

CHAPTER

1

CORPORATE GOVERNANCE FRAMEWORK

What corporate governance is, which rules and documents make up a company's governance framework, and how to apply them in proportion to the company's size and ownership.

IN THIS CHAPTER

1.1	The concept of corporate governance	16
1.2	Corporate governance framework	17
1.3	Proportionality in governance	19

1.1

THE CONCEPT OF CORPORATE GOVERNANCE

Corporate governance is "the system by which companies are ***directed and controlled***"[1], and the concept goes beyond formal legal requirements, setting a higher standard. The term corporate governance was coined in the mid-1970s together with ***agency theory,*** which prevailed in Anglo-Saxon countries and focused on large, centralised, hierarchical organisations that were then the key drivers of economic growth.

In 1984, ***stakeholder theory*** emerged, seeking to explain how value creation is possible in a world of great change and turbulence, to address the problem of the ethics of capitalism and to outline the managerial mindsets required. It is inherent in the continental corporate governance model through the composition of the Board (e.g. employee representation in Germany) and the consideration given to the interests of different stakeholders.

In 1991, ***stewardship theory*** was introduced, arguing that executive managers essentially want to be good stewards of the corporate assets and that their own reputation is tied to the firm's performance. Focus is placed on the overall design of the organisational structure so that managers can be empowered to take action. Stewardship codes are more principles-based than rules-based ("*comply or explain*") and should therefore provide more flexibility and enable Boards to maintain a long-term focus. Yet this approach does not incentivise innovation; moreover, legal reforms in different jurisdictions are so frequent that they create "compliance fatigue".

While limited liability joint-stock companies appeared in the mid-19th century, the world's first corporate governance code was developed by Sir Adrian Cadbury only in 1992, focusing on listed public companies. Before that, the role of directors was defined by company law or by financial and auditing standards. Recent developments indicate that all entities need good governance, and the ISO 37000:2021 Governance of Organisations Standard has been approved, guiding the governance of organisations of all industries, sizes, geographies, structures and objectives towards meeting their obligations so that their purpose is fulfilled.[2]

1 Cadbury Committee (1992), Report of the Committee on the Financial Aspects of Corporate Governance, London.
2 ISO 37000:2021, Governance of organizations – Guidance.

1.2
CORPORATE GOVERNANCE FRAMEWORK

A corporate governance framework serves as an important supporting structure: a set of rules and procedures that defines decision-making and accountability roles and the way in which the Board performs oversight of the company's operations. A well-established corporate governance framework promotes efficient operation of the company, accountability, fairness and openness in how the company operates and interacts with its stakeholders.

A good governance framework unifies decision-making, operational, risk management, reporting and financial processes to keep the Board informed and to help the Board make considered, data-based decisions that ensure the implementation of the company's strategy.

It is imperative that **governance documentation** is accurate and kept up to date. These documents establish the rules by which the company is governed, set out the rights and obligations of the shareholders, the Board and management, and provide evidence to shareholders and all other stakeholders of the governance processes and procedures in place.

Policies, codes, guidelines and other governance-related documents approved by the Board are important because they address relevant issues, such as the rules and principles for oversight of the company's operations, accountability, reporting and communications. They ensure compliance with laws and regulations, reflect the culture of the organisation, give guidance for decision-making and risk appetite, and streamline internal processes. These governance documents should be current and in line with legislation, regulations and good practice, as well as with the long-term goals and strategy of the company. They should not contain confidential information, because they should be made publicly available (for example, disclosed on the company's website) so that everyone understands the way the company is governed. An indicative list of the topics to be covered by corporate governance policies is provided in Annex 2.

A corporate governance framework should encompass:

1. Governance structure: the relationship between the shareholders, the Board (including its committees) and executive management
2. Roles and responsibilities of the shareholders, the Board, its committees and the CEO/Management Board
3. The appointment process for the Board and its committees

4. Performance of the Board and its committees (self-evaluation and performance improvement action plan), and review of the required Board competencies and composition
5. Remuneration of the members of the collegial bodies and the CEO/ Management Board
6. Ethics, “tone at the top” and company culture: how the company conducts itself and behaves
7. Strategy development, renewal and oversight of its implementation
8. Monitoring of the company’s performance (financial and non-financial)
9. Oversight of internal control, risk management, compliance, and internal and external audit
10. Relationship and engagement with shareholders and all other stakeholders
11. Disclosure and reporting (financial and non-financial, internal and external), transparency and accountability
12. Regular review and improvement of corporate governance practices within the company

To start building a corporate governance framework for a particular company, aim to answer these questions:

1. Who are the people with authority in your organisation, and what kind of authority do they need to have?
2. What information do those people need to access, and when?
3. What does the organisational structure look like?
4. How does the structure influence how decisions are made?
5. What are the organisation’s reporting obligations?
6. How does information need to flow inside and around the company?
7. What is the relationship between company units – and does this present any challenges in terms of accountability, authority or responsibility?
8. If there is a group of companies, how is the relationship between the group companies and the parent company established?
9. How is the relationship built with shareholders and all other stakeholders?

1.3
PROPORTIONALITY IN GOVERNANCE

Good corporate governance is not a "**one-size-fits-all**" model. While the core principles of governance are broadly the same for all companies — clear accountability, effective oversight, transparency, integrity, proper risk management and long-term value creation — the way these principles are applied should be proportionate to the company's size, ownership structure, complexity, public interest and risk profile. Proportionality does not mean weaker governance. It means applying governance practices in a practical, relevant and cost-effective way, so that governance strengthens the company rather than becoming a formal exercise.

