The Cadbury Report 1992: Shared Vision and Beyond

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ABSTRACT

This paper explores the shift from the Cadbury Report (1992) norms and rules to the current UK Corporate Governance Code (2014) focusing upon the reasoning, the influences and the implications thereof. The Cadbury Report (1992) has provided us with the legacy of definition of the corporate governance as the "system by which companies are directed and controlled", voluntary adoption of the governance best practices and the "comply or explain" principle.

The adoption of good governance practices is especially significant for the relationship between managers and shareholders in achieving high standards of corporate behaviour. Issues relating to managerial accountability, transparency, and regulation have been complex and still require further evaluation. The publication of the Cadbury Report (1992) has proven to be an influential in the development of a number of corporate governance codes worldwide. The greatest achievement of the Cadbury Report (1992) is the voluntary adoption of the corporate governance recommendations and use of the comply or explain principle.

We believe that the flexibility provided by the adoption of the voluntary code of best practice is the strength of corporate governance in the UK, yet the constantly evolving UK corporate governance code may be an indication of a deeper problem. An important part of the corporate governance is the prioritisation of the shareholder value, and although this is still the case, the UK Corporate Governance Code 2014 has veered for behavioural change, and requiring further confirmation by directors on several matters such as risk management, internal control, and going concern suggesting greater accountability, with further changes to disclosure and confirmation by the directors. This reaffirms that the corporate governance is changing, and is expected to change in the future.
INTRODUCTION

Corporate governance in United Kingdom has changed since the Cadbury Report (1992) was first produced by the Committee on the Financial Aspects of Corporate Governance (Cadbury Committee), is changing, and is expected to change in the future, which is evident from the number of corporate governance codes at national levels and the need for greater accountability and corporate transparency. We begin with the Cadbury Report, which correctly has been universally received and that it might almost be considered a truism for corporate governance. Over the twenty-five years since this report, the growth of interest in corporate governance, worldwide, has been dramatic. We note three major themes that the Cadbury Report has significantly contributed to corporate governance practices: the definition of corporate governance, voluntary adoption of the code and the "comply or explain" approach. The advancement of the Cadbury Report was enhanced by the London Stock Exchange (LSE) requirement for all listed companies in the UK as a continuing obligation of listing to state whether they are complying with the code and to give reasons for non-compliance (Cheffins, 1997, 76-77). Currently the corporate governance code is non-statutory, which only applies to companies listed on the London Stock Exchange. This paper explores the shift from the Cadbury Report (1992) to the current UK Corporate Governance Code (2014) focusing upon the reasoning, the influences and the implications thereof.

In the early 1990s, the reputation of the London as a financial centre would have dramatically suffered because of the failures of some major companies due to heightened attention of the following: corporate fraud, director malfeasance and the extent of these problems were not revealed by the published accounting report (Cadbury, 2000). Hence, a private sector initiative made up of the Financial Reporting Council (FRC), the London Stock Exchange (LSE) and the accounting profession set up a committee to review the Financial Aspects of Corporate Governance. The aim was to establish a code of best practice, whilst avoiding an inflexible one size fits all approach. The Cadbury Report identifies three themes to strengthen the unitary board system of all listed companies and summarise their recommendations in a code of best practice: the structure and responsibilities of boards of directors; the role of auditors and recommendations to the accountancy profession; and the rights and responsibilities of shareholders.

Comparative study of different corporate governance regimes recognises that corporate governance systems typically evolve in the context of the legal, political and institutional infrastructure in each of the jurisdictions. These corporate governance systems can be broadly categorised into two types. First, the strong equity-outsider system often known as the market-based system (Yonekura, Gallhofer and Haslam, 2012, 316) characterising more developed markets such as the United States and the United Kingdom. Both countries are characterised as conventional Liberal Market Economies (LMEs) within the comparative capitalisms literature (for example, Hall and Soskice, 2001). An important part of the corporate governance is the prioritisation of the shareholder value and strong protection of shareholder rights in both the UK and US economies, despite the major differences between

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corporate governance in the two countries (Siepel and Nightingale, 2014), which are often overlooked. As such, corporate governance in these two countries is based essentially on agency theory (see Jensen and Meckling, 1976; Eisenhardt, 1989; Fama and Jensen, 1983), in contrast to a wider stakeholder perspective, (Turnbull, 1997, 190), associated with corporate governance in Coordinated Market Economies (CMEs), (Hall and Soskice, 2001) as in Germany.

The second characterisation of corporate governance systems is the weak equity-outsider system (also known as bank-based system or insider) observed in East Asian countries, France, Germany and Italy. There are important differences in corporate governance systems across the two groups of countries, which relate to ownership and control. The contrasting corporate governance ownership and control systems are often known as either insider or outsider systems (Franks and Mayer, 1997; Mayer, 1997; Nestor and Thompson, 2001; Short and Keasey, 1999). For the outsider system of corporate governance (observed in the US and UK) the critical conflict of interest is between strong managers and widely dispersed weak shareholders. On the other hand, for the insider systems (Germany and Japan), where ownership and control are relatively closely held by identifiable and cohesive insiders (Nestor and Thompson, 2001) and the critical conflict is between controlling shareholders (or blockholders) and weak minority shareholders (Maher and Andersson, 2000; Yonekura et al., 2012). Likewise, categorisation as the strong and weak equity outsider systems, are not only used for corporate governance analysis, but have been used in other disciplines such as accounting, for example, that used by Nobes (1998, 180-181) for classifying the reasons for international differences in financial reporting.

Durisin and Puzone (2009, 281) analysis of corporate governance articles show that Jensen and Meckling (1976) and Fama and Jensen (1983) are the most widely cited papers in corporate governance research. Both papers are main contributors to the understanding of agency theory problem, where ownership and control are often separated in corporations. Although these papers considered the key issues around the governance of corporations, however they did not overtly refer to the term corporate governance. We know of very few academic literatures that have studied post Cadbury 1992 in the UK, for example, Haxhi and Aguilera (2014); Jones and Pollitt (2004); Mallin, Mullineux and Wihlborg (2005); Nordberg and McNulty (2013).

In this paper, we review articles that have reproduced the Cadbury definition in accounting, finance, management and business journals. We briefly analyse how the definition has endured since its first publication to the current UK Corporate Governance Code 2014. We first, consider the journal, Corporate Governance: an International Review (CGIR) and other journals ranked by ABS 2015.

The structure of the paper is as follows: an overview of Cadbury definition, the development of the corporate governance within the UK context and an appreciation of the voluntary adoption of the code and comply or explain principle discourse revealing issues and controversies surrounding the UK corporate governance system; discuss the changes to the UK Corporate Governance Code 2014 and finally concluding comments.
CADBURY DEFINITION OF CORPORATE GOVERNANCE

Many academic articles do not define corporate governance. It may be that these authors believe corporate governance to be a well-defined concept understood by potential readers. First, a commonly cited definition of Corporate Governance is that provided by the Cadbury Committee, the “system by which companies are directed and controlled,”2 (Cadbury Report 1992, Introduction s2.5) (hereafter Cadbury definition) is a central company level definition of several codes of corporate governance. Originally, put forward by the Committee of the Financial Aspects of Corporate Governance in the UK, (the London Stock Exchange, the Financial Reporting Council and the accountancy profession). The paragraph 2.5 is still the classic definition of the context of the Code within UK’s subsequent corporate governance codes consisting of the Combined Codes (1998, 2003, 2006) and the UK Corporate Governance Codes (2010, 2012, 2014).

The Organisation for Economic Cooperation and Development (2004) takes a wider position in describing corporate governance:

Procedures and processes according to which an organisation is directed and controlled. The corporate governance structure specifies the distribution of rights and responsibilities among the different participants in the organisation such as the board, managers, shareholders and other stakeholders and lays down the rules and procedures for decision-making.3

The Cadbury definition is used to describe corporate governance by various academic authors (for a list see Table 1), international institutions (for example, European Central Bank)4, within the corporate governance codes of countries (for examples, Armenia, Lebanon, South Africa)5 and the EU corporate governance framework6. However, on searching for the term “directed and controlled” in different country codes, we find that the Cadbury definition is often subsumed within the Organisation for Economic Cooperation and Development (OECD) definition. An alternative term “managed and controlled” is also used, for example Luxembourg7. Several authors use the Cadbury definition, but without referring to the original source and often using only the term “directed and controlled” (Fuenzalida, Mongrut, Arteaga and Erausquin, 2013; Haxhi, van Ees and Sorge, 2013; Larkin, Bernardi and Bosco, 2013; Millet-Reyes and Zhao, 2010; Okaro, Okafor, Ogbodo and Nkamnebe, 2010). Directed and controlled has been used by Hume (1970) in terms of describing a financial system that was “directed and controlled” by a central finance ministry. The original work was directed towards the significance of Jeremy Bentham’s writings on bookkeeping and accounting.

