

Order in the boardroom

The collapse of Enron, the massive Houston-based energy giant, has plunged the world's financial, accounting and legal communities into deep waters. Canada has been pulled in too, with new rules and regulations coming down the pipe to ward off "another Enron" north of the border. But what about the boards in the not-for-profit sector? How do regulatory bodies measure up? *Engineering Dimensions* takes a closer look.

by Karen Hawthorne

T

he fallout from the Enron scandal is rapidly spreading northward, and the debate over reforms to prevent “another Enron”

is already affecting Canadian corporations, accounting firms and law firms. This year, the Ontario Securities Commission expects to introduce new independence rules for boards’ audit committees. Accounting regulators are developing new rules requiring companies to expense their employee stock options, and Canada’s auditors will come under the supervision of a new independent regulator.

The recent lessons from Enron, WorldCom, and others, demonstrate that the responsibility for clear financial reporting lies with the board of directors—and this accountability cannot be delegated away.

Insolvency and restructuring lawyer, Robin Schwill, LLB, says it’s the director’s role to ensure that there is a level of integrity in the organization’s accounting and financial systems, and that appropriate internal controls are in place. The auditors are not bloodhounds searching for and sniffing out all irregularities with their annual review.

“There may be a misunderstanding (by board members) who think that, ‘Oh well, if I’m passing the financials off to the accountant and the auditor, they are setting the financial reporting policies and practices of the business for me,’” says Schwill, who teaches MBA students at York

University’s Schulich School of Business how to analyze and interpret what financial statements are really saying.

Boardroom vacancy

As harsh scrutiny continues to zero in on the people at the top of corporate governance, potential directors are thinking twice before accepting a seat on a board. There is the fear of exposure to litigation, inadequate liability insurance and the increased workload. Performance standards and expectations on board members are going up, and boards must be held accountable for and take an active role in overseeing the organization’s management team and its strategic plan—not to mention maintaining its fiscal responsibility.

“Because of the scrutiny involved now, it will be more prestigious to serve on a board,” says Marie-Josée Roy, PhD, who teaches strategic management in Laval University’s MBA program, faculty of administrative science, and conducts research on corporate social responsibility and corporate governance.

Workload for directors will increase and training will be required to familiarize directors with the organization’s purpose and how that purpose is realized, but the payoff will be better use of the expertise and talents of those people who have been elected or appointed to serve on the board.

“People will know, in terms of competency and the amount of time, what is required of directors,” she says. “It’s not

rubber-stamping anymore, there’s a real job to do as a director.”

Shakedown

Most damaging in the aftermath of corporate accounting scandals is the shaken public confidence in good governance and professional ethics. As the dust settles, nagging questions remain: Can professionals be relied upon to do their jobs well and ethically? Is the traditional high regard for professionals, including lawyers, doctors, accountants and engineers, in jeopardy? And are the governing bodies that regulate these professions really doing their jobs?

Although regulatory associations are located a long way from Wall Street, these recent events have ramifications for all elected boards of directors. Not-for-profit organizations don’t have the same rewards-based motivation as Enron or WorldCom, and their bottom-line doesn’t impact a stock price. But the fallout has raised a warning flag, reminding directors that members, like investors, expect transparency and accountability in return for their money.

“I think on some level the trust has been shaken so badly that making sure that financial information is available to stakeholders is not enough,” says Roy.

She advocates a “balanced scorecard” approach that turns financial statements into an easy-to-read financial roadmap charting where the organization has been with its funds, its achievements and where it’s headed. The approach allows companies to

Regulating the medical profession: The College of Physicians and Surgeons of Ontario

PEO’s counterpart in the medical profession is the College of Physicians and Surgeons of Ontario (CPSO).

CPSO issues certificates of registration to doctors to allow them to practise medicine, monitors and maintains standards of practice through peer assessment and remediation, investigates complaints against doctors on behalf of the public, and disciplines doctors who are guilty of professional misconduct or incompetence.

The college also offers an on-line listing of physicians, and is the only organization in the province that provides this service for members of the public. All doctors in Ontario must be members of the college to practise medicine in the province. The role of the college, as well as its authority and powers, are set out in the *Regulated Health Professions Act* (RHPA), the *Health Professions Procedural Code* under the RHPA, and the *Medicine Act*.