For **listed companies**, governance expectations are usually the highest. They raise capital from public markets, have dispersed shareholders and are subject to market disclosure, investor scrutiny and regulatory requirements. Their Boards are expected to have a high level of independence, well-functioning committees, robust internal control and risk management systems, transparent remuneration practices, regular Board evaluation and high-quality disclosure. In listed companies, governance is not only a matter of internal effectiveness, but also a key condition for market trust, investor confidence and access to capital.

State-owned enterprises (SOEs) and municipally owned companies require governance that protects the company from political interference while ensuring proper accountability to the state, the municipality and the public. Their Boards must act in the best interests of the company, while recognising the company's public policy objectives where these are clearly defined by the owner. Proportionate governance in SOEs should include transparent selection and nomination of Board members, a clear letter of expectations from the owner, independent from political interference Boards, objective performance targets, transparent reporting, high-quality disclosure, and a clear distinction between the roles of the owner, the Board and management. In SOEs and municipally owned companies' governance is not only a matter of internal effectiveness, but also a safeguard against political influence which ensures the company's best interests and transparency.

Group companies create additional governance challenges because responsibilities are divided between the parent company and subsidiaries. The parent company may set group strategy, policies, risk appetite, reporting and accountability standards, but each subsidiary Board must still understand its own legal duties and act in the interests of the company it governs. Proportionate governance in groups should define reserved matters, delegation of authority,

reporting lines, intra-group transactions, risk oversight and the role of subsidiary Boards. Particular care is needed where subsidiaries operate in regulated sectors or different jurisdictions, have shareholders outside the group or are listed companies.

Private companies are not due to the same level of public disclosure as listed companies, but they still benefit significantly from sound governance. For growing private businesses, good governance helps professionalise decision-making, clarify the roles of owners, Boards and management, attract financing, manage risk and prepare for succession, sale, acquisition or listing of the company. In smaller companies, proportionality may mean a simpler Board structure, fewer formal committees and lighter reporting processes. However, the essential elements should remain: a clear strategy, competent and independent challenge, reliable financial information, proper controls and disciplined decision-making.

Family businesses require particular attention to the relationship between family, ownership, Board and management. Their strength often lies in long-term commitment, entrepreneurial culture and strong values. At the same time, they may face specific governance risks, including informal decision-making, unclear succession, conflicts between family members, or difficulties in separating family interests from company interests. Proportionate governance in family businesses should therefore include clear rules on family participation in the decision-making, succession planning, related-party transactions, dividend policy, employment of family members and the role of independent Board members. A family council, shareholders' agreement or family charter may be a good starting point in establishing good governance principles in the business.

In all types of companies, **proportionality should be based on substance rather than form**. The question is not whether the company has copied the governance structure of a large listed corporation, but whether its governance system is adequate for its purpose, risks and stakeholders. A smaller company may not need several Board committees, but it does need reliable financial controls. A family business may not need extensive public reporting, but it does need clear succession rules. An SOE may have public policy objectives, but it still requires commercial discipline and professional oversight. A group subsidiary may follow group policies, but its Board must still ensure its interest.

The **Board should regularly assess** whether the company's governance arrangements remain **proportionate and effective**. As companies grow, raise capital, internationalise, become more complex or acquire greater public significance, their governance should also evolve. Proportionality is therefore not a

justification for minimal governance; it is a disciplined approach to applying good governance in the right way, at the right level, and at the right stage of the company's development.

KEY TAKEAWAYS

A. Corporate governance is the system by which companies are directed and controlled. It goes beyond legal compliance and sets a higher standard of accountability, oversight and transparency.

B. The corporate governance framework is the set of rules and procedures that defines who decides what, who is accountable to whom, and how the Board oversees the company. It should be documented, kept up to date, aligned with legislation, good practice and the company's strategy, and made publicly available.

C. A complete framework covers twelve elements: from governance structure and roles, through Board appointment, performance and remuneration, ethics and culture, strategy, performance monitoring and oversight of control and risk, to stakeholder engagement, disclosure and regular review.

D. Building the framework starts with practical questions: who has authority, what information they need, how decisions are made, what must be reported, and how the company relates to its group, shareholders and other stakeholders.

E. Good governance is not "one-size-fits-all". The core principles are the same for every company; their application should be proportional to the company's size, ownership structure, complexity, public interest and risk profile.

F. Proportionality is based on substance rather than form and never justifies minimal governance. Listed companies, SOEs, groups, private companies and family businesses each have specific priorities, but all need clear roles, reliable controls and independent challenge.

G. Governance must evolve with the company. The Board should regularly assess whether the governance arrangements remain proportionate and effective.

QUESTIONS FOR THE BOARD

1. *Do we have a clear, written and up-to-date corporate governance framework, and when did the Board last review it?*
2. *Are the roles and responsibilities of the shareholders, the Board, its committees and the CEO/Management Board clearly defined and understood, including which decisions are reserved for whom?*
3. *Are our governance documents (articles of association, Board charter, policies and codes) consistent with legislation, good practice and our strategy, and are they publicly available?*
4. *Does the Board receive the right information, at the right time, to exercise effective oversight and take considered decisions?*
5. *Which of the twelve elements of the governance framework are weakest in our company, and what is our plan to strengthen them?*
6. *Is our governance proportionate to our size, ownership structure, complexity, public interest and risk profile: neither copied from a large listed company nor reduced to a formality?*
7. *If we are a group company, an SOE or a family business, are the issues specific to us, such as reserved matters, the owner's expectations or succession, properly addressed?*
8. *As the company grows or changes, what would trigger a review of our governance arrangements?*