EFFECTIVE GOVERNANCE & SYSTEMS THINKING
-BEYOND INDEPENDENT DIRECTORS' ROLES & RESPONSIBILITIES-

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SYSTEMS THINKING & EFFECTIVE GOVERNANCE?

There are many definitions of governance, but from a Systems Thinking perspective, the most useful definition is "seeing to it that the organization achieves what it should and avoids unacceptable situations." The key words in the definition are "seeing to it". Responsible governance is an arm's length relationship to the actual work of the organization.

The primary focus of governance occurs in the "helicoptor view", holding the whole organization as its primary concern. The governing body looks through the big picture lense of the future environment (Phase E, see *Figure 1* below), defining the purpose of the organization in terms that clarify the customer value to be achieved in the future, while at the same time defining the risk tolerance levels around prudence and ethics.

Governance is about translating owner expectations into actual results. This means defining:

A. What the organization should achieve and what should be avoided, primarily in terms of prudent and ethical behavior?
B. How should the achievement of identified outcomes and means utilized to achieve the desired results be measured and monitored?
C. What's the current assessment and status of organization's governance and its effectivenes? Where are the gaps? What are the critical governance issues and challenges facing the organization?
D. What plans, policies, strategies, processes, structures, actions, controls and culture need to be developed and implemented to address the gaps and achive the defined results without creating unacceptable situations?
E. What is changing or may change in the internal and external environment during and over the organization's planning horizon necessitating review and readjustment of its thinking and actions

Effective governance is proactive in defining outcomes, impacts and values. Once these factors are established, effective governance allows its system to work in its natural flow where the system organizes to deliver on the specified direction. *Effective governance does not interfere with that natural flow; but it does hold the system accountable to deliver on the prescribed outcomes and impacts and to integrate the defined value system to avoid the unacceptable situations.*
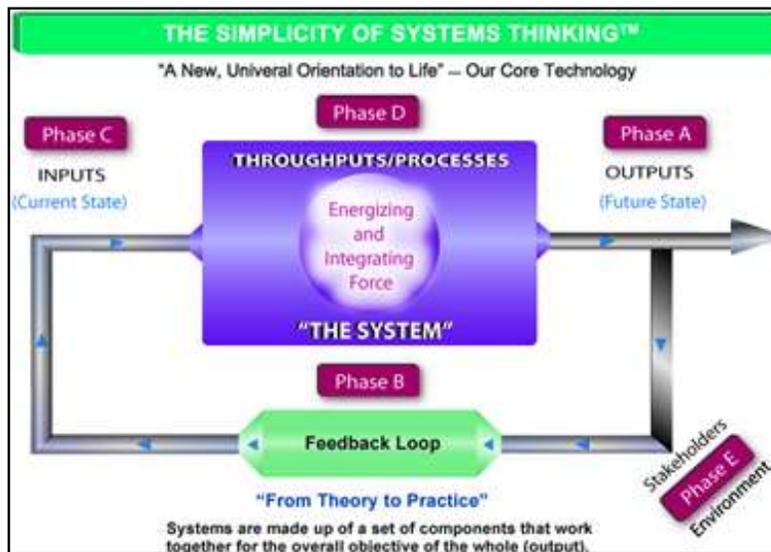
Figure 1: Systems Thinking Model (A-B-C-D-E)

Independent directors must understand, align and commit themselves to systems thinking framework and perspective of effective governance to justify their role and responsbilities. In fact, they should use the Systems Thinking Model to define their own vision, goals, strategies, measurements and actions in the context of their responsibilities as independent directors.

Effective governance at every level, including that of independent directors, requires:

1. Knowing for whom you are working
2. Assuring the organization is effective in delivering relevant stakeholder value
3. Assuring the appropriate balance between the hierarchical control and operational freedom
4. Discipline in exercising authority while properly empowering others
5. Fairness in making decisions and judging performance
6. Predictable and trustworthy behaviors
7. Keeping it simple yet integrated

GOVERNANCE & MANAGEMENT

Governance differs from management considerably. Governance focuses on big picture (whole system), while management works to optimize the parts so that whole system prerformance is maximized. In Systems Thinking, the whole is primary and parts are secondary. Thus without effective overall governance in place, management will be ineffective. Governance of a system rises to the helicopter view, while management focuses on effective performance in the trenches. The independent directors focus on both.

But where are the boundaries between governance and management?

Governance involves itself with the broadest decisions in its realm of authority. Management has the authorityi to make strategical and tactical decisions inside the parameters set by the next hierarchical level.

