL/CONFIDENTIAL

ACTION PLAN

ACTION STEP	WHO?	WHAT?	WHEN?	WHOM?	HOW?	WHERE?	FOLLOW-UP
1) Inform Miller of the letter and his intention to fly in tomorrow to see him and the letter signaturies.	Jones	calls	now	Miller	by phone	at home	✓
2) Arrange group meeting with letter signaturies.	Jones	calls	afterwards	letter signaturies	by phone	at home	✓
3) Discuss perceived problems.	Jones	meets	tomorrow 3 pm (arrival time)	Miller	conference room meeting	Stockholm airport	✓
4) Discuss written issues.	Jones	meets	tomorrow 6 pm	letter signaturies	group meeting	Hotel Conference room in Stockholm	✓
5) Discuss written issues with Sales Mgr.	Jones	meets	the following day 8 am	Johansson	conference room meeting	same hotel	✓
6) Meet other Sales Representatives (who did not sign the letter)	Jones	meets	9 am (20' per individual)	4 other Sales Representatives	individual meetings	same hotel	✓
7) Meet other department heads (reporting to the General Manager)	Jones	meets	10.30 am (30' per individual)	3 other department heads	individual meetings	same hotel	✓
8) Inform GM about Steps 4) to 7)	Jones	meets	12 am	Miller	lunch	same hotel	✓

Action plan

2 What Happened in Reality?

The same night Jones prepared his trip by studying parts of two books he had read long time ago:

- The chapter about “Sweden” in the book *Multicultural Management*
- The chapter about “Group Psychology” in the book *Conflict Management*

After having read the simplicities, Peter was aware of the facts that the Swedish environment differs very much from the American one and that it is essential to know as much as possible about the characteristics of team building in Scandinavian countries.

When Jones met Miller at the airport and after reviewing the letter, Miller pointed out that in his opinion the letter was initiated by the Sales Manager.

During the group meeting with the six Sales Representatives, the General Manager was again accused of his perceived inappropriate behaviour. Jones repeatedly asked them to verify their statements. But no individual was able to do so. The result of the long group meeting (which ended after midnight) was that the Sales Manager had initiated them to originate the letter.

The next step was obvious: Jones met the Sales Manager and confronted him with the findings of his group meeting with the Sales Representatives. The Sales Manager reacted by admitting it was true. As a consequence of his action, the Sales Manager agreed to leave the company with immediate effect.

The other department heads, the Sales Force and the other staff were informed about this agreement accordingly: effective immediately, all Sales Representatives were appointed Sales Managers of their district reporting directly to the General Manager. By this decision, one management level was eliminated; the jobs of the Sales Representatives were enriched, evaluated and compensated higher and information falsification, bureaucracy and overall costs reduced.

This case demonstrated two things. If, there is a leadership problem:

1. First we always have to determine where the cause of the problem is located, on the individual or group or organizational level.
   In our Case if Jones would not have asked this question, the risk to the organization would have been the loss of an effective executive.
2. Second we always have to be aware of the whole situation by using a 360° view of the perceived problem.

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Financial Competence on the Board Case

by Peter Leibfried
(Switzerland/Germany)

University of St. Gallen
International Center for Corporate Governance

1 Situation

Mike Muckelroy is the chairman of the board of a larger Swiss company, with revenues around CHF 600 Mio and about 2000 employees. Being a lawyer himself, he has taken over the position as the chairman about 15 years ago, when being asked to do so by one his clients, the family owning the company. Since almost more than one generation, no one from the family has been actively involved in managing the company. Ownership within the family is somewhat spread, with ten shareholders. No one has the majority, percentages of ownership range from 1% to 25%. Luckily, so far there have not been any serious conflicts amongst the owners. This is not only due to the wise stewardship of Mike Muckelroy but can probably also be attributed to Allan Parker, who has been CEO of the company for almost 20 years now. Since then, the company has been growing steadily, is producing stable and predictable profits every year and generally seems to be in a perfect shape.

