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GOVERNANCE SCORECARDS AS TOOLS FOR BREAKTHROUGH RESULTS

Foreword

The best governance framework does not guarantee acceptance and implementation if it is not applied by companies, analysts and investors. But with the appropriate tools, good governance can be successfully applied in most countries.

Practical approaches for implementation are therefore essential. One of the proven ways to achieve this is the systematic analysis of the governance situation via a scorecard.

Since its first application in Germany in 2000, the scorecard-concept has found good reception on an international level.[1] The detailed approach described by Mr. Estanislao underlines the importance of the application of the scorecard for assessing the governance practices of companies by all parties concerned. Ideally, the scorecard should have the following features:

- Complies with the structure of the underlying corporate governance code.
- Contains an individual scoring process followed by a summary page which gives an overview by showing the partial scores achieved for each key-criterion as well as the total score.
- Enables comparisons across industries and countries.
- Enables companies to easily assess the 'reach' and the quality of their own governance situation.
- Is usable at no or low cost for companies and analysts/investors.
- Is readily available through the Internet.
- Ensures high degrees of usage via programmed tools (i.e. MS Excel).

[1] Apart from Germany, scorecards are in use inter alia in Croatia, Indonesia, Philippines, Russia, USA, UK.

The reader of the article finds encouragement to use the scorecard to achieve further governance improvements. This should help to steadily improve company performance and generate above market returns for investors. Could there be a better reason for intensive governance efforts?

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GOVERNANCE SCORECARDS AS TOOLS FOR BREAKTHROUGH RESULTS

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Manila, December 14, 2007. This paper was the basis for his Annual Lecture at the School of Economics, University of Asia & the Pacific, where Dr. Estanislao holds the title of "University Professor". Following tradition, the lecture is given in December of each year.

Introduction

Governance has become a mantra for doing the good and proper things. In public life, it has become more than a mini-rage: when things fail, a failure of governance is brought up as the explanatory variable; and good governance is presented as the alternative pathway to success. In the private sector, corporations are given ratings for the propriety of their governance practices: presumably, those that receive high ratings are governed well and can become the recipients of high market approval ratings, while those at the lower end of the ratings scale are to be dealt with as high-risk enterprises.

All this has been presumed. But does governance really matter? Does it really facilitate the achievement of breakthrough results? The answer for non-financial corporations has come in: for them, proper corporate governance does pay; those with good corporate governance practices are being rewarded with higher growth rates in sales. Moreover, the economies in which the regime for corporate governance leads to proper governance practices appear to enjoy higher rates of growth in real GDP, factor productivity, and investments. The econometric results shown in the study providing these answers are positive and significant; moreover, they appear to be robust.[2]

If good governance does lead to good breakthrough results, it is well worth our while to look more closely at what governance entails and in what way this may lead to higher levels of performance that brings about desirable results. We do need to get down from merely repeating governance as a mantra and into actually observing, as much as possible in day-to-day operations and actions, the discipline of governance. We do need to **meet the fundamental governance challenge, which is to connect**

[2] De Nicolo, G; Laeven, L; Ueda, K. (July 2007). "Corporate Governance Quality: Trends & Real Effects". IMF Working Papers. Washington D.C.

the values we aspire to hold and the actions we need to undertake so as to give flesh and substance to those values. The challenge is, indeed, how to walk the talk about governance.

The Talk about Governance

First and foremost, governance insists on *anchors*. The ebb and flow of events and circumstances can bring us out to sea, unless we have secured the anchors that keep us holding on to our core values, in pursuit of our permanent mission, by which we aim to make a difference and make the world we live in at least slightly better off because we exist. In addition, we should be clear about what we see ourselves becoming in the distant, yet already foreseeable future: this provides us with a vision, with its big, hairy, audacious goals, that we aim to achieve within a reasonably long horizon. These three—core values, mission, and vision—provide us with a fundamental governance charter, one we need to keep referring to, if we are to stay grounded on the core propositions, which we are never to compromise or trade away.

Second, governance insists on *balance*. With a governance charter as our guide, we then look at ourselves, the strengths and weaknesses we have as well as the opportunities and threats we face. There may well be outliers, unexpected, sometimes undesirable, events that we nonetheless have to consider. We need to weigh all these carefully. In weighing them, we need to have a balanced framework, one that enables us to consider the most important facets of day-to-day challenges. These facets include the financial and economic, of course. But they are not limited to these. There are others closely associated with the demands of learning and growth, of internal processes by which we serve and carry out our key functions and duties, and of the different constituencies we are called upon to serve. Understood broadly, these different facets have embedded in them others that we cannot relegate to the background: the environmental and physical facets, let alone the ethical and other duties imposed by social responsibility. Using this balanced framework, we make choices of the few strategic priorities we set for ourselves moving forward, with our governance charter as our fundamental guide.

