



Consultants in  
Organization Effectiveness,  
Leadership &  
Pay for Performance

# Governance & Global Finance for a Sustainable Planet

International Society for Systems Sciences  
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&

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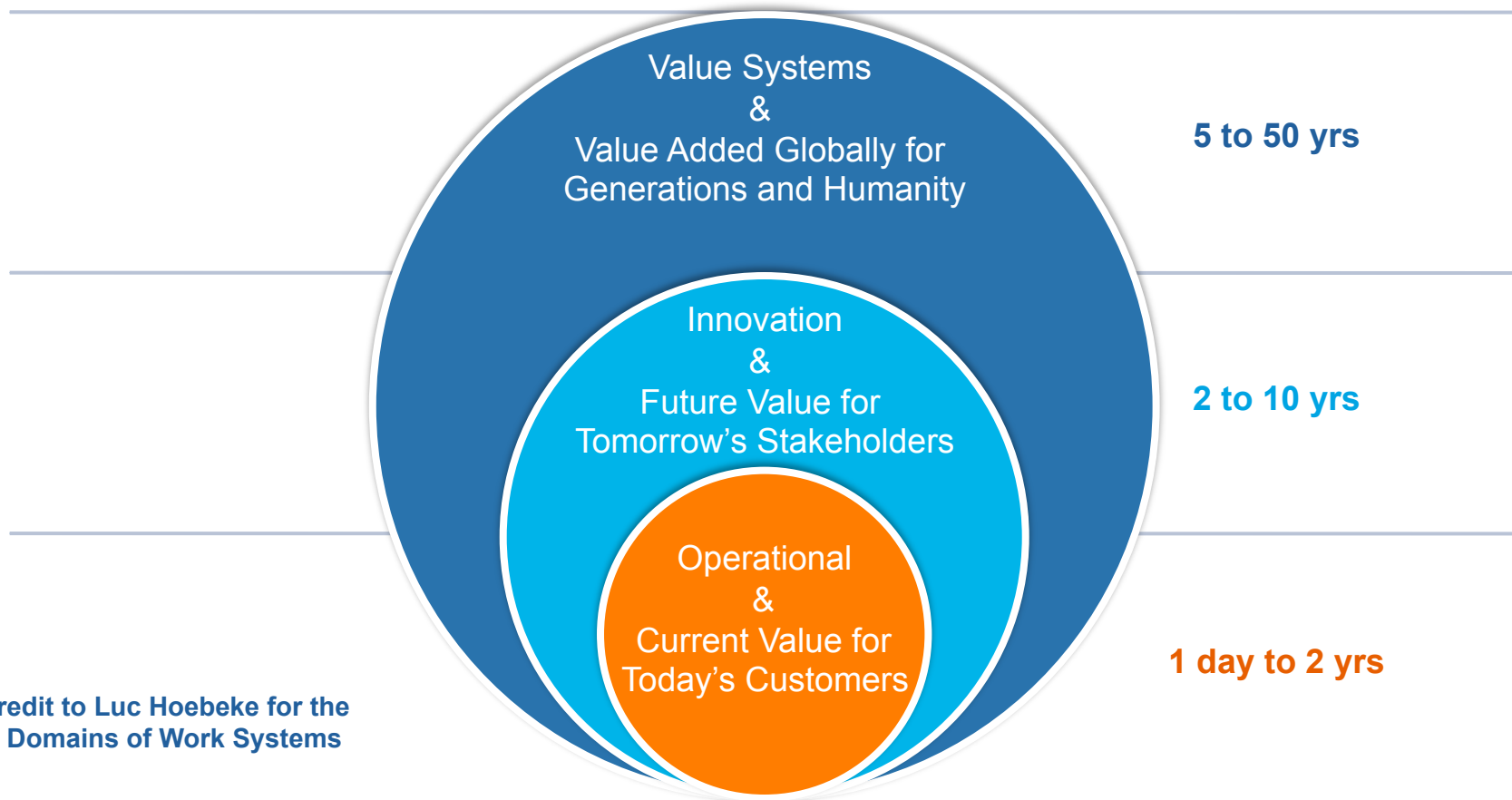
# Corporate Governance Today Neither Viable or Sustainable