A few months ago, the company has hired a new CFO, as the previous one retired after 25 years of service. Ben Counter is just above 40 and has spent the major part of his professional career in a much larger, yet also family-owned, international company. Shortly after starting to work for your company, he has brought up the issue of changing the company's accounting standards from local Swiss company law (Obligationenrecht) to an international standard such as IFRS (International Financial Reporting Standards).

Mike Muckelroy has been talking to a couple of people about this idea already. However, opinions seem to be quite diverse:

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- The new CFO is heavily in favour of converting to international standards. Unlike many other people within the company's finance and accounting department, he seems to be very energetic, dynamic and motivated.
- CEO Allan Parker is very sceptical of any effort being put into accounting in general. In his eyes, accounting is a legal burden which unfortunately cannot be avoided but does not provide any benefits in terms of sales or innovation. Thus, he would like to keep everything as is.
- The two main shareholders of the family (25% each) are also quite happy with what they receive and also would like to save cost.
- The external auditor—a small, local firm—is also pretty reserved. However, a sales presentation made by one of the Big4 audit firms about a year ago also suggested that converting to IFRS would a good idea.
- Besides Mike Muckelroy as a lawyer, the board of the company consists of former top management employees of the company and a few family members. No one has professional experience in the finance sector.

What should Mike Muckelroy do? To advise him, please be aware: besides what can be directly taken from the case, what might be the driving factors for the positions taken by the various stakeholders above?

2 What Happened in Reality?

After a lengthy debate (with the CFO almost leaving again), the company decided to change its accounting system to an international standard. The consequences were quite significant:

- Under the local accounting system, the company apparently had made great use of earning management techniques to hide profits (in good years) and losses (in bad years).
- It became visible that the company's financial situation is much more volatile (and vulnerable) than the shareholders have thought. It turned out that the company can react much better and quicker, if fluctuations in the market are shown in the financial statements.
- The CEO apparently tried to calm the owners by smoothing income, also having a positive effect on top management compensation (as the budget was always reached).
- It also turned out that the two major shareholders had a different view on the company than the rest of the owners. While the larger shareholders wanted to increase long-term company value, the smaller shareholders largely were focussed on dividend distribution. The new accounting also led to fruitful discussions amongst the shareholders about what governance rules to follow amongst them.
- The necessary work to adapt the accounting system caused significant personal overturn in the finance department and also in IT. At the end, almost all former

accountants had left the company, and a younger, more dynamic and more business-oriented team was in charge. This was to the benefit of the operating management, too. Also, new accounting software was introduced, which produced more reliable and up-to-date numbers.

- Also, the audit firm changed, from the smaller company to a Big4 company. Later on, this was also helpful in international tax issues and when international acquisitions came along. It was, however, significantly more expensive than before.
- In the future, not only the CEO and the inner circle of top management really knew how the company was performing, but there was one version of the truth throughout the broader management and the shareholders.

3 Takeaways

While accounting at first sight always seems to be about numbers only, in reality, it does heavily involve people and culture. Thus, also general management should be open to the respective issues, and not push it into a technical, sometimes even "nerdy" corner. Very often, discussions about numbers are in reality discussions about underlying business or cultural issues. In order to bring them up, the board needs at least one member (financial expert) who is on a level playing field with the CFO and the auditor and will not be distracted by (presumably) complicated technical questions.

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Check for updates

IPO Governance Case

by Jean-Pierre Jeannet
(USA/Switzerland)

Babson College
IMD

Orthotec was a privately held company manufacturing surgical tools for orthopaedic surgery. Founded by Thierry Monnet and Serge Begulin, two engineers, its products required sophisticated and state-of-the art machinery to shape the metal parts to the high requirements of orthopaedic surgery. Customers were orthopaedic implant companies that packaged their implants with the surgical tools and distributed them to hospitals worldwide. Since its foundation some 30 years ago, sales had reached about CHF 50 million with average profitability for this industry.