Third, governance insists on *systems*. The priorities we choose can not be left as though they were unrelated to each other. In fact, we need to see the interdependence among them. We should be able to see that serving any one of them would facilitate our serving a few others as well. Thus, we should be able to string them together: we should trace through how one strategic priority facilitates another, or a few others; and those that are more closely connected with each other can be bundled together under a common strategic theme. In this way, a governance strategy map is drawn: thus, a systemic road map is formulated, which lays out how we intend to travel or move from our core values, in pursuit of our permanent mission, and into the realization of our vision.

Fourth, governance insists on *initiatives*. Under each strategic priority, we should determine how we measure progress towards milestones we must reach on our way towards realizing our vision. We need to specify a measure: as has been said often enough, unless we measure, we would not be able to manage properly. We need to be able to tell whether or not we are making progress and effectively moving towards clear milestones. These milestones are targets we need to meet by certain intervening dates (or years) on the way towards the end-year when our vision should be realized. And in order to meet these targets, we have to be specific and concrete about initiatives we need to undertake and action programs we need to pursue. It is at this level, at the level of concrete, specific initiatives and actions, where our governance charter takes on real flesh and substance. And this is because measures and targets have been etched in stone, insistently calling for actions that would bring about the corresponding outcomes and results.

Fifth, governance insists on *checks*. The initiatives undertaken and the actions taken need to be monitored. They have to be evaluated. They need to be checked on whether they are bringing about the corresponding outcomes and results in the manner and according to the schedule that had been set. Actual outcomes need to be compared with the anticipated outcomes embedded in the measures prescribed and the targets previously fixed. Those responsible for positive variances, taking into account the circumstances of actual operations, should be recognized and adequately rewarded. Negative variances, on the other hand, would call for some soul-searching with a view towards adopting appropriate remedies: generally, help should be extended to those in need of special assistance, and punishments meted out to those deserving of them.

Sixth, governance insists on *resolutions*. Making departments, units, and individuals accountable for the outcomes and results they produce from the initiatives and actions they take would turn out to be positive only if it is used as an opportunity for making resolutions and evoking a strong determination to carry them out. Good outcomes should become a basis upon which to obtain even higher and better results. Bad outcomes should be seized as an opportunity to introduce changes, initiate reforms, play catch up, and foster more effective team work. Indeed, each accountability review should become an occasion for renewal and re-commitment: there has to be a renewed commitment to the strategy map and its measures and targets, and more fundamentally to the core values, mission and vision in the governance charter.

In view of these six demands that governance insists upon, we can no longer refer to governance as a mantra, hollow of serious content. It is clear from its demands for anchors, balance, systems, initiatives, checks, and resolutions that governance is serious business. Meeting these demands would secure complementation between the values we aspire to hold dear and the outcomes the operationalization of those values in the governance charter should deliver.[3] Governance helps us ensure that we do not set the aspirational elements of the governance charter to one side with no influence upon the operational elements of day-to-day decisions and actions. Tying them neatly together—indeed putting aspirations and operations like glove to hand—**leads to the breakthrough results that make governance matter.** It makes governance matter positively and substantively.

Walking the Talk about Governance

To make governance matter and produce breakthrough results, we need to find a tool that would help us meet its insistent demands. That tool should enable us to deliver the anchors, balance, systems, initiatives, checks, and resolutions that good governance requires. **That tool is the governance scorecard**. This is forged and is made to work in a systemic manner, which means that: the ground has to be prepared for its use; the organization is aligned accordingly so it can be used properly; proper coordination is secured to use it effectively; and subsequently, a permanent mechanism is established to keep it always at the cutting-edge of effectiveness.

The ground is prepared for the governance scorecard by conscientiously making the case for change. The status quo, it should be abundantly clear, cannot and should not hold: there is a need for performance to be brought up to a much higher level. And the only way to do this is to have a portfolio of strategic priorities that we can rally around and be fully committed to. That commitment has to come from the core: thus, it should come from a clearly articulated set of core values, sense of mission, and a lofty yet realizable (within a reasonably long time horizon) vision. A strategy map needs to be drawn so as to highlight the strategic themes, and therefore the close inter-connection between the priorities within the portfolio of strategic priorities. This strategic orientation shifts the focus away from personalities, who come and go, with their own rather short-term ambition for legacies that may address tactically only a few issues. Instead, the focus shifts towards institutions, which remain and thus cry out with demands for their long-term development that can be secured by tapping into the strategic inter-connection between all key issues. In order to make this shift in strategic orientation, we need to create the occasion to step back from the hustle and bustle of operations. We need to go into a retreat of sorts, lasting a few days, to come up with a strategy map, which then demands a governance scorecard to track progress on clearly identified measures towards pre-set targets.