CPSO’s governance is structured much like PEO’s. A Council sets direction and policy for the organiza-

tion and sets parameters within which staff must operate. The RHPA stipulates that the Council is composed of at least 32 and no more than 34 members comprising:

- ◆ 16 physicians elected by their peers on a geographical basis every three years;
- ◆ three physicians appointed from among the five faculties of medicine (at the University of Western Ontario, McMaster University, University of Toronto, Queen’s University and the University of Ottawa) for a maximum four-year term; and
- ◆ no fewer than 13 and no more than 15 non-physician or “public” members appointed by the provincial government for terms decided by the government.

CPSO is headquartered in Toronto. The college does not have a system of chapters or branches like PEO; elections for Council members are carried out through the college’s electoral districts.

In terms of outreach activities, senior staff travels to the province’s five medical schools and special events to speak about CPSO and professional issues.

The college president is elected from and by Council and serves a one-year term. Council members sit on committees of the college and serve on task forces as the opportunity arises.

Council meetings are held five times a year, at which time the activities of the college are reviewed and matters of general policy are voted on. College staff, headed by the registrar, carries out the day-to-day functions of the college.

Among recent initiatives, CPSO has developed a practical plan to address the province’s urgent need for more doctors. Foreign-trained professionals practising in other jurisdictions can now access a streamlined assessment and registration system. Where required, a trained assessor will visit the candidate for a day’s evaluation, reviewing patient charts, and interviewing patients and colleagues.



THE HOT SEAT

set performance standards, show how standards have been met or how the company is addressing roadblocks.

"The core of the whole thing is good communication to your membership—providing relevant, pertinent and timely information that is easy to understand," says Roy.

That communication goes beyond an annual report, and is shared through member publications, reports and up-to-date website postings.

Roy used this approach to help develop the new corporate governance guideline released by Certified Management Accountants of Canada (CMA Canada) last September, designed to improve the performance of company boards and CEOs. The guideline encourages companies to focus on setting measurable governance objectives, and to report on their success in achieving these objectives—acting as a monitoring system of checks and balances for its stakeholders.

"It's systemic," says David Fletcher, vice president, public affairs, CMA Canada. "Many companies fail because their boards lack a strategic performance measurement and process. This results in inadequate board oversight and control, which allow improper activities to take place," he says. CMA Canada's corporate governance guideline is designed to help a board understand the risks associated with its company's strategy, and put into place control systems to flag activities that could hurt the company and its stakeholders. "These systems could, for example, provide early detection of practices that might distort financial results and mislead investors about the true state of a company's competitive position," says Fletcher.

In 2001, CMA's board approved a set of strategic performance measures based on the balanced scorecard approach. Next, outcomes the organization wanted to achieve with respect to the strategic plan were determined, such as outcomes that addressed marketplace relevance and recognition, product differentiation, operational performance within the organization and membership growth.

"What we're trying to do is to make sure that we're meeting goals in certain areas," says Fletcher.

Liability concerns are running rampant at the board level of publicly traded companies. However, board and council members of regulatory bodies are generally better protected from litigation than their equivalents in the private sector.

According to PEO Councillor David Sims, a retired lawyer, directors of regulatory bodies are protected by statute that protects the individual from litigation as long as that person is acting conscientiously and in good faith. Organizations such as PEO have bylaws indemnifying directors, and in addition carry directors' liability insurance. These provisions are generally "universal" or "you would be foolhardy to serve on any board," says Sims. "You'd never get anybody to sit on the board."

PEO's case

The *Professional Engineers Act* has subsections on Immunity and Councillor Indemnity-45(1) and 45(2)—which also protect employees and committee members, providing that they are acting in good faith in the performance or intended performance of a duty under the Act.

"This immunity has been upheld by recent court decisions," says Roger Barker, P.Eng., PEO's former CEO/Registrar.

In addition, PEO carries directors' and officers' insurance for further protection and coverage of legal costs in defending actions that are brought against the association, officers and employees.