2 Directed and controlled has been used by Hume (1970) in terms of describing a financial system that was directed and controlled by a central finance ministry. The original work was directed towards the significance of Jeremy Bentham’s writings on bookkeeping and accounting.


corporate governance structures and processes of governance characteristics. The internal governance have a dual purpose of getting a return on their investment. Just like the Cadbury definition, this is considered to have a dual purpose. The articles distinguish across two paradigms, internal and external governance characteristics. The internal governance characteristics discuss different corporate governance structures and processes that can be controlled by the board and

The papers identified in Table 1, from the journal CGIR, shows that corporate governance is not characterised by a single unifying theory but there exists a wide range of theoretical perspectives covering from agency theory, institutional theory, stakeholder theory, shareholder value, management hegemony, path dependency and resource dependency. This reflects a wide perspective that academic researchers take in formulating the research questions, and the context in which corporate governance is set and the different disciplines in which corporate governance is viewed. The Cadbury definition is not confined to profit making companies, but also non profit making organisation such as the NHS in the UK (see Deffenbaugh, 1996; Prowle and Harradine, 2014). Within the finance literature the commonly cited definition is that by Shleifer and Vishny (1997, 737) who describe corporate governance as "ways to which suppliers of finance to corporations assure themselves of getting a return on their investment." Just like the Cadbury definition, this is considered to have a dual purpose. The articles distinguish across two paradigms, internal and external governance characteristics. The internal governance characteristics discuss different corporate governance structures and processes that can be controlled by the board and

A search on the Google scholar for the Cadbury definition gave 1,720 results and for the term directed and controlled gave 12,000 results. Hence, the search was narrowed down to include the following journals: Corporate Governance: International Review (CGIR) A search using the phrase Cadbury Report 1992, in the journal CGIR showed 122 articles from 1998 to April 2016. We then narrowed the search for the phrase directed and controlled as this would allow for any articles that paraphrased the definition. For the period, 1993 (when the first issue of the journal was published) to April 2016, using the search engine for directed and controlled gave 24 full-text articles in CGIR. Of these, two were book reviews and one Corporate Governance Report: Modern Company Law, which are not cited in Table 1. A similar search was conducted using the Business Source Premier articles of which 14 were from CGIR. We use articles from journals that are ranked by the Association of Business Schools Academic Journal Guide 2015 (ABS 2015) and ignore those that are not ranked.

Overall, the Cadbury Report has had significant influence in the development of the international codes on corporate governance, such as OECD and other countries, for example, Malaysia, Sweden.

Pro Cadbury definition authors such as Lannoo (1999, 271); Mallin et al. (2005, 532) suggest that the Cadbury definition has a duality role as it considers both internal and external perspectives of corporate governance. Internally it recognises internal controls and board structure and externally with the shareholder relationship. This was undoubtedly important in the context of privately owned companies in which the agents (managers) and principals (shareholders) were usually the same persons. Hence, one anticipates no conflict between the persons managing or controlling the company and the ultimate beneficiaries, unlike the companies where there is separation of ownership and control.

shareholders, whereas the external characteristics relate to rules and norms of the market for corporate control, legal system, accounting standards and the stock exchange. However, it is recognised that in reality corporate governance is far more complex and will be blended between the two paradigms. Often the corporate governance purpose is descriptive as to whether corporate governance is a system or structure or processes or has a normative function as ideal corporate governance recommendations that should be adopted.

It is difficult to find a unitary approach to corporate governance research and should be viewed as a loose collection of different research questions and issues within different national contexts. Although the papers exhibit substantial geographical spread, academic writers focus more on the LME countries such as UK and the CME countries such as Germany. Most papers address corporate governance post Cadbury Report, except, for example, Holm and Laursen (2007, 323) is one of the few papers that mentions corporate governance pre-Cadbury 1992.

"Internal controls" has been central in the debate on regulating financial reporting and corporate governance since the Cohen report on the auditors responsibilities (1978) and especially the Treadway report on fraudulent reporting (1987).

The use of the Cadbury definition to describe corporate governance, should be associated more to the UK, yet the papers have exhibited a greater dispersion addressing countries such as Australia (Turnbull 2007), Bahrain (Hussain and Mallin, 2002), Iceland (Jonsson, 2005), India (Jackling and Johl, 2009), Lebanon (Jamali, Safieddine and Rabbath, 2008), Nigeria (Akinkoye and Olasanmi, 2014; Okaro et al., 2015), Peru (Fuenzalida et al. 2013), Russia (Roberts, 2004), South Africa (Smith, 2015), South Korea (Solomon, Solomon and Chang-Young, 2002) and Turkey (Mugaloglu and Erdag, 2013) as well as the more traditional Anglo-Saxon countries. Majority of the research, however, is discussed for single countries and there has been some comparative international analysis but greater focus on the more advanced economies such as UK, US and Germany, for example, Mintz (2005); the UK and Netherlands (Hooghiemstra and Van Manen, 2004). Often the differences lie in the following areas: legal system, existence of a unitary board or two-tier board structure and ownership structures.

Sternberg (2000) refutes the definition provided by the Cadbury report for reasons of its simplicity and corporate governance is more than just control and offer her own definition. Many other academic authors also provide their own definition, these definition play a substantial role in shaping corporate governance. One could categorise them broadly into either shareholder orientation or extending the governance boundary to include a stakeholder orientation. Indeed, in recognition of the various corporate governance definitions raises the question how nuanced are the definitions that the authors try to provide. For example, whether the legitimate stakeholder groups are a homogenous group, all with the same interests, or are they seen as heterogeneous. The examples for the latter would include majority versus minority shareholders, block versus dispersed shareholders, executive versus non-executive director and salaried managers versus managers with equity stakes. capturing a nuanced approach ranging from broadly divided.

**Similarities with Cadbury definition**

Although some authors do not cite the exact Cadbury definition, but we find similarities in the use of the term "direct and control" as shown below:
Corporate governance of a firm operating at the BOP [bottom of the economic pyramid] can be viewed as "the system, or the set of mechanisms that internally direct and control the firm in the prevalent social and economic context (Chakrabarty and Bass, 2014).

The role of the board is instrumental in good corporate governance. The task is characterised by the pressure of responsibility, limited time and distance from operations of the company which the board is set to direct and control (Sponbergs, 2007).