The way we operate would need to be aligned so the governance scorecard can be used. It is not enough to introduce governance changes at the top: in the case

[3] Kaplan, Robert S. and Norton, David O. 1996. The Balanced Scorecard. Harvard Business School Press. Boston, MA.

of corporations, at the Board level (e.g. Board committees may have to be set up); and in the case of other governance units, at the level where strategy and policy decisions are made, with collegial checks and balances (e.g. a multi-sectoral coalition may have to be set up). It is also necessary that corresponding strategy maps---with clear commitments, also according to clear measures, to pre-set targets---be formulated at lower, subsidiary levels in the organizational structure or hierarchy, preferably down to the level of individuals (these are referred to as subsidiary strategy maps). In other words, operating units at the lower level, and even individuals, should see themselves in the institutional strategy map. Through their corresponding subsidiary strategy maps, they should fit properly and snugly into the institutional strategy map. They should be able to identify what positive difference they are expected to make, and what contributions they need to commit to delivering, in support of the bigger institutional vision, in line with the institution's mission and core values. Thus, the governance scorecard would refer not only to the institution as a whole. It refers to the institutions' subsidiary operating units and even to individuals within them.

With the governance scorecard being applied to all levels, we **need to put in place a coordinating system to administer it efficiently and properly**. A governance office may have to be set up to try and pull together all the initiatives towards the execution of strategy. Vital and necessary tasks that may fall in between organizational silos need to be picked up and eventually slotted. Proper sequencing of closely inter-connected and mutually interdependent initiatives needs to be laid out and secured. Support resources need to be deployed and placed at the disposal of those units in critical need of them. Reporting and monitoring systems need to be put at an operational level to effectively track problems that need resolution, and progress that can be speeded up. An incentive mechanism would broadcast sterling achievements and stimulate operative resolutions to aim higher and produce much better outcomes the next time accountability reports are made and issued. The functions of a coordinating governance office charged with the multi-faceted demands of the governance scorecard become so crucial for strategy execution that they cannot be split up and assigned to several offices. A new, small albeit top-level office needs to be set up to take on this massive responsibility of administering the governance scorecard.

The responsibility of administering the governance scorecard with a view of bringing about breakthrough results entails **embedding the governance discipline in day-to-day operations so everyone's everyday job is permeated with it.** This is a tall order. It can be met only by promoting and deepening a governance culture founded upon ethics and social responsibility, in full cognizance of the fundamental governance charter. To be able to do so, we should be prepared to sustain the effort of instilling such a culture over the long haul. In this regard, the top-level office charged with the governance scorecard can be made to evolve into a fullpledged center for governance and leadership. It should then work to connect all the planning and budgeting functions with the discipline and demands of the strategy map. The planning for IT, human resource development, etc. and the corresponding budgeting, both for the medium and short-term, should be undertaken with a view towards properly executing the strategy map. Moreover, performance evaluation, from the very top and down to the last individual, should be undertaken with due consideration given to personal contributions being effectively made towards executing strategy.

It is clear from the above that the governance scorecard delivers on all six demands (for anchors, balance, systems, initiatives, checks, and resolutions) that governance insists on.[4] In summary, it does so by bringing about change that leads to breakthrough results.

- **It initiates change by making a strong case for it**. By preparing the ground for the governance scorecard, we set a new strategic orientation; and perhaps in a retreat, we forge a governance charter and formulate a *strategy map*, which become a common banner around which we should all rally.
- **It aligns the organization to become more compliant** with the demands of change. A few proper governance practices are introduced (a Board protocol and Board committees in a corporation; a multi-sectoral coalition in other governance units). Subsidiary maps specify positive commitments from operating units and individuals to the strategy map.
- **It takes out some insurance for the proficient and professional operationalization of change**. A small, high-level governance office is set up in order to administer the demands of coordinating strategy execution and of administering the governance scorecard itself.
- **It institutionalizes a governance culture, founded upon ethics and social responsibility**, in line with the governance charter. It embeds such a governance culture in all facets of operations. It seeks to imbue all levels with such a culture by installing a performance evaluation system, down to the last individual, using the demands of that culture as its frame of reference.

The governance scorecard is necessarily systemic.[5] It needs to be comprehensive, by anchoring itself on the governance charter and by constantly renewing commitments not only to higher aims and purposes but also to higher levels of performance and even to breakthrough results. It goes way beyond being a mere checklist of things to do and items to take care of. It goes into the very core of why certain things have to

[4] Kaplan, Robert S. (October 2007). "Creating Strategy-Focused Public Sector Enterprises". Balanced Scorecard Collaborative Papers. Washington D.C.