About 15 years ago, the original founders had looked towards an exit strategy and engaged Christian Volland as executive and CEO with medtech industry experience. When entering the company, Volland was able to acquire Volland's 50% stake in the firm and Monet continued as shareholder.

The company then grew from about CHF 2 million to CHF50 million under the leadership of Volland. Originally, the company had a majority of its activities in the machining of advanced components for the watch industry. With growth prospects in the medical sector judged much more favourably, new ownership decided to pivot the company into the medtech space and pursue implant OEMs aggressively. The rapid growth was both a managerial and financial challenge.

When the remaining founder, Begulin, wanting to sell his stake, caused some difficulties for CEO and co-owner Volland who suddenly was faced with having to find not only new capital for growth but also replace a retiring founder. Volland viewed a strong potential for the firm to double in size with a possible acquisition that would expand the product line from niche towards full line and also offering metal cases for tools that could be carried into the hospital operating rooms.

After a lengthy search for replacement capital and funds for growth, Volland had attracted some local private equity firms who were prepared to share the investment doubling the company's value from CHF 25 million to 50 million. Given investment

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limits, none of the local PE funds could shoulder this deal alone. A distributor in Europe was acquired and had been paid for with shares. With the new capital, and an acquisition to boot, the company expected to reach sales of about CHF 200 million and eventually go for an IPO valued at above CHF 250 million, a substantial return for all equity owners. Although Volland and one of his key executive together owned slightly more than half of the equity, they had to accept three outside board members to join Volland and his colleague.

One of the largest OEMs and a major client of Orthotec were looking to sell one of its plants to Orthotec together with a multi-year sales contract for existing products. Volland saw the possibility to rapidly move towards the eventual goal as the industry players were moving rapidly towards outsourcing complete surgical tool sets from suppliers, rather than pick them one by one and assembling kits themselves. Volland signed an agreement in principle with the OEM. To complete this transaction, he required a bank loan of CHF 20 million combined with a capital increase of CHF 5 million. A bank stood ready to lend but then suddenly rescinded its commitment.

When Volland convened his board of directors, he was surprised to face resistance. Among his private equity investors, the lead investor was very hesitant and argued that he was not sure that Volland was the right person to take this company to the IPO level and that Orthotec should first completely digest the previous, small, acquisition. After a long debate, the board consisting of Volland and his senior executive, as well as three outside investors, finally decided that Volland could close the deal but there could be no capital increase, and the board would want to monitor every step of the discussion and negotiation taking place. The lead investor even announced willingness to sell its stake.

At this point, Volland faced some very tough choices. Under the present situation, he could not go through with the deal, which would make him loose face with his major customer, a situation he wanted to avoid at all costs. He might find another lender willing to accept step in, but with a deadline looming of 3 months out this appeared difficult. He was considering finding new investors to buy out those unwilling to go further. Another possibility arose with some competitors who signalled interest to do a trade sale. Volland was wondering how to best salvage the possibility of an eventual IPO down the road with the chance of a higher return on the invested equity.

Epilogue

With the expiration of the purchase agreement with the major OEM just 3 months away, Volland was hesitant to pursue options that would take a long time and possibly not be realizable. He did not think the new investor route would be realistic within the deadline, and the new bank/lending agreement might be risky to conclude as well. Ending with no deal in place to acquire the offered plant felt like the worst-case scenario to him. In the end he concluded a trade sale, which he could, with a

majority of shares and a drag along agreement with shareholders. This sale did not yield much more than the earlier valuation from the entry of the PE investors. Worse, the new owner did not grow the business, and the prospects of a much larger company fizzled. Employment in the Orthotec company main plants shrunk, leaving everyone a loser compared to earlier growth prospects.

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Fraud Governance Case

by Fred van Eenennaam (the Netherlands)

and Hagar Michel (Switzerland/ the Netherlands)

VBHC, Center Europe
International Center for Corporate Governance
The Decision Institute

Gerard van de Aast was appointed as board member of the 150-year-old technical services provider Royal Imtech N.V. (Imtech) in December 2012. Imtech was the darling of the Dutch stock exchange AEX with an order book of 27,000 projects, 29,000 employees and revenue of approximately 5.5 billion euros. By April 2013, Van de Aast would replace Imtech's CEO Van der Bruggen who had led the company since 2002 together with CFO Gerner.

