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A Study of the Role of the Board of Directors in Corporate Governance Based on UK Listed Companies

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Abstract: Companies are directed and controlled by corporate governance. It acts on the company internally and externally. The board of directors is responsible for the governance of the company; that is to say, the board of directors is the brain of the company, while corporate governance is the blood distributed throughout the company, which not only supplies blood to the whole, but also reflects the situation. Therefore, with regard to the role of the board of directors in corporate governance, this paper objectively analyzes the importance of the board of directors in corporate governance from theory to practice and from the internal composition of the board of directors to the impact of the board's actions on the enterprise as a whole based on United Kingdom (UK) listed companies.

Keywords: UK listed company; Corporate governance; Board of directors

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1. Introduction

Any listed company will have a board of directors. Some companies that have limited shares require standardized corporate governance during the brokerage counseling period before listing. During this period, the board of directors would have had existed. Ever since Berle and Means pointed out that the core feature of modern companies is the separation in rights of ownership and control, the role of the board of directors in corporate governance has become increasingly prominent [1]. As long as the board of directors has the ability to mitigate risk or boost innovation, the board can make business decisions and guide the development of the company [2]. Without governance constraints, managers are more likely to deviate from the interests of shareholders. Therefore, it can be said that the board of directors is an important factor in the governance structure of large companies in connecting the preceding and the following. The board should not only be responsible for the shareholders' meeting and protecting the interests of stakeholders, but also provide decision-making support for the operation of the management team. How the board of directors affects corporate governance is a practical issue that is worth discussing. The composition of the board of directors lays the foundation for corporate governance, the members of the board guide corporate governance, and the effectiveness of corporate governance is reflected by the development dynamics of the enterprise, which means that the board of directors is the beginning of corporate governance, and the two interact with each other to identify, realize, and manage the enterprise.

In this paper, it is important to first understand how the board of directors is structured. Exploring how the board of directors is structured would enable us to understand the allocation of corporate governance content. Each member of the board has a value to realize in the process of corporate governance. Therefore, it is important to discuss the impact of board composition on corporate governance. Secondly, it is important to consider how corporate governance is measured. The management's consideration of shareholder rights is a direct reflection of the level of governance in each company. Shareholder equity is seen at the level of shareholder wealth, where shareholders are concerned with how much profit the company makes and how that profit is distributed. In addition to this, the level of corporate governance is reflected in the share price. These measures of the level of corporate governance are determined by the behaviors of the board of directors. Therefore, the impact of the behaviors of the board of directors on corporate governance is also discussed. Last but not least, the role and importance of the board of directors in corporate governance is outlined based on theoretical and real-life examples of corporate governance in UK listed companies.

2. Impact of board composition on corporate governance

One of the roles of the board of directors in corporate governance is to balance the company structure and set up the Committee of the board of directors to form the adhesive for a good company structure. The board of directors includes the Chairman, Chief Executive Officer (CEO), an audit committee, a nomination committee, a remuneration committee, and other board committees [3]. The board needs to handle the relationship with the management in a proper manner. Holding a combination of interests and judiciously authorizing work can increase the flexibility in corporate governance.

The Institute of Directors (IoD) Good Governance Index (GGI) reduces information asymmetry to display the intuitive standard of corporate governance and compare the largest United Kingdom (UK) listed companies. The score consists of five evaluation indicators, one of which is the board effectiveness. In 2017, Diageo PLC gained an average unweighted score of 841, ranking the first worldwide. Based on the 47 data sources collected, the percentage of board meeting attendance was relatively high, corporate governance frameworks were established by the boards, and a clear separation of the roles of the Chairman and the Senior Independent Director was observed.