Table 2 shows various journals, ranked by ABS 2015, in areas of accounting, economics, finance, law, management, public sector, corporate social responsibilities that cover various corporate governance themes. This also suggests the range of disciplines in the area of corporate governance.
<table>
<thead>
<tr>
<th>Authors using, &quot;directed and controlled&quot; to describe Corporate Governance</th>
<th>Geographical Location</th>
<th>Theory/ Subject of Analysis</th>
<th>Evidence</th>
<th>Summary of Findings/Conclusions</th>
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<tbody>
<tr>
<td>Short, Keasey, Hull and Wright (1998)</td>
<td>UK</td>
<td>Insider and outsider systems, Governance mechanisms</td>
<td>Secondary literature</td>
<td>Reviews the relationship between corporate governance mechanisms such as the market for corporate control and concludes that the policy debate and research has been directed towards accountability.</td>
</tr>
<tr>
<td>Mallin (1999)</td>
<td>UK</td>
<td>Analysis of financial institutions corporate governance activities using interviews and analysis of corporate governance policies</td>
<td>Contemporary documentation, secondary literature</td>
<td>Concludes that increasing influence of UK institutional investors in corporate governance, for example, 1:1 dialogue, increasing shareholder focus; continuing pressure to vote.</td>
</tr>
<tr>
<td>Solomon and Solomon (1999)</td>
<td>UK</td>
<td>Agency Theory, Shareholder Activism</td>
<td>Postal questionnaire of 198 unit trust managers</td>
<td>Empirical evidence suggests that institutional investors are supportive of the UK CG reforms. They are embracing higher activism, developing voting policies; encouraging relationship investing and more supportive of the long termism in the financial market.</td>
</tr>
<tr>
<td>Cadbury (2000)</td>
<td>UK, Australia, Canada, US, Netherlands, Japan, Belgian</td>
<td></td>
<td>Contemporary documentation</td>
<td>Concludes that institutions investors focus is now increasing more than boards.</td>
</tr>
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<td>Ow-Yong and Kooi Guan (2000)</td>
<td>Malaysia and the UK</td>
<td>Malaysian Code and contrast them with UK Corporate Governance Codes (Cadbury, Greenbury, Hampel and Combined). Examine the related parts of the results published from the Kuala Lumpur Stock Exchange and the PriceWaterhouseCoopers.</td>
<td>Contemporary documentation, secondary literature</td>
<td>Compares the UK and the Malaysian corporate governance. Concludes requirement of sound CG principles, different patterns of ownership structure between the two countries and historical factors and cultural characteristics influence board behaviour.</td>
</tr>
<tr>
<td>Mallin (2001)</td>
<td>UK, US, Australia, and Germany</td>
<td>Fiduciary duty</td>
<td>Contemporary documentation, secondary literature</td>
<td>Examines voting system across different countries. Concludes that institutional investors should take on the responsibility to exercise their votes and the concept of voting as a fiduciary duty is varied across different countries.</td>
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<tr>
<td>Hussain and Mallin (2002)</td>
<td>Bahrain</td>
<td>n/a</td>
<td>Survey questionnaire to 38 Bahrain Stock Exchange companies with 21 companies responding.</td>
<td>Analyse responses to determine the CG structures of Bahrainian companies.</td>
</tr>
<tr>
<td>Solomon et al. (2002)</td>
<td>South Korea</td>
<td>Conceptual framework methodology</td>
<td>Contemporary documentation, secondary literature</td>
<td>Outline the traditional system of corporate governance and review reforms taking place to build a conceptual framework.</td>
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<tr>
<td>Jonsson (2005)</td>
<td>Iceland</td>
<td>Concentrated ownership</td>
<td>Directors of 9 listed companies and 2 non listed companies; using questionnaire and follow up interview.</td>
<td>Builds a framework for the leading roles of the board.</td>
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<tr>
<td>Long, Dulewicz and Gay (2005)</td>
<td>UK</td>
<td>Institutional, agency and management hegemony</td>
<td>74 listed companies and 86 unlisted companies</td>
<td>For listed companies non executive directors are more concerned with protecting long term interests of shareholders compared to that of executive interests; whereas for the unlisted boards the non executive directors are more involved with strategic and financial operations.</td>
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<tr>
<td>Mallin et al. (2005)</td>
<td>UK</td>
<td>CG reports</td>
<td>Reviews post Cadbury 1992 development in UK corporate governance; focuses on institutional investors and the financial sector</td>
<td></td>
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<tr>
<td>Mintz (2005)</td>
<td>Germany, UK, US</td>
<td>Various including shareholder model; stakeholder model</td>
<td>Literature review and corporate governance reports</td>
<td>Examines factors underpinning the development of corporate governance systems. Sceptical with regard to achieving convergence in corporate governance systems given the underlying differences in financing and culture within the different countries.</td>
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<tr>
<td>Nestor (2005)</td>
<td>European telecom industry</td>
<td>Privatisation</td>
<td>Contemporary documentation, secondary literature</td>
<td>Discusses four central objectives of privatisation from a company’s view: depoliticisation, commercial incentives, financial flexibility and valuation. In addition, it examines elements of corporate governance, adapting the</td>
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<tr>
<td>Edwards and Wolfe (2007)</td>
<td>UK</td>
<td>Ethical approach; compliance - competence</td>
<td>Skandia, a UK life assurance Company.</td>
<td>Uses a template analysis to assess the ethical compliance - competence as a communication tool for both managers and external stakeholders.</td>
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<tr>
<td>Holm and Laursen (2007)</td>
<td>Europe</td>
<td>Understanding internal control and risk management</td>
<td>Corporate governance reports and auditing reports.</td>
<td>Examines the role of the external auditor. They analyse changing perceptions of the audit process and regulatory demands for transparency.</td>
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<tr>
<td>Jamali et al. (2008)</td>
<td>Lebanon</td>
<td>CG; Corporate Social Responsibility (CSR); Path dependence</td>
<td>In-depth interviews with top managers of eight corporations.</td>
<td>Suggestion of increasing convergence between CG and CSR. Strong CG frameworks acts as a driver for long term sustainable CSR.</td>
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<tr>
<td>Talaulicar and v. Werder (2008)</td>
<td>Germany</td>
<td>Code Compliance</td>
<td>Kodex Report 2006 and 671 companies listed on the Frankfurt Stock Exchange.</td>
<td>Look at classification of compliance patterns among German listed firms, which declare conformity with the German Corporate Governance Code. Use seven measures of code compliance and eight groups of companies based on</td>
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9 Uses the term “directed and controlled” as a key feature of network governance.
<table>
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<th>Authors using, “directed and controlled” to describe Corporate Governance</th>
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<tr>
<td>Jackling and Johl (2009)</td>
<td>India</td>
<td>Agency theory; Resource dependency</td>
<td>180 observations from a sample of top listed Indian companies.</td>
<td>distinct code conformity. They find that different companies share common patterns of code observations. This allows for identifying distinct groups of companies.</td>
</tr>
<tr>
<td>Mande, Park and Son (2012)</td>
<td>US</td>
<td>Agency Theory</td>
<td>2,049 observations consisting of 288 observations with equity issuances and 1,761 observations with debt issuances.</td>
<td>Examines the role of CG on a company’s choice of financing policy. They find that with stronger CG, companies prefer equity finance over debt finance. This is more pronounced in smaller companies.</td>
</tr>
<tr>
<td>Haxhi et al. (2013)</td>
<td>UK</td>
<td>Comply or Explain</td>
<td>Development of UK corporate governance codes.</td>
<td>Links institutional actors and business elites in the development of the UK corporate governance(CG) codes</td>
</tr>
</tbody>
</table>
Table 2 “ABS ranked journals using the Cadbury definition ‘system by which companies are directed and controlled’”