Imtech's targets for 2015 were revenue of 8 billion euros and an operational EBITA margin between 6 and 7%. Between 2001 and 2013, Imtech acquired an aggregate of 86 companies in the Benelux, Germany, Austria, Eastern Europe, the UK, Scandinavia, Turkey and Spain. Imtech Germany and Eastern Europe (Imtech Germany) was the most profitable subsidiary of Imtech. In 2010, Imtech Germany had an EBITA margin of 8.3%, a revenue growth of 18% to 1.3 billion and an order book growth of 14%.

Imtech's working capital position had been a point of conversation since August 2011 and reached a new actual record by March 2012: approximately 47% of trade receivables were overdue, of which 22% more than 2 months. From that moment onward, the audit committee, analysts and investors repeatedly expressed concerns about the working capital position of Imtech, the rapid growth of the order book and revenue (particularly in Germany) and the upcoming departure of the CEO and CFO of Imtech.

A 155 million euros mechanical and electrical contract for a Polish amusement park called Adventure World Warsaw (AWW) was approved of by Imtech Germany in July 2011. The contract grew to 680 million euros but subsequently failed to secure financing. In March 2012, Imtech had to provide guarantees for a quarter of the contract price of the project (147.6 million euros incl. taxes). Imtech Germany's CEO suggested to make an advance payment through a promissory note, an agreement between AWW and Imtech Poland that stated AWW would pay the guarantees.

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Over the course of 2012, the promissory note expired twice without financing. In November an analyst from ABN Amro advised to sell shares, and, in the same month, Imtech's accountant KPMG stated that the promissory note could not be included in the 2012 annual results as cash and cash equivalents. A second opinion from EY, requested by the board of management, stated the same in January 2013.

On the morning of February 27, 2013, Van de Aast received an overview of incurred costs on Imtech's biggest project in history: 70 million euros had been spent on the 680 million euros AWW project. The highest amounts listed were payments to companies that did not exist according to Google, and all management involved in the project was not able to provide satisfactory answers on questions posed.

After a supervisory board meeting and an initial dive into the AWW issue, Van de Aast asked Rabobank for 200 million euros extra borrowing capacity and instructed Imtech Germany's CEO to suspend the CEO and CFO of Imtech Poland together with 31 key employees. Imtech announced a write-off of at least 100 million euros on the Polish project, a forensic investigation into possible irregularities and the postponement of the publication of the 2012 results. Imtech Germany's CEO and CFO were dismissed the day after.

A new CFO and two others were added to the board of management of Imtech. Two of the six supervisory board members stayed and two new members joined, while three other potential supervisory board members would join when future funding was set. KPMG stayed on as accountant to deliver the annual report, and a 500 million euros rights issue underwritten by ING and Rabobank was announced to strengthen Imtech's equity, used for debt reduction.

Van de Aast prepared to meet with the chairman of the supervisory board to discuss further steps. What should he propose as his first steps? And what should be the role of the rest of the board of management, the supervisory board members, auditors and banks?

1 What Happened in Reality?

- The focus of the new board of management was threefold: mapping past events and making them public, operational excellence (with a strong focus on ethics, control and decentralized management models) and financial recovery. Dozens of advisors were hired to help in the process.
- Newspapers continuously published articles about possible price fixing and fraud, and Imtech stated time and again that they were looking into all past events.
- Imtech's operational result was disappointing, and the financial performance was lower than expected. It became clear that Imtech had historically inflated its performance using accounting schemes, which was reflected in its working capital. Customers left, cash flow and revenue declined by 2013, and by 2014, driven by the de-risking behaviour of its financiers, the implied interest rose from around 5% to 16.4%. As a result of the increased interest charges, Imtech no longer generated cash and was unable to repay its outstanding debt from operating cash flows. The outstanding bank guarantees amounted to 897 million euros with headroom under existing guarantee facilities of 155 million.