The UK Corporate Governance Code was released by the Financial Reporting Council. It points out the areas of corporate governance that should receive more attention in the future, including salary distribution, diversity of the board of directors, as well as efficiency and composition of the board of directors. In 2017, women in board positions made up 27% of the Financial Times Stock Exchange (FTSE) 100, a raise from 13% in 2010. The FTSE 100 company ranking proves the importance of gender diversity on the board of directors in corporate governance. ITE Group (listed on the London Stock Exchange [LSE]) transparently matches compensation to performance. The board of directors of ITE Group achieved board transformation and strategic growth through compensation-performance reform. In 2018, De La Rue won the "Corporate Governance Award" from World Finance Magazine, owing to the effectiveness of its board. Good cooperation and mutual support had played a significant role. At the same time, the board had the ability to adapt to the company environment in terms of supervision and governance.

3. Impact of board behavior on corporate governance

Another role of the board of directors in corporate governance is to serve the overall interests of the company as an important decision-making body. The board of directors sets goals and carries out strategies. Through analyzing and approving plans, investigating the use of large capital contingencies, and building strong connections in support of the company's strategy, the value and importance of the board of directors are evident [4].

The board of directors is usually composed of people with experience, resources, and foresight by reasonable planning. Having professional abilities and sound judgement in making decisions would be very helpful in guiding the company. According to the International Register of Certificated Auditors (IRCA), British American Tobacco PLC (BAT) ranked the first in terms of governance. In its annual report for board performance summary (2016), Chairman Richard Burrows regarded 2016 as a vintage year, driven by a successful strategy. Compared with 2015, the cigarette volume, the share of key market, and other indicators have made progress to varying degrees. Among them, total shareholder return (TSR) was 16.1%, which demonstrated good corporate performance as a Fortune 500 company in 2018. The board includes the Chairman, two Executive Directors, one Senior Independent Director, and seven Non-Executive Directors in the main board and management board. The members of the main board come from seven countries with varied expertise aligned to the needs and provide the leadership. The management board comprises senior leaders with about 300 years of industry experience in total that creates wealth for BAT. BAT also has corporate responsibility and contributed good social benefits to the tobacco industry. The board meets at least six times a year to ensure effective communication. Such a reasonable composition and meeting frequency reduce the possibility of unreasonable decision-making. All members of the board of directors balance each other and serve the overall interests of the company from different directions and angles.

However, regardless of the healthy development of the industry and the finance environment, if the board of directors does not have a correct strategic goal and constantly touches the bottom line to serve itself, it is considered to be poor governance, which may even lead to the bankruptcy and demise of the company. Thomas Cook Group (TCG), the world's first and oldest travel agency, announced that it had submitted an application for compulsory liquidation to the British High Court in 2019. Its share price decreased by 98% from £151 in May 2018 to £3.2 in September 2019. This signifies that the tourism enterprise, which has survived for 178 years, declared bankruptcy. Company failures are often caused by many factors. The decline of tourism or political factor is one of the reasons of TCG failure, but the root cause is poor management. This can be traced back to the huge dividends of nearly £48 million paid to the top management of the board in the past decade [5]. The precarious profits were divided up, in the meantime, the board thought that the British government could allocate funds to save the company. This corporate governance led the company to liquidation. In addition to the profit distribution, the board of directors did not solve the issues related to its own core competitiveness and adaptability. The board failed to grasp the advantages of a century old enterprise, and the accumulated resources could not be effectively transformed to adapt to the industry situation. The board of directors is responsible for the formulation of strategy. This case, on the contrary, demonstrates that the board is intended to ensure the sustainability of the long-term value built.

4. Conclusion

In general, corporate governance and the board of directors are all serving the company; there is no containment relationship intended. Based on the case studies of large listed companies in the UK, this paper analyzes the important role of the board of directors in corporate governance. In terms of corporate governance, an objective composition of the board ensures strategic guidance and effective supervision for the company and management, respectively. The dynamic behaviors of the board of directors demonstrate a concrete realization of the company's strategic development. At the same time, the board of directors demonstrates its responsibility and loyalty to the company and shareholders. Since the establishment of LSE, many companies have experienced ups and downs. Both excellent and poor corporate governance cases have also witnessed the change of board of directors. Corporate governance and the board of directors are growing together. It can be said that corporate governance is inseparable from the role of the board of directors.

Disclosure statement

The author declares no conflict of interest.

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