<table>
<thead>
<tr>
<th>Journal if on the ABS 2015 ranking</th>
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<tr>
<td>International Review of Law and Economics</td>
<td>Diacon and O'Sullivan (1995)</td>
<td>UK</td>
<td>Governance characteristics</td>
<td>Postal questionnaires of 129 U.K. life and general insurance companies</td>
<td>Identified 18 governance measures and uses factor analysis to reduce these to five. Evidence suggests that some governance instruments are more effective in influencing company performance.</td>
</tr>
<tr>
<td>Journal of Common Market Studies</td>
<td>Lannoo (1999)</td>
<td>European Stock Markets</td>
<td>CG Convergence</td>
<td>Data on European Stock Markets</td>
<td>Examine CG in Europe and conclude that the European countries still show variations in the functioning of CG mechanisms. They reason that these variations are due to different shareholding structures and social and economic behaviour. However, the national CG codes do show convergence in their recommendations such as self-regulation.</td>
</tr>
<tr>
<td>European Accounting Review</td>
<td>Olivier (2000)</td>
<td>Main focus on European Union</td>
<td>Reiterates the broadening of the role of the accounting profession from the traditional bookkeeping.</td>
<td>Secondary literature and institutional reports</td>
<td>Considers the influence of technology and regulatory framework framework and the needs of accounting profession to adapt.</td>
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<tr>
<td>Australian Journal of Public Administration</td>
<td>(Ryan and Ng, 2000)</td>
<td>Australia</td>
<td>Corporate governance analysis via: board, actors and</td>
<td>Annual reports; Contemporary</td>
<td>Explores the possibility of generic corporate governance framework across all public sector bodies.</td>
</tr>
<tr>
<td>Journal if on the ABS 2015 ranking</td>
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<td>International Journal of Auditing</td>
<td>Paape, Scheffe and Snoep (2003)</td>
<td>European Union</td>
<td>Survey questionnaire; 50 Largest companies in EU in 2001</td>
<td>Sketches the relationship between internal audit function and corporate governance seen as an important and an integral part of CG.</td>
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<tr>
<td>Accounting &amp; Business Research</td>
<td>Hooghiemstra and Van Manen (2004)</td>
<td>Netherlands</td>
<td>Qualitative research using survey questionnaire on the role of non executive directors.</td>
<td>Reports expectation gap for non executive directors in areas of non executives; shareholder influence and directors’ remuneration.</td>
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<tr>
<td>Europe-Asia Studies</td>
<td>Roberts (2004)</td>
<td>Russia</td>
<td>Corporate governance code in Russia</td>
<td>Questions the extension of Anglo-Saxon hegemony of shareholder capitalism to Russia with different cultural values and legal system.</td>
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<tr>
<td>California Management Review</td>
<td>Elkington, Emerson and Beloe (2006)</td>
<td>Sustainable development; Triple Bottom Line</td>
<td>Interviews and case studies</td>
<td>Suggest the use of a “value palette” to benefit both profit making and non profit making organisations.</td>
<td></td>
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<td>Journal if on the ABS 2015 ranking</td>
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<tr>
<td>Australian Accounting Review</td>
<td>Cortese (2009)</td>
<td>Australia</td>
<td>Non executive directors</td>
<td>50 largest Australian companies, reviews 438 board members;</td>
<td>Assess the extent to which companies adhere to the Australian Stock Exchange’s Principles of good corporate governance.</td>
</tr>
<tr>
<td>Managerial Auditing Journal</td>
<td>Porter (2009)</td>
<td>Australia</td>
<td>Audit function</td>
<td>Secondary literature and institutional reports</td>
<td>Corporate accountability is not confined to the financial reporting but includes the tripartite relationship among external auditors, internal auditors and the audit committee.</td>
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<tr>
<td>Corporate Governance: The international journal of business in society</td>
<td>Spitzeck (2009)</td>
<td>UK</td>
<td>Stakeholder perspective to corporate governance</td>
<td>Business in the Community (BITC) Corporate Responsibility Index</td>
<td>Corporate responsibility is now integrated with corporate governance and it is common to have a separate corporate responsibility committee.</td>
</tr>
<tr>
<td>Corporate Governance: The international journal of business in society</td>
<td>Apostolides (2010)</td>
<td>UK</td>
<td>Annual general meeting (AGM)</td>
<td>40 AGMs</td>
<td>Advocates three areas from his observations at AGM, which are corporate social responsibility, directors’ remuneration and board to characterised as well balanced and independent range of skills.</td>
</tr>
<tr>
<td>Journal of International Financial Management &amp; Accounting</td>
<td>Millet-Reyes and Zhao (2010)</td>
<td>France</td>
<td>Agency theory; one-tier and two-tier board types</td>
<td>174 French companies from 28 industries over the period 2000–2004; secondary literature</td>
<td>Provides empirical evidence that there is agency conflict among providers of finance</td>
</tr>
<tr>
<td>Corporate Governance: The international</td>
<td>Lenssen et al. (2010):</td>
<td>n/a</td>
<td>Stakeholder theory</td>
<td>Qualitative research on stakeholder</td>
<td>Find stakeholder participation varies from low to strong regarding</td>
</tr>
<tr>
<td>Journal if on the ABS 2015 ranking</td>
<td>Authors</td>
<td>Geographical Location</td>
<td>Theory/Subject of Analysis</td>
<td>Evidence</td>
<td>Summary of Findings/Conclusions</td>
</tr>
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<tr>
<td>journal of business in society</td>
<td>Bliss (2011)</td>
<td>Australia</td>
<td>Audit fee pricing</td>
<td>799 Australian publicly listed companies in 2003</td>
<td>Find evidence that higher proportion of independent directors without CEO duality is associated with higher audit fee pricing.</td>
</tr>
<tr>
<td>Accounting &amp; Finance</td>
<td>Brown, Beekes and Verhoeven (2011)</td>
<td>Global</td>
<td></td>
<td></td>
<td>Review of corporate governance</td>
</tr>
<tr>
<td>Auditing: A Journal of Practice and Theory</td>
<td>Bierstaker, Cohen, Todd DeZoort and Hermanson (2012)</td>
<td>US</td>
<td>Audit committee compensation</td>
<td>Experiment based using 56 audit committee member of publicly listed companies</td>
<td>Find audit committee supports auditor in an accounting disagreement under the following circumstances: audit committee compensation includes long-term stock options and when viewed that failure to change is seen as unfair to shareholders</td>
</tr>
<tr>
<td>Journal if on the ABS 2015 ranking</td>
<td>Authors</td>
<td>Geographical Location</td>
<td>Theory/ Subject of Analysis</td>
<td>Evidence</td>
<td>Summary of Findings/Conclusions</td>
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<td>Journal of Business Research</td>
<td>Fuenzalida et al. (2013),</td>
<td>Peru</td>
<td>Corporate Social Responsibility</td>
<td>8 companies on the Lima Stock Exchange</td>
<td>Find that investors positively value adoption of good corporate governance.</td>
</tr>
<tr>
<td>Accounting &amp; the Public Interest.</td>
<td>Larkin et al. (2013)</td>
<td>US</td>
<td>Proportion of women on Fortune 500 boards</td>
<td>Fortune 500 (2010); Corporate Responsibility Magazine’s (2011); Ethisphere Magazine’s (2011)</td>
<td>Find higher percentages of women on the boards of the companies if the Fortune 500 companies are listed on the Corporate Responsibility Magazine’s (2011); Ethisphere Magazine’s (2011)</td>
</tr>
<tr>
<td>Business History</td>
<td>Nordberg and McNulty (2013)</td>
<td>UK</td>
<td>Institutional theory</td>
<td>Current documentation; secondary literature</td>
<td>Finds that codes define and then redefine the terms. The redefinitions integrates the learning from the practice of directors. The evolution of the codes is strongly embedded in the communication and use of persuasive rhetoric. It allows for flexibility that change will recur.</td>
</tr>
<tr>
<td>Journal of Law and Society</td>
<td>Magnier (2014)</td>
<td>European Union</td>
<td>Stakeholder</td>
<td>Current documentation, secondary literature</td>
<td>Argues that the comply or explain principle adoption in the European Union will enhance the harmonisation process of the adoption of best practices in corporate governance.</td>
</tr>
<tr>
<td>Corporate Governance: The international journal of business in society</td>
<td>Mouselli and Hussainey (2014)</td>
<td>UK</td>
<td>Agency theory</td>
<td>1,514 UK firms listed in the London Stock Exchange</td>
<td>Finds a positive association between corporate governance and analyst following</td>
</tr>
<tr>
<td>Journal if on the ABS 2015 ranking</td>
<td>Authors</td>
<td>Geographical Location</td>
<td>Theory/ Subject of Analysis</td>
<td>Evidence</td>
<td>Summary of Findings/Conclusions</td>
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<td>International Journal of Public Sector Management Prowle and Harradine (2014)</td>
<td>UK</td>
<td>Questionnaire to all finance directors in NHSTs in England supported by semi-structured interviews</td>
<td>Focuses on financial aspects of corporate governance within the UK NHS.</td>
<td></td>
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<tr>
<td>Academy of Management Journal Tihanyi, Graffin and George (2015)(^{10})</td>
<td>Evolving practices in corporate governance practices Secondary literature</td>
<td>Provides an overview of corporate governance by management scholars</td>
<td></td>
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\(^{10}\) The same article had a different reference as follows: Tihanyi, Graffin and George (2014)
BACKGROUND TO THE CADBURY REPORT

The Cadbury Report 1992, first produced by the Committee on the Financial Aspects of Corporate Governance (Cadbury Committee), which was set up in May 1991 to address the concerns raised about financial reporting and accounting of the publicly listed companies in United Kingdom (see preface in Cadbury Report 1992). The report was first published in December 1992. It is without doubt, that the Cadbury Report 1992 has legitimately provided a framework for the corporate governance rhetoric underpinning the governance evolution. In their book Spira and Slinn (2013), state that the Cadbury committee’s primary aim was to restore confidence in the UK capital markets in light of the many ethical failures (see also (Dewing and Russell, 2004; Jones and Pollitt, 2004)). In addition, the Cadbury report was concerned with improving the way corporations are run and thus contribute positively to the promotion of good corporate governance (p.10). The UK Financial Reporting Council, the London Stock Exchange and the accounting profession were the main supporters of the Cadbury committee (Cadbury, 1992; Mees, 2015, 200). The Cadbury Report 1992 key objectives represent setting out measures to enhance corporate reliability based on improved information, continued self-regulation, more independent boards and greater auditor independence.