- Imtech had sold its ICT and Turkish businesses, and a second rights issue of 600 million euros was announced which diluted the existing equity to less than 0.8% of total equity. 52.44% of the rights were exercised in the second rights issue, and ING bank, Rabobank, COMMERZBANK and ABN Amro bank became holders of the remainder of Imtech's outstanding and issued share capital.
- Imtech Germany filed for bankruptcy in August 2015, and the appointed administrators sold most assets of Imtech throughout 2015 and 2016.
- Two administrative fines of, respectively, 1 and 1.25 million euros to the former CEO Van der Bruggen and CFO Gerner of Imtech were dismissed: there was no law that forced the Imtech directors to disclose information on Imtech's finances, as long as the directors did not doubt financing would come through.
- In February 2017 the former CEO of Imtech Germany was sentenced to almost 4 years in jail for making 47 illegal payments of almost 3 million euros to a firm that was owned by the man who was Imtech Germany's CEO until 2002.

2 What Are the Most Important Lessons Learned from This Case for the Effective Direction and Control of Companies?

- An aggressive growth strategy is not sustainable: the targets for 2015 would mean Imtech expected that the historic average revenue growth of 14% could be persisted until 2015—during crisis times.
- 'If it's too good to be true, it's probably not true': business controls are important with decentralized units. Only trust is not enough in an organization the size of Imtech, an eye has to be kept on working capital position, outstanding guarantees and gross debt of the entire organization to see if unwanted practices are taking place.
- Sanity checks are always necessary: Is building an amusement park in the midst of a crisis wise? And after the fraud was discovered, was a 500 million right issue enough to go through the whole change process, including the financial consequences that a fraudulent department brought along?

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Afterword: Lessons Learned from the Living Cases and from the Global Financial Crisis[1]

by Martin Hilb
(Switzerland)

International Board Foundation and its
International Center for Corporate Governance

The global financial and economic crisis has uncovered four major weaknesses in the direction and control of many large, publicly traded companies, especially in the financial services sector.

Firstly: With only a few exceptions, among them South Africa, most countries have, contrary to the OECD principles, adopted the Anglo-Saxon corporate governance guidelines, targeting the maximization of shareholder value.

Secondly: In contrast, successful companies in the financial services sector—such as family companies, partnerships and global companies—have only been affected to a limited extent by the financial crisis. Those companies most affected by the crisis did not dispose of holistic, measurable success criteria that added simultaneous value to customers, owners, employees and the society.

Thirdly: As a consequence, the vast majority of variable compensation packages were set for a short-term period, mainly yearly and using one often irrelevant financial ratio as opposed to nonfinancial ratios and competitive benchmarks. Furthermore, the integration of board, CEO and personnel compensation concepts has been largely neglected.

[1]This was first published in “Swiss Business” (January/February 2010) and is the internationally most cited paper of Martin Hilb.

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Fourthly: Accordingly, holistic monitoring, opportunity and risk management concepts have been largely disregarded on the board level of many large organizations. Four broad recommendations, each including two lessons for an improved corporate governance of large international publicly traded companies, can be deducted from these four weaknesses.

Keep It Situational

Corporate governance has to be adapted periodically to the changing conditions on an international, national and corporate level.

First Lesson

On a national level, it is necessary for corporate governance guidelines to be challenged. Several corporate scandals have provoked a precipitous adoption of the shareholder value maximization dictum. The related focus on quarterly figures is one of the main drivers of the financial crisis. This should be replaced by a holistic approach. Companies can compete and succeed with sustainable fundamentals only if simultaneous value is added to shareholders, customers, employees and the society.