[5] Estanislao, Jesus P. (August 2007). "Governance Pathway: Milestones to Improvement". ISA Working Papers. Manila, Philippines.

be initiated and done in a proper manner, and why all items, in a balanced manner, should be taken care of to lead to very high-level outcomes.

Moreover, **the governance scorecard is custom-made.** It has to be designed to fit a specific portfolio of strategic objectives, each with proper measures and targets, which in turn ask for proper initiatives. It is the outcomes of these proper initiatives that need to be monitored, and thus scored. But the scoring is always for a higher purpose: it is not only to track progress; it is also to ensure consistency with the governance charter, and consistency of outcomes with the realization of a vision. Towards the vision that should galvanize and rally every one, commitments to performance are made not only from departments and working teams, but also from every individual. Thus, through the governance scorecard, the importance of the contribution of every individual is duly underscored.

Concluding Comments

The systemic character of the **governance scorecard puts into bold relief the imperative of wide participation in any governance process.** The determination of the fundamental governance charter and the choice of portfolio of strategic objectives may have to be a responsibility assigned to the very top of the organizational hierarchy. But the execution of strategy and the undertaking of necessary initiatives should be the responsibility of individuals and teams at all levels: down to the very last individual, **there has to be buy-in, commitment and involvement, and clear accountability for high-level performance that contributes to breakthrough results**. It is in this sense that the governance scorecard makes abundantly clear that governance is not only for the governors alone; it is as much for the governed. The teaming up and the solidarity between the governors and the governed, between those on top and the many others at the bottom, are crucial for governance to matter and produce breakthrough results.

Through the governance scorecard, those breakthrough results can be achieved precisely by the unbroken link between aspirations and strategy with actions and initiatives. The former inspire and guide; the latter substantiate and bring us to the desired destination. This link has been missing in too many instances of governance failure. All too often, we may have been great with our talk about our aspirations; or, we may have overwhelmed by our having to walk in many different uncoordinated directions. And the results we may have gotten have been underwhelming, bringing us to levels way below what we wanted to achieve. The governance scorecard now supplies us that missing link.

Having found the missing link, we should now apply the governance scorecard to governance at all levels**.** It should be used in the public governance of our nation. It should be spread more widely in the governance of the main institutional drivers of change in our national society: local government units, corporations, schools, and families. In all these instances as well as directly in personal governance, it should also be applied at, and brought down to, the level of the individual person. After all, it is at this level where breakthrough results are most needed; and once we deliver such results here, then we can more pro-actively influence governance at higher levels, where similar breakthrough results are also absolutely necessary.

About the Author

Dr. Jesus P. Estanislao is the Chairman and CEO of the Institute for Solidarity in Asia and the Chairman of the Institute of Corporate Directors in The Philippines. He holds the title of University Professor at the University of Asia and the Pacific. Dr. Estanislao has spent much of his career founding or reforming institutions, including successfully rehabilitating the Philippines Development Bank following the People Power revolution in 1986. The Institute for Solidarity in Asia, an independent, non-partisan, not-for-profit institution, seeks to improve the practice of public governance in The Philippines at all levels of government, gradually aligning the standards of public governance with global principles and best practices.

After rehabilitating the Development Bank of the Philippines, a task he completed in three years, Dr. Estanislao was appointed to the Cabinet of President Corazon Aquino, whom he served as Secretary of Economic Planning and Director General of the National and Economic Development Authority (1989), and later as Secretary of Finance (1990–1992). As the country's chief economic officer, he oversaw the economic recovery and reform program of a newly reinstalled democracy.

After he left government, Dr. Estanislao was asked to become the Philippine representative in APEC's Eminent Persons Group by President Fidel Ramos, whom he served as Adviser during the Philippine chairmanship of APEC in 1996. He also served as the Philippine representative in ASEAN's Eminent Persons Group on Vision 2020.

Dr. Estanislao holds a Ph.D. from Harvard University, where he was also a Teaching Fellow and Research Fellow. He obtained his MA in Economics from Fordham University, and his AB in Economics and Ph.B. (summa cum laude) from the University of San Carlos. He has been conferred honorary doctoral degrees by Angeles University, Xavier University, St. Paul University, and Manila Central University.

In 1992, Dr. Estanislao was awarded the Philippine Legion of Honor.

OUR MISSION:

Established in 1999, the Global Corporate Governance Forum is an IFC multi-donor trust fund facility located in the Corporate Governance and Capital Markets Advisory Department. Through its activities, the Forum aims to promote the private sector as an engine of growth, reduce the vulnerability of developing and transition economies to financial crises, and provide incentives to corporations to invest and perform efficiently in a socially responsible manner.

The Forum sponsors regional and local initiatives that address the corporate governance weaknesses of middle- and low-income countries in the context of broader national or regional economic reform.

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