The Cadbury Report is the first in a series of important guidelines that would come to be published for the institutionalisation of the European Union members’ corporate governance and adopted as an outline of best practice in the EU (Keay, 2014).

The Cadbury Report may therefore be regarded as the cornerstone of the comply-or-explain framework in Europe, long before this system was introduced in European law (RiskMetrics Group, 2009)\(^\text{11}\).

With its popularisation, the Cadbury Report and its framework soon began appearing in more corporate governance narratives and the OECD 1999 Corporate Governance further established the wider use of this framework. Since the Cadbury Report, over 90 countries have instated national codes of corporate governance (see http://www.ecgi.org/codes/all codes). The two main goals of every code suggests convergence in areas of improving the quality of companies’ governance and raising the accountability of companies to shareholders while maximizing shareholder value (Aguilera and Jackson, 2010). However, Lazonick and O’Sullivan (2000) argue that there is significant limitation of the shareholder maximisation concept of corporate governance, and doubts whether this in fact develops the long-term sustainable performance of companies. Within corporate governance, a key debate that continues today is to regard managers whose primary duty is to shareholders rather than of wider responsibility to other stakeholders (Walker Review, 2009, 137)\(^\text{12}\). This debate goes back to the writings of Berle (1931) who interpreted that corporate powers are entrusted to shareholders and nobody else. However, Dodd (1932, 1162) differs from Berle (1931)’s suggestion and makes the following statement:

\(^{11}\) Study on monitoring and enforcement practices in corporate governance in the Member States conducted by RiskMetrics Group for the EU (23 September 2009) at 22, available at http://ec.europa.eu/internal_market/company/docs/ecgforum/studies/comply-or-explain-090923_en.pdf (accessed 1 April 2016)

Business - which is the economic organization of society - is private property only in the qualified sense, and society may properly demand that it be carried on in such a way as to safeguard the interests of those who deal with it either as employees or consumers even if the proprietary rights of its owners are thereby curtailed.

Berle (1932) takes a pragmatic view and infers that responsibility to multiple parties would exacerbate the separation of ownership and control issue and make management even less accountable to shareholders. The Walker Review, 2009, 137, mainly directed to the banks and other financial institutions (BOFI), is of the same view and states that:

To dilute the primacy of the duty of the BOFI director to shareholders to accommodate a new accountability to other stakeholders would risk changing fundamentally the contractual and legal basis on which the UK market economy operates. It would introduce potentially new uncertainty for shareholders.

Within the capitalism literature, corporate governance systems are converging and positioning towards the Anglo-Saxon model of corporate governance or the shareholder value (Hall and Soskice, 2001). This aligns, with agency theory, where corporations' role is to create wealth for their shareholders. The latter are also at higher risk than other stakeholders, further suggesting that corporate directors are singularly accountable to shareholders.

Aguilera and Jackson (2010, 381) suggest that the polarisation of the Anglo-Saxon model is observed in the development of corporate governance codes across different countries. Although we may see corporate governance changing, in the CME countries, with some elements of the Anglos Saxon model such as shareholder value and share based remuneration, nevertheless characteristics associated with, for example, German corporate governance are still in place Goergen, Manjon and Renneboog (2008).

Cadbury Report formed the framework for the development of international corporate governance provided by the international institutions, for example, OECD, the Commonwealth and California Public Employees' Retirement System (CalPERS) (Demirag and Solomon, 2003), International Corporate Governance Network (ICGN); and European Fund and Asset Management Association. In 1999, the OECD issued a document, The OECD Principles of Corporate Governance, that emphasises that corporations should be run, in the interests of shareholders (OECD 1999)13. Notably the change reflects from competitiveness and access to capital to high standards of corporate behaviour and accountability of the Cadbury Report. Interestingly, the OECD committee included representatives from leading countries with strong financial markets, such as France, Germany, Japan, the UK and the US. Sir Adrian Cadbury was one of the key member of this committee. The OECD Principles of Corporate Governance (1999) assists member and non-member countries in evaluating and enhancing their legal, institutional and regulatory framework for improved corporate governance. The OECD code followed the Anglo-American model of widely dispersed

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shareholders, agency problem, unitary board structure and only a small focus on the stakeholders.

The OECD report provides member countries a framework when considering statutory or voluntary adoption of corporate governance recommendations. The report advocates, that the corporate governance framework should ensure, for example, fairness, transparency, accountability and responsibility, and reduced regulatory intervention (Cadbury, 2000, 13).

In addition to the OECD Principles 1999, the literature on legal origins became accepted with the work of La Porta studies (La Porta, Lopez-de-Silanes, Shleifer and Vishny, 1997; 1998). This literature looked at two main legal traditions in developed countries, which comprised of the Anglo American common law tradition and the civil law or the Romano-Germanic legal tradition. The English common law system has a long tradition of self-regulation and is open to industry specific initiatives, which do not take legislative form. Both the US and UK are characterised as common law countries, yet the US legal system is different as it has both written law as well as "judicially crafted common law" (Jordan, 2013). Within the common law system, legislation has been usually seen as a last resort. However, in continental European legal systems, written legislation dominates, which may take various forms such as constitution, civil and commercial codes. According to Jordan (2013) the concept of a voluntary nature of code is countries with a civil law is seen as an oxymoron, since codes are seen as a form of formal written legal rule, which avoid conflicts. Perhaps in the modern financial markets categorically needs both forms of regulation i.e. self-regulation or rule based corporate governance mechanisms.

The Cadbury Report has contributed to the "strong governance culture" among the listed companies on the London Stock Exchange, thus assuring investors on the information they receive from the board being "fair, balanced and understandable" (FRC 2014) 14

**VOLUNTARY ADOPTION OF THE CODE**

**Soft law vs hard law**

The UK Corporate Governance Code 201415 reflects the Cadbury Report, by reiterating the Cadbury definition; however, this document is significantly different from the Cadbury Report (1992). The two pages "Code of Best Practice" is replaced by a detailed and differentiated approach to corporate governance structured along the lines of the OECD Principles 2004 (Jordan, 2013). The Cadbury Report (1992) and the UK's subsequent reports on corporate governance have kept within the soft law area. So far, we have seen little regulation and the FRC has adopted a precautionary position with continuous reviews and revisions of the corporate governance codes to address new developments and not requiring regulation of the UK corporate governance by use of hard law. Although there may be similarities to that of hard law, however the recommendation of the corporate governance codes and the use of soft law allows for greater flexibility compared to legislation. The regulation by hard law provides for a minimum standard that outlines the framework for

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company conduct, whereas soft law illustrates best practice. In addition, soft law is exemplified by a high degree of voluntarism, which provides the recommendations with the flexibility necessary for companies to adjust the principles on corporate governance in relation to the individual company’s circumstances. The advantage of flexibility provided by soft law is that no one size fits all solution for all companies when it comes to corporate governance. Thus, the recommendation is that companies optimally organise their governance within a loose framework. Since the Cadbury Report, the UK corporate governance code continues to uphold the voluntary nature of governance, thus relying on self-regulation. The soft law commitment in the UK highlights that shareholders will exercise their influence, in particular, we now have the additional requirement for institutional investors to publish their policy on shareholder engagement (Institutional Shareholders Committee Principles 2002)\(^\text{16}\). This reference was endorsed by reference in the Combined Code 2003, and endorses comply or explain approach since the introduction of the Institutional Shareholders Committee Principles 2002, which was then developed into the Stewardship Code 2010.

One would expect that the unexpected collapse of Enron in 2002 should have changed the way, we think about corporate governance. The Enron\(^\text{6}\) collapse caused a major impact on the financial markets as it was closely followed by the bankruptcy of other large companies in the US such as WorldCom. Carnegie and Napier (2010) suggest \(\text{Enronitis}\) a term derived from the scandals of Enron, is now a label used to describe blame, alluding to the alleged highly suspicious accounting, and auditing practices. Although these practices were strongly criticised, they undermined confidence in corporate reporting and auditing and the corporate regulation. According to Bratton (2001) the self-regulatory system of corporate governance is highly implicated in Enron\(^\text{6}\) failure. Thus requiring the legislators and the financial community to replace the current soft law regime to be substituted by a hard law regime with greater enforcement powers in order to enhance \(\text{transparency and accountability}\) (Cuomo, Mallin and Zattoni, 2015). Following the debacles of Enron\(^\text{6}\) collapse and Arthur Andersen\(^\text{6}\) role as the external auditors a large scale federal regulation of independent, public accountant was initiated, with the enactment of the Sarbanes Oxley Act 2002 \(^\text{17}\) (SOX) (Riotto, 2008; Romano, 2009). SOX followed the hard law regime, which required all listed companies on the US stock markets to adopt fully the provisions of the SOX. In contrast, rather than intervene in the governance of companies, the UK government commissioned the Higgs Report (2003) and the Smith Report (2003) to report on the non-executive directors and the audit committee, respectively. Both of these reports were addressed in the Combined Code 2003. This is different from the original Combined Code 1998 since it now places greater emphasis on the independent non-executive directors in a company’s governance structure and decision-making processes (Pass, 2006).