Second Lesson

On an international level, the direction and control of subsidiaries, the so-called subsidiary governance, have to be critically reconsidered. Many companies that have been strongly affected by the financial crisis have failed in the field of subsidiary governance. Complex structured companies in the international arena should not govern their subsidiaries by "puppet boards" which neither direct nor control subsidiary management. They should be composed of competent, committed and independent local board teams. Those subsidiary boards should each be chaired by a member of the board of directors and not by a member of the management team of the above operative unit, as it is now being commonly practiced.

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Keep It Strategic

The financial crisis has shown that many boards do not have the know-how required for an effective direction and control of management in times of crisis. Power structures on the board level have often been designed in such a way that the question of Peter Senge arises: “How can a team of individual IQs above 120 have a collective IQ of 60?” became reality.

Third Lesson

The board of directors should possess in breadth the same market/product and functional know-how as top management, to be able to direct and control effectively and efficiently. Complementary team roles such as the roles of a critical thinker, a controller or a creative thinker have to be present on the board. Furthermore, each member should play the role of one stakeholder such as customer, shareholder, employee and society/environment.

Fourth Lesson

The sustainability of the company’s success cannot be ensured by a one-dimensional way of focusing on top executive value and quarterly results. Thus, the board has to develop holistic measures for the company success that differentiates the company from its competitors on the customer, owner, employee and societal level. The board should periodically measure and review success in each of the four dimensions.

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Keep It Integrated

The crisis has provided evidence that the globally dominant Anglo-Saxon soft governance laws has caused negligence for the softer dimensions of companies, including the successful selection, evaluation, remuneration, development and succession of members of the board of directors and especially of the managing board. However, misguided incentives and inadequate succession planning became realities within the current crisis.

Fifth Lesson

The financial crisis has confirmed that a company needs an integrated board, management and personnel compensation concept that is based on internal, external and company performance equity. In securing the success-based equity, the variable compensation packages have to account for both the long-term and the short-term success horizon of the company (e.g. for boards, 100% of bonuses on a 3-year basis; for CEO, 50% of bonuses on a 3-year basis and 50% on a 1-year basis). The rating has to be based on both financial ratios (e.g. EVA) as well as nonfinancial success indicators (e.g. voluntary customer, employee and public loyalty). These in turn have to be compared regularly to those of relevant competitors.

Sixth Lesson

Succession planning of the board and management represent one of the main weaknesses and are sources of risk for many companies. Based on a sustainable, competent succession planning system, the board of directors therefore, should nominate periodically and confidentially successors for all key positions on the board and managerial level.

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Keep It Controlled

Last, but not least, the global financial crisis has shown that many boards exhibit weaknesses in terms of controlling, ethical compliance, opportunity and risk management.

Seventh Lesson

The effective review of internal and external auditing, quality of financial reporting, holistic, opportunity and risk management and internal control, IT governance and communication and legal and ethical compliance are some of the most important board tasks.

The crisis has illustrated that for publicly traded companies, the greatest area for improvement is not within legal but within ethical compliance. This implies that not everything that is abided by law corresponds to legitimate action. Furthermore, it has to be understood that codices for proper behaviour are worthless if they merely exist but are not followed by the top decision makers in the company.

Eighth Lesson

The well-known victims of the financial crisis did not conduct periodic, objective and comprehensive evaluations with regard to the direction and control of the company. Therefore, companies should not await new regulations but proactively initiate a periodic multidimensional evaluation of the board's performance from the viewpoint of directors, (core) shareholders and management. That can help not just to overcome the current crisis but also to prevent future crises.

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Conclusion: Search for Sustainability and Common Sense

"Common sense is the least common of all senses". The global financial crisis has confirmed the Oscar Wilde quotes: "Common sense means that money should serve people, and not the other way around". This attitude should be kept in mind also when new corporate governance guidelines are developed for directing and controlling companies. Thus, whether companies rank among losers or winners of the financial crisis depends to a large extent on their willingness and ability to consider within a sustainable concept of multiple constituencies rather than just the interest of top executives and shareholders. The ability of companies to permanently add simultaneous value to customers, shareholders, employees and society will be decisive.

> Common sense means that money should serve people, and not the other way around.

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