ISSN 2616-5902 Vol. 3, Issue 10: 44-46, DOI: 10.25236/AJBM.2021.031008

Evaluate the importance of the board of directors to the corporate governance of large listed UK firms

Siyu Du

Beijing Jiaotong University, Weihai, Shandong, 264401, China

Abstract: *People sometimes question the centrality of the board of directors as the British governance reform policy debate, because the daily impact of the board is hard to be perceived. However, when things go wrong, they become the focus of attention (Adams et al, 2010). Agency theorists believe that the board has two main functions: decision management and decision control (Amama & Grzegorz, 2014). The UK Code (Financial Reporting Council, 2014, p. 1) reflects the difference, pointing out that "corporate governance is the processes and a combination by which companies are directed and controlled" and "the board of directors is responsible for corporate governance". This paper will start from two major aspects of corporate internal governance and external governance, and evaluate the importance of the board of directors in agency relationship, independence and supervision, and crisis respectively, so as to illustrate that the important role of the board of directors in comprehensive corporate governance is inevitable and crucial, and the core position of the board of directors in the corporate governance mechanism.*

Keywords: *Board of directors, Internal and external governance, Importance and status*

1. The practical role of the board of directors

The board of directors has taken a lot of actions to coordinate the interests of stakeholders, laying the foundation for a good corporate governance framework. The board of directors acts as the agent of shareholders and acts in their best interests. One of the challenges often faced by the board is to coordinate the conflicts of interests between management and shareholders (Nicholas, 2018).

Communication and coordination are important components of good corporate governance, in which the board of directors plays a great role. First of all, coordinating a 2 good working relationship with the manager is more conducive to setting an example of internal governance between the board and management. Given that corporate governance is rooted in ethical conduct and business principles (Terry and Abigail, 2015), the board of directors is inclined to hire honest executives who are more in line with the strategic preferences of the directors to prevent wicked problems such as fraud from occurring and to promote good corporate governance environment, and the board of directors cultivates mutual trust through regular communication with senior management. Furthermore, the board is required to update shareholders on all relevant events and future plans to inspire trust among investors, as firms with poor governance structures are more likely to grab benefits from external investors (Amira and Chin-Bun, 2016).

Apart from the interest relationship between management and shareholders, the board is also committed to maintaining the integrity of its relationship with a wider range of stakeholders, including supply chains and customer base. The annual report of BP (2019) indicates that the board evaluates and influences the corporate culture through adequate communication, while the unique corporate culture attracts more stakeholders' participation by shaping corporate governance frameworks such as corporate leadership and working methods.

2. The relationship between the board of directors and the organizational structure

The board of directors promotes good corporate governance through its independence and main supervisory functions. Good corporate governance depends on the separation of the roles of chairman of the board and chief executive officer. It is indicated that the fact that more than 99.3% of the listed companies in FTSE 150 have role separation is also a good proof of this (Filipe et al, 2020). The separation of roles enables the board of directors to better supervise and constrain the management. Imad

ISSN 2616-5902 Vol. 3, Issue 10: 44-46, DOI: 10.25236/AJBM.2021.031008

(2017) argues that ensuring compliance with best 3 practices is one of the actions to promote corporate governance, which encourages the board to provide a majority of board seats to nonexecutive directors.

The independence of non-executive directors and their concern for their reputation in the external labour market also enable them to monitor the behaviour of executive directors and ensure that they pursue the best interests of shareholders (Hwa-Hsien & Chloe, 2014), thus better performing their supervisory functions. As a part of the whole board of directors, the committee of the company's board of directors, which comprises primarily non-executive directors as part of the overall board, also contributes to the strong governance arrangement of the company. Among them, the independence of the remuneration committee promotes the better connection between executive compensation and performance, while the recommendations of the audit committee improve the quality of audit and financial reports, thus improving the effectiveness of corporate governance. In addition, Amama and Grzegorz (2014) provide evidence that the stronger monitoring capability of the board of directors can promote the improvement of the company's operating performance, and the stronger governance standards of the board of directors can bring higher non-adjusted shareholder 'return.

3. The significance of the Board of Directors to the Company

The board of directors is committed to improve corporate governance through external contact and cooperative leadership to cope with corporate crisis. The market for corporate control is an external governance mechanism (Charlie et al, 2002), among which acquisition is considered as the most effective control mechanism. Filipe’s survey results (2020) show that when large listed companies encounter such problems, leadership is usually assumed by the board of directors in collaboration with the CEO, and the board of directors strives to improve the reputation and corporate governance of the company by seeking the 4 trust and cooperation of shareholders and powerful external stakeholders such as the central bank, the government and regulatory agencies. A typical example is Kraft Heinz's failed acquisition of Unilever.