Post SOX, the empirical research shows a decline in the new foreign listings in the US. One of the reasons for the decrease in the US IPOs is the change in the geographical distribution of IPOs with London as the more attractive choice to cross list (Zingales, 2007). Doidge, Andrew Karolyi and Stulz (2009); Piotroski and Srinivasan (2008) find adverse effects of SOX on foreign listing and the relative attractiveness of the UK over the US stock exchanges due to the growth in the LSE\(^\text{6}\) Alternative Investment Market. However, the


adoption of the full corporate governance code may be burdensome for the smaller companies.

Since the Cadbury report 1992, several countries have issued corporate governance codes to which corporations can adhere voluntarily (Claessens and Yurtoglu, 2013). Several empirical studies show strong links in adoption of voluntary corporate governance mechanisms of companies to higher market valuation and reduced cost of capital (Black, Jang and Kim, 2006; Gompers, Ishii and Metrick, 2003; Joh, 2003).

Durnev and Kim (2005); Klapper and Love (2004) provide evidence that improved voluntary company governance practices matter more in countries with poor shareholder protection rights. However, their analysis is taken with caution since in countries with weak governance practices, voluntary adoption of corporate governance mechanisms may not fully have the desired effect.

COMPLY OR EXPLAIN

The UK’s principle based approach to corporate governance is underpinned by the comply or explain principle of accountability. This requires a listed company choosing to depart from a national corporate governance code to provide details of sections of the corporate governance code it has deviated from and the reasons for doing so. The Combined Code (Pass, 2006) and the UK corporate governance codes continues the Cadbury Report’s (1992) norms and rules of conforming to good governance practices without the backing of legal endorsements i.e. based on soft law approach (Haxhi et al., 2013), more specifically, using the comply or explain principle. This important aspect, the comply or explain approach of the Cadbury report has had a major impact on corporate governance codes, globally (Keay, 2014; Magnier, 2014). Underpinning this is that the UK corporate governance relies on self-regulation (Roach, 2011, 465), a voluntary code of best practice, and transparency. However, the failure to comply with the recommendations is not a violation of rules, or delisting from the stock exchange, but implies that the board of directors of the company have chosen an alternative approach, that is more sustainable over the longer term. Although the comply or explain principle is strongly associated with that of the Cadbury report (1992), however, this exact label was not written in the report. What the Cadbury report (1992 s1.3) suggests to ensure that investors are aware of any non-compliance with the code is:

The London Stock Exchange intend to require all listed companies registered in the United Kingdom, as a continuing obligation of listing, to state whether they are complying with the Code and to give reasons for any areas of non-compliance.

The comply-or-explain principle requires companies to explain their reasons for not adopting the recommendations of good corporate governance proposed in the governance code (Magnier, 2014). According to FRC in the UK Corporate Governance Code 201218 the responsibility lies with both companies and shareholders for ensuring that comply or explain principle remains a valuable option compared to a rules-based system. This approach has now gone global and been promoted by national/supranational organisations and adopted by European Union through the Directive 2006/46/EC (Nerantzidis, 2015; Seidl, Sanderson and


To the extent to which a company, in accordance with national law, departs from a corporate governance code it shall explain its reasons for doing so (Directive 2006/46/EC, s.7b).

A disadvantage of the corporate governance codes is that the adoption of the soft law may diminish governance structure overall as they do not belong to hard-law regulation. Magnier (2014) refutes the rhetoric that codes recommendations contain nothing because a rule that has a weak normative value, which is simply ‘recommendatory’, may have an extremely strong normative effect, in so far as it is seen as binding by those it targets. Nordberg and McNulty (2013) suggests that the Higgs Report (2003) reiterates the content of Cadbury’s provision, using different words but in a compelling statement that: ‘Companies should have a free hand to explain their governance policies’ suggests an availability of an alternative. the next statement suggests that compliance takes precedence: ‘It is expected that listed companies will comply with the Code’s provisions most of the time’. 

Sergakis (2013) argues that within the European context we see diversity in ownership structures. He advocates that within the national contexts with concentrated share ownership, the use of soft law measures may not be suitable in promoting good corporate governance structures. In contrast, in countries such as the UK with dispersed ownership, soft law measures may be appropriate, thus avoiding formal regulators to perform supervisory function.

Within UK the Cadbury report was followed by further reports to the current UK Corporate Governance Code 2014 and the UK Stewardship Code (2010, 2014).

**Board Committees**

The UK corporate governance since the Cadbury Report (1992) has place great emphasis on the continuation of the UK unitary board structure (Spira and Bender, 2004). This contrasts the German system where we see a two-tier system consisting of both a supervisory board and a management board. The board reform has been one of the major corporate governance issues. The Accountants International Study Group (AISG, 1977, p.1) indicated that audit committees were not very frequently observed in the UK, but the concept was not unknown. In the UK, The Cadbury Committee (1992, p.28) recommendation of all listed companies to establish an audit committee (Collier and Gregory, 1999) to date remains embedded in the voluntary codes of Cadbury and the current UK CG2014. Audit committees and non-executive directors were not new, the Cadbury Report itself was picking up the provisions from the New York Stock Exchange listing rules, however the difference is that in the US it is a mandatory requirement for all NYSE listed companies, unlike the comply or explain

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approach in the UK. Since, 2002 SOX the audit committee requirement\textsuperscript{20} is now statute an applicable to all publicly listed companies.

Hopt (2011) emphasises that the law reforms, which include codifications aim to minimise the inherent principal-agent conflict between the shareholders and the managers. Following the seminar work of Berle and Means (1932) on the ëseparation of ownership and controlî, where they argue that the dispersed share ownership within corporation meant that it was managers rather than the shareholders who controlled the companies. However, difficulty with the principal-agent relationship exists between various parties, for example, controlling shareholders and the minority shareholders, and, between the shareholder and other stakeholders, such as creditors and bondholders. Examples of codification include the UK companies Act 2006, Australian Corporation Act 2001 and the Switzerland plans of the ëgrosse Aktienrechtare formî.

**Shift to independent directors**

Within the UK unitary board model, executive directors influencing the board may seem to be problematic (Tricker, 1984). Cadbury Report suggested that the number of NEDs on the board should be increased to balance the influence of the executive directors. The current corporate governance achieves this by going beyond what the Cadbury Report (1992) recommended:

> An essential quality which non-executive directors should bring to the board deliberations is that of independence of judgement. We recommend that the majority of nonexecutives on a board should be independent of the company. This means that apart from their directors' fees and shareholdings they should be independent of management and free from any business or other relationship, which could materially interfere with the exercise of their independent judgement. It is up to the board to decide in particular cases whether this definition is met (Cadbury 1992, s.4.12)

This is in contrast to those countries that have a dual board structure, such as Germany and Sweden. The origins of this are from legal requirements and traditionally have boards composed of mainly NEDs.

**Shareholder activism**

Many concerned about UK corporate governance have urged equity owners in listed companies to quit the common favouritism of passivity and act as responsible, engaged owners. The financial crisis 2007-2009 has given added drive to such calls, with the notion of ëstewardshipî dominating and resulting in the launch of a Stewardship Code. The Stewardship code is a set of best principles focusing on the encouragement of the institutional investors to engage in stewardship of their investee companies and is enforced on a comply or explain basis (Roberts, 2015). The Stewardship Code originated from the code entitled ëResponsibilities of Institutional Investorsî issued in 2009 by the UK Institutional Shareholders' Committee (Heineman, 2010). The OECD in their report suggests that institutional investors have not been effective as corporate governance intermediaries, and hence the outcome of the adoption of the entire Stewardship Code, is unlikely to result in

corporate accountability. The European Commission’s Green Paper on Corporate Governance (2011) defines shareholder engagement as actively monitoring companies, engaging in a dialogue with its management and using shareholder rights, including voting and co-operation with other shareholders, to improve the governance of the investee companies in the interest of long-term value creation. This approach provides a broad spectrum of shareholder means, from selling and buying shares to expressing their views on a large number of issues from board composition to major transactions and takeover bids (Gillan and Starks, 2007).