GOVERNANCE & SEVEN LEVELS OF LIVING SYSTEMS

Goevernance is necessary at every level of the Seven Levels of Living Systems or Natural Rings of Reality (see *Figure 2* below). Each level has its governance authority.Just as natural systems have a hierarchy, so do our human systems. In the work team or group level (Level # 4); the team leader is accountable for governing. In intergroups (Level # 4A), the division leader is generally accountable for governing. In the total organization (Level # 5), the CEO is accountable for governing. In Level # 5A, accountability for governing is usually held by a Board of Directors.
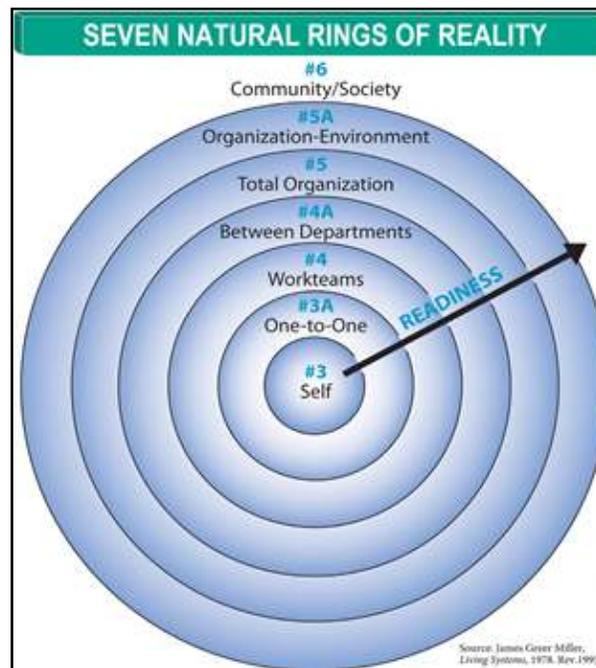

Figure 2: Seven Natural Riings of Real

There are key structural questions of governance at every level:

1. Who is the ownership group whose values and expectations influence our policy and decision-making?
2. What do these owners value in terms of what we achieve and how we get there?
3. Who are targeted beneficiaries/customers for our outputs?
4. What are the outcomes or impacts of the work we need to produce?
5. How will be know and measure the success of our work?
6. What are the cost constraints to the organization for us to achieve our outputs?
7. What is unacceptable to the owners in how we approach potential solutions?
8. What is the accountability for the outputs?
9. What is accountability for appropriate enabling processes? For example, what is our accountability for integrity to a budget? For ethical treatment of staff? For treatment of customers?

According to Karl & Susan, Priinciples of Haines Centre for Strategic Management, effective governance and independent directors should also recognize the importance of the following laws:

i. **_Holism:_** Governance sees the whole organization as it primary concern. It speaks with one clear voice to that organization
ii. **_Open Systems:_** Effective governance assures that the system is open. It gathers information about the future environement. It listens to the ownership to understand their expectations and keep them posted on material developments.
iii. **_System Boundaries:_** The boundaries between governance and operations are collaborative conversations, not a brick wall. Effective governance complements and integrates with operations to maximize results
iv. **_Input-Process-Output:_** Effective governance sees to it that the inputs from the environement are transformed through integration with its unique content, processes, structures and culture. Outputs from this transformation yield desired outcomes for stakeholders.
v. **_Feedback:_** Feedback stimulates learning and change. It is an essential part of accountability resulting from delegation of authrolty. Feedback begins with defining Key Success Measures and core strategic values. All activity is measured against these definitions.
vi. **_Entopy:_** Effective governance is the impetus to assure that "booster shots" are regularly injected through education, learning, feedback and accountability to reverse the effect of entropy or a tendency to lose steam or fall back over time. "Buy in" to an idea is relatavely easy but "Sta in" requires renewable energy from the open system environment.
vii. **_Hierarchy:_** Effective governance uses hierarchy appropriately to enable visionary leadership, future-oriented thinking, and collaboration among stakeholders, self-organizing systems, and flatter, highly productive structures. The key is strategic consistency with operational flexibility.
viii. **_Dynamic Equilibrium:_** Effective governance addresses the internal culture to refine it and then maintain it in dynamic equilibrium through standards of prudence and ethics.

BOARD GOVERNANCE

Keeping in mind the list of effective governance requirements above, let's apply this list to the role of a board of directors:

1. **Ownership**
   The Board of Directors is a microcosm of the owners. It is established to act in the interests of the owners. Board governance is a unique position created to be the link between owners and the operational organization. In systems thinking, the primary relationship of the Board of Directors is with the owners, not the CEO. Consequently, governance is a downward extension of ownership rather than an upward extension of management. The Board works for the owners to assure that the organization achieves what it should and avoids unacceptable situations.