At that time, the British trade union and even the British Prime Minister paid attention to the matter. The involvement of the British authorities made the acquisition more difficult. Ultimately, the failed acquisition had an impact on Unilever's future development. Unilever conducted an 18month internal review to set clear directions for the firm to change its structure, processes and culture, including the board's decision to adopt Unilever's unification to increase the strategic flexibility of the investment portfolio, and its decision to unify the firm's legal structure to further improve governance to adapt to the complex and changing business environment (Unilever, 2020), showing the strong leadership of the board in corporate governance. Besides, the research results of Amira and Chin-Bun (2016) show that during the financial crisis in 2008, large listed companies in the UK were more likely to comply with the Code, and there was a significant relationship between good corporate governance and investment by shareholders. And the compliance with the Code has enhanced the supervisory ability of the boards of (Amira & Chin-Bun, 2016), which has a vital influence on corporate governance alongside with the leadership.

4. Conclusion

By analysing the relationship between the board of directors, shareholders and management, and the independence and supervision functions of the board of directors, this paper finds that the communication and coordination of the board of directors, the separation of the roles of chairman and chief executive officer, and the independence and supervision functions of the board of directors and the board 5 committees are all important activities that the board of directors has a positive impact on the establishment of corporate governance framework and corporate governance in large listed companies in the UK.

After that, through the analysis of the wicked problems such as external governance of the acquisition company, this paper draws a conclusion that the board of directors plays an important role in corporate governance by coping with the crisis through external contacts and collaborative leadership. Therefore, the board of directors plays an extremely important role in corporate governance. Good corporate governance will contribute to better information disclosure, financial reporting, an advanced business environment and a highly transparent set of rules and regulations. This not only benefits the company internally, but also reflects the company's stronger competitiveness and greater confidence in the market, and ultimately drives the increase in investment.

ISSN 2616-5902 Vol. 3, Issue 10: 44-46, DOI: 10.25236/AJBM.2021.031008

References

[1] Charlie, W., David, L. & Philip, J. (2002) Internal and External governance mechanisms: Their impact on the performance of large UK companies. Journal of business finance & accounting, 29 (5-6), p.579.

[2] Adams, R., Hermalin, B., & Weisbach, M. (2010) The Role of Boards of Directors in Corporate Governance: A Conceptual Framework and Survey. Journal of economic literature, 48 (1), p.58-107.

[3] Filipe, M., Andrew, K., Nada, K. (2020) Leading through discontinuous change: A typology of problems and leadership approaches in UK boards. Long range planning, 53 (2), p.101870

[4] Terry, M. & Abigail, S. (2015) Developing the Governance Space: A Study of the Role and Potential of the Company Secretary in and around the Board of Directors. Organization studies, 36 (4), p.513535.

[5] Amira, H. & Chin-Bun, T. (2016) How Corporate Governance Affects Investment Decisions of Major Shareholders in UK Listed Companies: Has the Recent Credit Crunch Changed the Game? Journal of accounting, auditing & finance, 31 (1), p.100-133.

[6] Hwa-Hsien, H. & Chloe Yu-Hsuan, W. (2014) Board composition, grey directors and corporate failure in the UK. The British accounting review, 46 (3), p.215-227.

[7] Nicholas, J. (2018) The Role of the Board of Directors in Corporate Governance. Available at: https://insights.diligent.com/corporategovernance/the-role-of-the-board-of-directors-in-corporategovernance/ [Accessed 1 February 2021].

[8] Nicholas, J. (2018) The Role of the Board of Directors in Corporate Governance. Available at: https://insights.diligent.com/corporategovernance/the-role-of-the-board-of-directors-in-corporategovernance/ [Accessed 1 February 2021].

[9] Imad, K. (2017) Role of Board of Directors in Corporate Governance. Available at: https:// www.academia.edu/35297049/Role_of_Board_of_Directors_in_Corporate_Governance [Accessed 31 January 2021].

[10] Unilever (2020) Unification of Unilever's legal structure. Available at: https://www.unilever.com/ news/press-releases/2020/unification-of-unilever-legal-structure.html [Accessed 2 February 2021].

[11] Financial Reporting Council (2014) The UK Corporate Governance Code. Available at: https:// www.frc.org.uk/OurWork/Publications/CorporateGovernance/UK-Corporate-Governance-Code-2014. pdf. [Accessed 30 January 2021].

[12] British Petroleum Company (2019) BP Annual Report and Form 20-F 2019. [pdf] London: British Petroleum Company. Available at: https://www.bp.com/content/dam/bp/businesssites/en/global/ corporate/pdfs/investors/bp-annual-report-andform-20f-2019.pdf [Accessed 30 January 2021]