By contrast, a UK government initiative, the Walker Report (July 2009)\(^\text{21}\) was published on the corporate governance in the UK banks. The Walker Report produced 39 recommendations, several of which concerned the chairman and non executive directors. At this time, the Combined Code on Corporate Governance was still in existence. However, the Walker Report (2009) recommended that the Combined Code should be separated into two: UK Corporate Governance and the “Principles of Stewardship”\(^\text{22}\).

**Table 3 Development of Corporate Governance Codes in the UK**

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\(^{22}\) See Recommendations 16 and 17, Walker Report (2009, 73)
<table>
<thead>
<tr>
<th>Year</th>
<th>Name of the Report</th>
<th>Issuer</th>
<th>Comment</th>
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<tbody>
<tr>
<td>1992</td>
<td>Cadbury Report</td>
<td>LSE, FRC, accountancy</td>
<td>First version of the UK Corporate Governance Code looked at Financial Aspects of Corporate Governance; for all listed companies, but recommended for small companies to adopt.</td>
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<td></td>
<td><strong>Post Cadbury and its successors</strong></td>
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<tr>
<td>1998</td>
<td>Hampel Report</td>
<td>LSE, CBI, IOD, NAPF, CCAB,</td>
<td>Review and revise the findings of the Cadbury and Greenbury report and recommends procedures to deal with institutional investors.</td>
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<td>ABI</td>
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<tr>
<td>1998</td>
<td>Combined Code</td>
<td>LSE, FRC, CBI</td>
<td>Drawing on the work of the Cadbury, Greenbury and Hampel committees, the original Combined Code.</td>
</tr>
<tr>
<td>1999</td>
<td>Turnbull Report</td>
<td>ICAEW</td>
<td>Best practice and principles-based approach to the implementation of a sound system of internal control and reporting to shareholders on internal control.</td>
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<tr>
<td>2000</td>
<td>Combined Code</td>
<td>LSE, FRC, CBI</td>
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<td>2001</td>
<td>Myners Report</td>
<td>UK Treasury</td>
<td>Institutional Shareholders in UK; focus on UK pensions industry.</td>
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<td><strong>Enron and the financial crisis</strong></td>
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<tr>
<td>2003</td>
<td>Higgs Report</td>
<td>DTI</td>
<td>Role and Effectiveness of NEDs; many recommendations of the Higgs report were included in the Combined Code.</td>
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<tr>
<td>2003</td>
<td>Smith Report</td>
<td>FRC</td>
<td>Recommendations in relation to the audit committee and the role of directors serving on the audit committee.</td>
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<tr>
<td>2003</td>
<td>Combined Code</td>
<td>FRC</td>
<td>Revisions to the Code.</td>
</tr>
<tr>
<td>2004/2005</td>
<td>Review of the Impediments to Voting UK Shares</td>
<td>FRC</td>
<td>Report by Paul Myners allow greater audit trail of vote instructions and increased transparency between issue and beneficial owner.</td>
</tr>
<tr>
<td>2006</td>
<td>Combined Code Revised</td>
<td>FRC</td>
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<tr>
<td>2008</td>
<td>Higgs Report Revised</td>
<td>DTI</td>
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<tr>
<td>Year</td>
<td>Name of the Report</td>
<td>Issuer</td>
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<tr>
<td>2008</td>
<td>Combined Code Revised</td>
<td>FRC</td>
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**Banking and the financial crisis**

<table>
<thead>
<tr>
<th>Year</th>
<th>Name of the Report</th>
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<tbody>
<tr>
<td>2009</td>
<td>The Walker Review23</td>
<td>HM Treasury</td>
<td>Review of corporate governance in UK banks and other financial industry entities</td>
</tr>
<tr>
<td>2010</td>
<td>Stewardship Code</td>
<td>FRC</td>
<td>To improve the quality of engagement between asset managers and companies to help improve long term risk adjusted returns to shareholders.</td>
</tr>
<tr>
<td>2010</td>
<td>UK Corporate Governance Code (Combined Code dropped and renamed)</td>
<td>FRC</td>
<td>Standards of good practice in relation to board leadership and effectiveness, compensation, accountability and relations with shareholders.</td>
</tr>
<tr>
<td>2012</td>
<td>UK Corporate Governance Code</td>
<td>FRC</td>
<td>The changes to the UK Corporate Governance Code are designed to give investors greater insight into what company boards and audit committees are doing to promote their interests, and to provide them with a better basis for engagement24. The Code revision in 2012 added a recommendation that FTSE 350 companies should put their external audit contract out to tender at least every ten years.</td>
</tr>
<tr>
<td>2012</td>
<td>Stewardship Code revised</td>
<td>FRC</td>
<td>Changes to 2010 Code relate to definition of stewardship, clarification of the role of asset owner.</td>
</tr>
<tr>
<td>2014</td>
<td>UK Corporate Governance Code</td>
<td>FRC</td>
<td></td>
</tr>
<tr>
<td>2014</td>
<td>Stewardship Code revised25</td>
<td>FRC</td>
<td>The UK Stewardship Code, which provides guidance on good practice for investors, should be seen as a companion piece to the UK corporate governance code.</td>
</tr>
</tbody>
</table>


DISCUSSION

Table 3 shows that the Cadbury report has been a catalyst for bringing out a quasi-law in response to corporate failures and legitimating the principle-based over the rule based forms of regulation in order to maximise compliance. Importantly, market based mechanisms are less prescriptive and adoption of the self-regulation helps to minimise direct interventions in the markets by the government or the Central Bank. Although the focus of the Cadbury Report can be considered too narrow, for example focusing on the control and reporting functions of the board, the role of auditors and shareholders, nevertheless it has positively contributed to good corporate governance. The Cadbury Report has spent considerable effort within its main provisions of the Code of Best Practice (see p.58-59) to outline the relationship between the directors, shareholders and the auditors - which arguably was a key part of making this report prominent (Dewing and Russell, 2004; Jordan, 2013).

The four main provisions within the Code of Best Practice are:

The board should meet regularly; retain full and effective control over the company and monitor the executive (s1.1)

Non-executive directors should bring an independent judgement 10 bear on issues of strategy, performance, resources, including key appointments, and standards of conduct. (s2.1)

Directors’service contracts should not exceed three years without shareholders’ approval. (3.1)

It is the board’s duty to present a balanced and understandable assessment of the company’s position. (4.1)

The Code of Best Practice recommended the roles of the CEO and chairman to be separate, (s1.2), inclusion of independent non-executive directors (s1.3; s2.1) and recommending that the audit committee should have at least three non-executive directors (s4.3) and the remuneration committees to be made up wholly or mainly of non-executive directors (s3.3). Evidence suggests that the separation of the CEO and Chairman of the board was more common in the European countries i.e. the German system where a dual board structure exists with the supervisory board and the management board. However, the corporate governance literature is still dominated by US-based research where the roles of chairman and CEO are mostly entrusted within the same person. Despite the recommendation by the US Sarbanes-Oxley Act (2002) minimal attention is given to addressing the separation of the two roles.

Since the Cadbury Report we have seen proliferation of codes (Aguilera and Cuervo-Cazurra, 2009) issued mainly by institutions (such as Pan European, Commonwealth, OECD and international Corporate Governance Network) and at the national level. However, we are also seeing codes issued by individual firms, for example, General Motors (Cuomo et al., 2015). Though the OECD principles does not recognise that one size should fit all, nevertheless, the over rational and framework for corporate governance has been derived from assumptions of liberal market economies (Hall and Soskice, 2001) and the primacy of shareholders. Typical examples of liberal market economies are the US and the UK, characterised as having strong market institutions, which coordinate the economic actors (Akkermans, Castaldi and Los, 2009).
At the EU level voluntary codes have been more popular. The mandatory adoption of the SOX had mixed outcomes such as the mandatory audit committees were defeated at the European parliament (Jordan, 2013). According to the comparison of the Cadbury, Vienot and Peter reports show similarities in recommendations such as truly independent directors, separation of chairman and CEO roles and self-regulation. An important legacy of the Cadbury report is the widespread acceptance of the division of the roles of Chief Executive and Chairman Sir Stuart Rose at Marks and Spencers is one of the few prominent people to have recently combined the two roles. M&S shareholders voted against him continuing in both jobs by margin of almost 38 per cent at the 2009 AGM.