For example, CMA Canada wants to make sure that its members are in demand in the marketplace. A market survey was conducted to determine a percentage level of employer understanding of the CMA designation and the skill set it represents.

"We go back to that benchmark to see what the increases are, over time, over each year," says Fletcher. "The services and programs that we are putting in place are having a positive impact—if they start to dip, we know that we have to make some adjustments."

These guiding principles can be adapted and applied by other public sector bodies to better demonstrate their transparency and reliability.

As Schwill points out with regard to regulatory associations: "You're giving spoonfuls of money to this quasi-bureaucracy and you want to know the value of where that money is going and why."

Most annual reports from the non-profit sector report on activities carried out to fulfill the mission statement and the dollars

Order in the court: The Law Society of Upper Canada

The Law Society of Upper Canada (LSUC) regulates the legal profession in the public interest according to Ontario law and the society's rules, regulations and guidelines.

Ontario legislation—primarily the *Law Society Act* and Regulations made under the act—authorizes the society to educate and license Ontario's lawyers and regulate their conduct, and competence.

LSUC bylaws and *Rules of Professional Conduct* set out the professional and ethical obligations of all members of the profession. Members failing to meet these obligations are subject to the society's complaints and discipline process, governed by the *Rules of Practice and Procedure*.

The society offers public services, such as a Lawyer Referral Service that matches individuals with local lawyers with the proper expertise, a directory of certified specialists and the Lawyers Fund for Client Compensation, which helps clients who have lost money because of a

lawyer's dishonesty. A member directory, with lawyers' contact information, is also available on-line.

The society provides support for lawyers through its Professional Development and Competence programs. These include Continuing Legal Education (CLE) programs, Advisory Services, and Practice Review. LSUC's governance is modeled much like PEO's wherein a "policy board" sets direction and policy for the organization and sets parameters within which staff must operate.

Headquartered in Toronto, LSUC also has a small satellite office in Ottawa to help facilitate regulatory functions in the northern part of the province. In contrast to PEO, LSUC does not have a system of chapters or branches that contributes to its governance; elections for board members are carried out through the society's electoral districts.

The society is governed by a board of 48 directors known as Benchers, 40 of whom are

spent in doing so, says Schwill. "How do you go from describing the activities to demonstrating value? That's where you need to interpose the balanced scorecard approach and develop measures of success."

The presentation of PEO's financial statements has been an issue in some recent annual general meetings, especially the 2002 AGM in Ottawa, says Roger Barker, P.Eng., the association's former CEO/Registrar. A Council motion requesting a more detailed breakdown was passed at the Council meeting on January 24, 2003.

"We will, therefore, be providing members at the AGM with more information on the breakdown of expenses," says Barker. (See pp. 41 to 47).

PEO has a number of communication vehicles to keep members and the public it serves informed and up to date about its core regulatory business and Strategic Plan. Member publications, the website, annual reports, chapter meetings and a speaker's bureau all serve to profile the association's functions and create an opportunity for dialogue (see www.peo.on.ca).

Masterminding

The Canadian Institute for Health Information (CIHI) is drawing a lot of attention to itself these days as funding

and strike action continue to threaten Canada's healthcare system.

Winner of the Conference Board of Canada/Spencer Stuart 2003 National Awards in Governance—Not-for-Profit, CIHI is an independent, pan-Canadian, not-for-profit organization working to improve the health of Canadians and the healthcare system. It provides quality, reliable and timely health information, with on-line databases of health human resources, for example, and reports on myriad health-related issues. CIHI information is used to develop health policy and effective management strategies, and promote public awareness of health determinants.

The history of its governance is noteworthy—and the focus of a presentation by CIHI Chair Michael Decter at the Conference Board of Canada's conference on governance in Toronto this January.

CIHI was incorporated in 1994 through the merger of four organizations. Difficulties resulting from merger issues and no new money led to an operational review in 1997 and a new board structure in 1998 that saw the establishment of an independent chair, better regional representation elected by jurisdiction, and a balance of government and non-government directors.

Its revamped governance, among other successes, initiated a national strategic planning process for priorities and needs. It acquired funds based on its strategic roadmap and established a balanced scorecard for organizational performance.