2. **Governance Position**
   The Board holds a commanding leadership role through its governance position. With the ability to hire and fire the CEO, the Board of Directors holds authority that comes before all other authority in the organization. As a result of this "frst authority", the Board of Directors holds commanding authority in the organization and over the CEO. And yet, because the Board is a part-time authority, spending at most several days a year to do its governing work, it must properly delegate much of its authority in a manner that empowers others. Remember that governance is seeing to it that the organization achieves what it should and avoids unacceptable situations.

3. **Delegation by Balancing Control and Freedom**
There is a direct relationship in the balance of control and freedom in the whole system. The more control, the more the Board limits the potential for agility, nimbleness and fexibility when opportunities arise, resulting in non-optimal results. When the balance is appropriate, the Board can control the entire organization with a few well-chosen restrictions that clarify what is unacceptable in terms of prudence and ethics. When control and freedom are in proper balance, the Board enables maximizing results without undermining accountability for operations.

4. **Limitations with any Reasonable Interpretation**
Controlling the organization with minimum restrictions can only be done through a governing system where the Board defnes what is unacceptable at the broadest level of concern, but then allows the CEO to use any reasonable interpretation of those words in defning the key compliance measures to be monitored by the Board as a part of its feedback loop.

5. **Governance Discipline**
Effective governance is a disciplined sport. The board must set parameters for itself in terms of how far it will reach into the operational organization, preserving its governing time for the issues that truly belong to the Board and not the CEO. Boards do this through creating policies starting at the broadest, most inclusive level and as necessary continuing into more detailed levels that narrow the range of interpretation from higher levels.

6. **Fairness in Monitoring performance**
Fairness in judging performance begins with a discipline of not undermining accountability for performance. An undisciplined board undermines the accountability of the CEO through micromanagement and unpredictability, then holding the CEO accountable for decisions that were actually made by the Board. Fairness implies that the Board has defned all expectations in advance, requiring the CEO to identify reasonable interpretations of these expectations and corresponding measures of success. The Board monitors solely on basis of these expectations. Fairness implies that the Board defnes what the organization should achieve (Ends) and what is unacceptable in terms of prudence and ethics.

7. **Board Holism**
Effective Board governance requires board members to work as a cohesive, unifed team. The Board's authority is a group authority rather than a summation of individual authorities. The Board's relationship with the CEO is formed around accountability of the position, not around individual tasks. The Board's concern is for total organizational performance for which it holds the CEO accountable. The CEO is accountable to the full Board, not individuals on the Board.

8. **Board Governing Process as Enabler**
A key component in a systems-driven organization is to assure that the Board is acting as an enabling system for advancing the outputs of the organization. The Board itself needs to consider its own operating system that enables the organization to deliver on customer value. A Board needs to examine its practices to ensure there is: (1) clear defnition of roles and boundaries, (2) clarity of delegation, and (3) rigorous monitoring for accountability of both the CEO and itself. Boards that are personality driven rather than systems-driven can create considerable upheaval in organizations. A systems-driven organization also needs a systems-driven board that is accountable to the ownership. Using a clear governance model provides the Board an objective way to measure its own consistency with a systems approach to governance.

Surprisingly, there is little research that demonstrates the impact of governing on an organization. There is, however, a theory-based model for a systems approach to governance. This model is called Policy Governance. Developed by John Carver it is the only coherent, comprehensive systems-based model of governance for Boards of Directors. The conceptual model has full external utility and can be applied at every level of governance in the organization

CONCLUSION

The Board of Directors is the body that begins this systemic pattern of accountability in the organization. The Board is accountable to the owners for the outputs of the organization and for integrity to its own rules of engagement. The CEO is accountable to the Board for the outputs of the operational organization in terms of Key Success Measures defned toward the achievement of Ends plus integrity of operations to the defned policies focused on enabling processes (administrative functions). All staff positions below the level of CEO are responsible for the delegations of authority that flow from the CEO, but the performance of the CEO is synonymous with the performance of the total organization.

As per IFC, the purpose of identifying and appointing independent directors is to ensure that the board includes directors who can effectively exercise their best judgment for the exclusive benefit of the organization. If so, it becomes pertinent for the independent directors to take a systems view of the organization's vision, goals, culture, stakeholder involvement and expectations to find the right context for their roles and responsibilites.