Compliance requirements differ across countries

The compliance with corporate governance codes required by stock exchanges has varied. To date, most governance codes introduced in the OECD member countries employ the comply or explain approach according to which listed companies may disregard aspects of the code, but in that case should disclose this fact as well as their motives. The alternative is mostly to require full disclosure of companies’ corporate governance arrangements relative to the topic comply or explain was facilitated by the adoption of the EU Directive 46 (2006), which has been integrated into the national regulatory frameworks of member states. In market places operating by comply or explain, a primary role for stock exchanges has been to ensure that company disclosures remain meaningful and are not reduced to a box-ticking exercise.

The comply or explain approach permits variations for the managers in terms of the level of disclosure and enforcement. For example, a listed company may be requested to disclose whether it complies with individual recommendations of the code or merely with the code globally. In terms of the enforcement, the ability of exchanges or other regulators to pursue companies, which do not provide adequate levels of disclosure, also varies. In most cases, codes are subject to some form of regulatory enforcement, but they may also be subject to enforcement largely by shareholders. For example, in Netherlands shareholders of the company are responsible to put in force adherence to material rules. In addition, shareholders decide whether boards have provided sufficient information in case of non-compliance. In contrast, in France, the question of enforcement may be more or less left to market forces. In most instances, stock exchanges are in some way involved in monitoring the compliance status although, again, their ability to take enforcement action differs based on the legal basis of the code and the national securities regulation frameworks.

The different corporate governance systems may be useful and form the point of debate for academics, however they tend to emphasise overly broad distinctions that are blurring as the governance systems are converging.

Should the corporate governance code be given full statutory backing since the corporate governance code without statutory backing does not have the force of law. While the Code allows listed companies to deviate from its provisions, listed companies must provide considered reasons within their Corporate Governance Report in their annual reports for any deviation.

The UK Corporate Governance Code does not apply to Alternative Investment Market (AIM) companies. AIM is LSE’s international market for smaller growth companies. Hence, AIM is a less regulated market, attracting companies from around the world by its light touch regime. The company’s nominated adviser or nomad oversees and supports the AIM company, given the absence of regulation. The Quoted Companies Alliance has developed a
A corporate governance code for the smaller companies, which are a set of minimum standards to be followed in their entirety, however most companies describe their governance systems in their annual reports.

**UK Corporate Governance Code 2014**

The FRC’s 2014 UK Corporate Governance Code goes beyond the traditional Cadbury report, although maintaining most of the content and the norms and rules of the report, but focusing on behavioural change among directors rather than introducing new technical requirements. (PwC)²⁶. Hence, as the preface to UK Corporate Governance Code 2014 states:

> One of the key roles for the board includes establishing the culture, values and ethics of the company. It is important that the board sets the correct ‘tone from the top’. The directors should lead by example and ensure that good standards of behaviour permeate throughout all levels of the organisation. This will help prevent misconduct, unethical practices and support the delivery of long-term success (UK Corporate Governance Code 2014, Preface p. 2).

The other key change from the Cadbury Report is that companies need to augment their governance practices in areas of setting risk appetite, risk management and internal control and how they manage going concern assessment and reporting. The pervasiveness of this change is emphasised in the press release as Stephen Hadrill, CEO of the FRC puts it:

> The changes to the Code are designed to strengthen the focus of companies and investors on the longer term and the sustainability of value creation. The changes on going concern implement the reforms proposed by Lord Sharman whose work has stimulated a sea change in thinking about the assessment and reporting of risk and business prospects.

The revised UK Corporate Governance Code 2014, changes in relation to the going concern requiring new formal statements or confirmations by the directors, thus bringing it in line with accounting and auditing standards. This change was not taken lightly and provoked strong argument over the consultation period. The directors now need to confirm regarding the going concern as follows:

> In annual and half-yearly financial statements, the directors should state whether they considered it appropriate to adopt the going concern basis of accounting in preparing them, and identify any material uncertainties to the company’s ability to continue to do so over a period of at least twelve months from the date of approval of the financial statements. (2014 Code provision C.1.3).

> In addition, to the above there is now requirement for two other statements. First, in relation to the ‘robust assessment of principal risks’ requiring the directors to confirm, reflecting the view of the FRC regarding solvency and liquidity risk been formally integrated into the main risk and internal control framework within the companies, thus requiring a description of the way the risks are being mitigated:

Confirm in the annual report that they have carried out a robust assessment of the principal risks facing the company, including those that would threaten its business model, future performance, solvency or liquidity. The directors should describe those risks and explain how they are being managed or mitigated (2014 Code provision C.2.1).

Second, requires a "viability statement" where directors will explain in the annual report their assessment of the company as follows:

Over what period they have done so and why they consider that period to be appropriate. The directors should state whether they have a reasonable expectation that the company will be able to continue in operation and meet its liabilities as they fall due over the period of their assessment, drawing attention to any qualifications or assumptions as necessary. (2014 Code provision C.2.2).

This is perhaps the most contentious issue as the period covered needs to be significantly longer than twelve months. Over time, the market will eventually decide the period and the value added.

As well as the changes to risk and internal control that relate directly to going concern, the Code provision (2014 Code provision C.2.3) sets out the Board’s role in the ongoing monitoring as is the case under the Turnbull Guidance. Other changes relate to auditor report, remuneration and investor relations.

**The role of the Institutional investors in Corporate Governance**

The Financial Reporting Council has made additions and adjustments to the UK Corporate Governance Code, in particular to the information disclosure. The annual report should contain a description of the policy of the board of directors on diversity, measurable objectives that the board has set in the implementation of the policy and progress in achieving these objectives.

There are two key tasks at the top of every public company — the running of the board and the executive responsibility for the running of the company’s business. There should be a clear division of responsibilities at the head of the company which will ensure a balance of power and authority, such that no one individual has unfettered powers of decision.

On the surface, this principle appears to forbid combining the roles of CEO and chairman. However, the code provisions suggest that the roles may be combined as long as the rationale for such a decision is disclosed. Regardless of whether the roles are combined or not, there is a requirement for a strong independent non-executive element on the board, including an identified senior independent director (sometimes referred to as a lead director), through whom concerns may be relayed to the board.

**CONCLUSIONS**

Durisin and Puzone (2009); Gay (2001) acknowledge the Cadbury Report as the "seminal event in the history of corporate governance in the UK." Further, no one would question that the development of the Cadbury Report in 1992 has directed attention in initiating worldwide
awareness in corporate governance and its commitment to the development of governance mechanisms to endorse it. The most significant feature of the UK Corporate Governance Code is that it is not written law by legislatures, but a voluntary code. In the Continental European legal system, a voluntary code is an oxymoron (Jordan, 2013). The Cadbury Report lives on in the UK and the adoption of its voluntary nature and “comply or explain” approach to corporate governance, both seen as the strengths of the UK corporate governance. The numerous academic articles have not changed their attitudes toward corporate governance

We believe that our approach, based on compliance with a voluntary code coupled with disclosure, will prove more effective than a statutory code. (s1.10)

A significant concern is whether the UK corporate governance code will become a rulebook, main conviction is given the increasing use of EU driven regulations, which tend to be mandatory. Nevertheless, it is important that the UK corporate governance remains voluntary in nature and provide the flexibility for companies to be able to deviate from the Code, but when they do the boards should provide a detailed explanation, thus maintain the comply or explain approach. We conclude that 25 years on the flexibility of the Cadbury Report is still evident in the UK corporate governance and under the current politics we do not expect to see any reduction in the use of a voluntary code of best practice and the comply or explain approach.

Corporate governance is of profound significance where corporate structures still exist if we continue to have strong managers and weak shareholders. While the legal and regulatory environment sets the framework within which choices are made, however, the board makes decisions within companies This paper has touched upon an array of important corporate governance attributes within the context of the UK and particular questions raised on whether to continue with the self-regulation or bring in regulatory intervention. More research is needed to assess the impact of Anglo-Saxon model of corporate governance and convergence of other national codes towards this system.
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