Its board members provide strategic direction to CIHI, strategic guidance to its health statistics division, and advice to the Conference of Deputy Ministers in matters of health information.

CIHI's planning and evaluation steps to success include: an annual planning and strategic-setting exercise, periodic in-depth reports on issues, constant "touching-base" with clients (e.g. ministers, deputy ministers, regional CEOs), two-minute CIHI evaluations at board meetings, and a biannual self-appraisal of the board.

Today, CIHI shows significant results. Its revenues have tripled since its inception. It fulfills its primary mandate of issuing regular reports on performance trends in healthcare, and increasing its reach, visibility, sustainability and use of its products. It has

increased its cooperative and collaborative ventures, including its far-reaching joint venture with *Maclean's* magazine on health system performance.

Wake-up call

Board exposure in the post-Enron era is a wake-up call for change, putting the role of governance front and centre.

"I think that we can see this as a positive—it's an opportunity to reassess our corporate governance," says Roy. Reforms for publicly traded companies call for the CEO and chair to be separate jobs, and executive sessions be held without the CEO to foster more board independence.

Turning stricter rules and regulations into a positive, Roy says, "depends on how the CEO is willing to take this opportunity and leverage all the skills that are around the table. They're bright people, chosen because of their knowledge, so let's make sure they all contribute."

Ultimately, governance is the backbone of an organization. Good governance is of strategic importance to all organizations, particularly regulatory bodies whose function is all about governance of the professions.

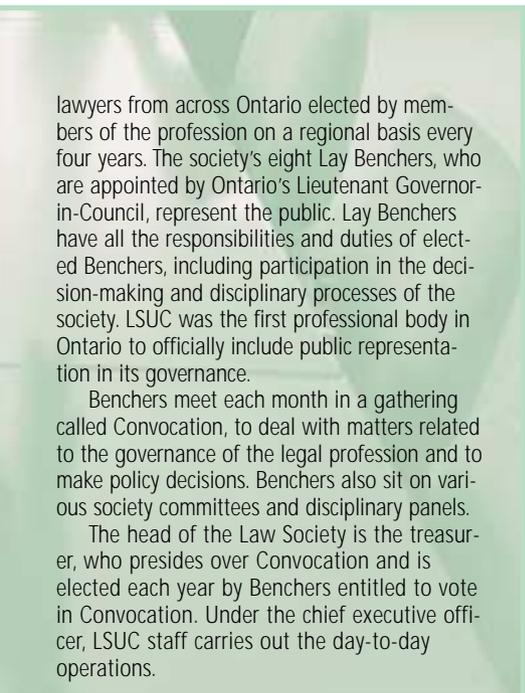
PEO Councillor David Sims, Q.C., a member of its Governance Task Force, says the threshold question ought to be: Does the organization exist for the members/licensees or the public? "The next question is what is its core business? I argue that for regulatory bodies it is competence assurance," says Sims. (For more, see "Looking for Good Governance" on p. 26).

The business of competence assurance should never have been more in demand than today, given the shake-up of public confidence.

Serving the public interest is top priority, says Sims. The majority of directors at all regulatory bodies comprise members/licensees of the organization, while other directors comprise a range of professionals to represent the community at large and enhance public accountability.

That representation is important because these organizations exist to serve the public interest.

"They are not member organizations like a fraternity that exist to advance the interests of the members—they're here to regulate," says Sims. ❖



lawyers from across Ontario elected by members of the profession on a regional basis every four years. The society's eight Lay Benchers, who are appointed by Ontario's Lieutenant Governor-in-Council, represent the public. Lay Benchers have all the responsibilities and duties of elected Benchers, including participation in the decision-making and disciplinary processes of the society. LSUC was the first professional body in Ontario to officially include public representation in its governance.

Benchers meet each month in a gathering called Convocation, to deal with matters related to the governance of the legal profession and to make policy decisions. Benchers also sit on various society committees and disciplinary panels.

The head of the Law Society is the treasurer, who presides over Convocation and is elected each year by Benchers entitled to vote in Convocation. Under the chief executive officer, LSUC staff carries out the day-to-day operations.