16th Session of the Committee of Experts on Public Administration (CEPA)

24 to 28 April 2017

Written Statement by International Shinto Foundation (ISF)

Agenda item 3: Ensuring effective implementation of the Sustainable Development Goals through leadership, action and means, 3 (d): Development of principles of effective governance

4. "Development of principles of effective governance"

Regardless of type or scale of any company or organization, corporate governance means not just a legal compliance, but rather the soundness of its fundamental power mechanism. For making the governance effectively work, independent outside directors and auditors play crucial roles, and they should constitute the majority of the board which is the decision-making body of the organization.

In the recent Toshiba's accounting scandal, a third-party probe blamed aggressive earnings goals and a corporate culture that discouraged employees from questioning superiors. Toshiba was one of the first Japanese companies to adopt a western board structure which, with more outside directors, is considered more transparent in terms of corporate governance. But the board failed to function as intended. Although the company shaped the composition of the board beautifully, the top management was not seriously committed to make it really work and carry out its mission. In other words, the independent outer auditors and directors were on the board, but were not composed or authorized to carry out their crucial mission.

Corporate governance actually depends on outer directors and auditors who are independent from the organization. The most important point is what kind of and to which extent of missions are they authorized to carry out – they, as a team, need to have the authority to dismiss the top manager or top management team when agreed.

Corporate governance matters most, when the management is economically becomes wrong or is already in wrong direction and needs to be rectified. The rectification would be eventually nothing more than a dismissal and replacement of the top manager or the top management team.

Real governance is the actually effective system and mechanism that can dismiss the top management which has been the obstruction for the organization's sustainable development, and replace him/them with new manager or new management team.

Rightly functioning corporate governance means a sound working of its power mechanism. The mission of sound power mechanism is to carry out a right power mechanism (reasonable decision-making and implementation) and avoid wrong power mechanism (unreasonable decision-making and implementation).

Therefore, no matter how democratic and good the power mechanism nominally looks, if vacuum of power occurs and the top management team does not carry out their duty, then such power mechanism is not sound just like when abuse of power occurs.

On the other hand, no matter how the top manager is popular and beloved within the corporate, if he/she goes out of control and begins to abuse his/her power and to run the organization unreasonably, he/she must be dismissed without remorse.

When the balance swings to either extremity of vacuum or abuse of power and does not return, the organization starts collapsing. The real mission of corporate governance is to avoid the collapsing of the organization. Namely, governance's true mission is to stop the fatal damage on the organization, when something wrong takes place. And it is principally and ultimately borne by independent outer auditors and directors.

In consideration of internal control and governance, there is a tendency to plae an "internal control room" which is directly managed by the top manager in many organizations. It is aimed at quickly conveying any serious bad news to the top manager, but this system has a big flaw. That is, if the top manager is not subject to the internal control, then he/she can keep on doing wrongs even while the internal control room is operating.

The top manager, the most powerful person in an organization could be said the easiest to corrupt. Therefore internal control excluding him lacks the most important factor. In other words, even if internal control system is established with the top manager as the ultimate responsible, it wouldn't work unless he/she is seriously committed. Needless to say, internal control is not for the benefit of top manager, an organization does not exist for the benefit of top manager. Since an organization is a public organ of society, the internal control should be institutionally and systematically carried out for the benefit of all the stake holders.

In this point, independent outer auditors and directors play crucial roles. They, not the top manager, should be the final recipient of the report, so that the top manager himself becomes the target of internal control too. The independent outer auditors and directors should be authorized to replace the top manager or top management team, which means they should together constitute the majority of the decision -making board and dismiss him/her or them when agreed. When there is any possibility that the top manager is involved in wrongdoings, internal staff's position would not usually strong enough to reveal and rectify it. To do it , the independent outer auditors and directors need to have the power to decide if they agree. This means they should have the majority of votes.

In closing, since corporate governance is a live and real power mechanism rather than just a concept or system, it will take certain time to be actually rooted in the corporate culture of the organization. Unless all the members' sense of value fundamentally change, no significant improvement would be expected in its governance. Therefore, the organization – top manager, top management team and also outer officials must tirelessly make every efforts to infiltrate its philosophy of real governance throughout the entity.