- 40 % Lacking Financial Viability (Not a Viable Economic System)
  - Credit Suisse Holt Performance Database: Market Capitalization > \$1 Billion in 2008
    - $2376 / 4992 = 47\%$  = number of global companies with CFROI return (appendix) (intrinsic value) less than cost of capital in 2008 (destroying shareholder value)
    - $1700 / 4992 = 34\%$  = number of companies where average CFROI over 20 years is less than cost of capital (destroying shareholder value)
- 85 % + Not Sustainable Longer-Term
  - Based on Proxy Statement Disclosures for CEO Metrics & Incentives
    - 85 % not held accountable or incented for Business Performance beyond 3 years
    - 90 % have NO non-financial measures of success & contribution to broader society ( Triple Bottom Line metrics & incentives )
- Boards & Institutional Shareholders Have Approved These Systemically Flawed Designs of Executive Accountability & Incentives while USA CEO Pay has climbed 6X over 20 years

We Need a New Model of  
Corporate Governance that Reflects the  
Complexity and Scale of the System  
being Governed

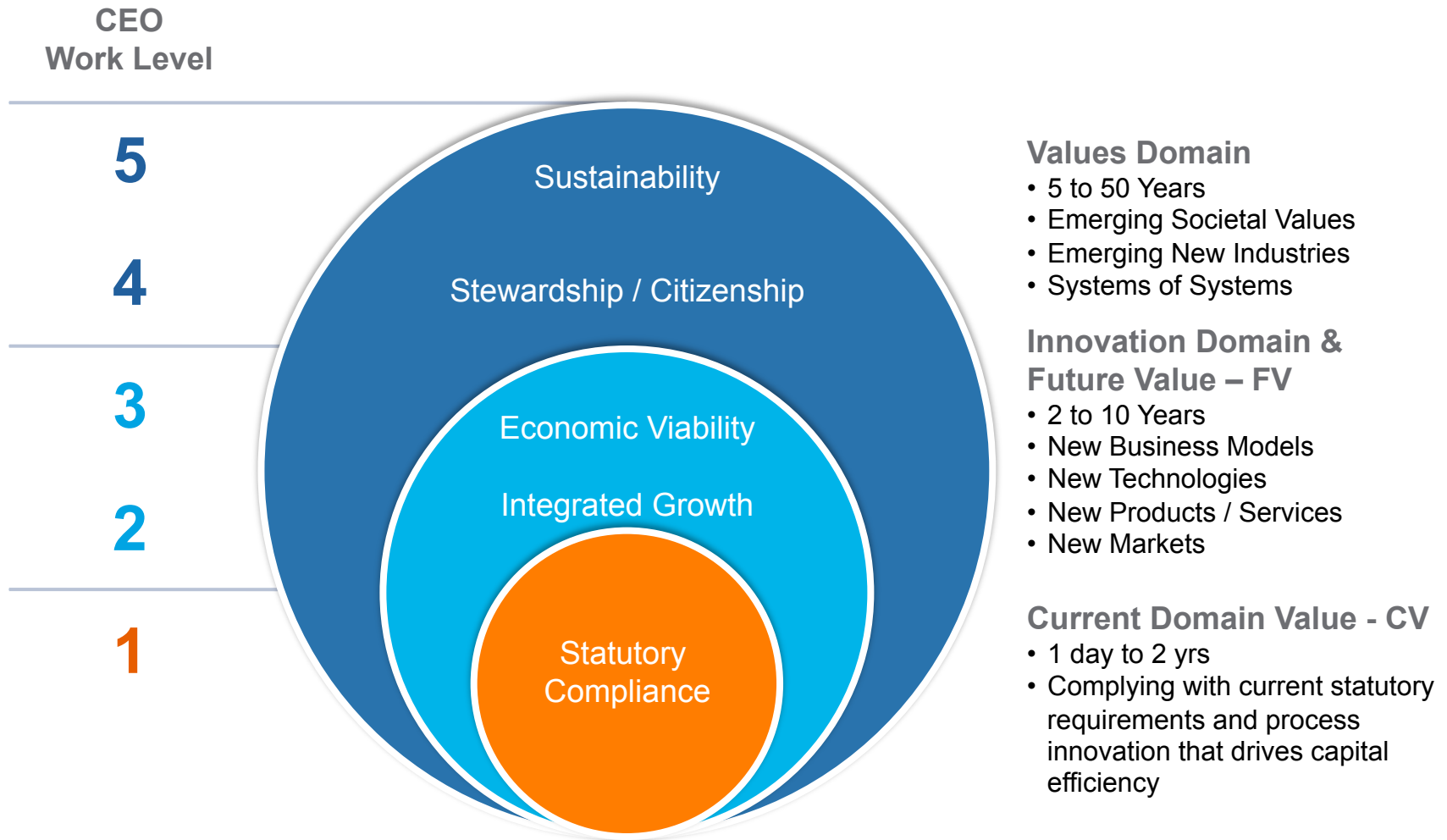
# 3 Domains of Work Systems

Different Process Levels &  
Time Scales of Work Systems

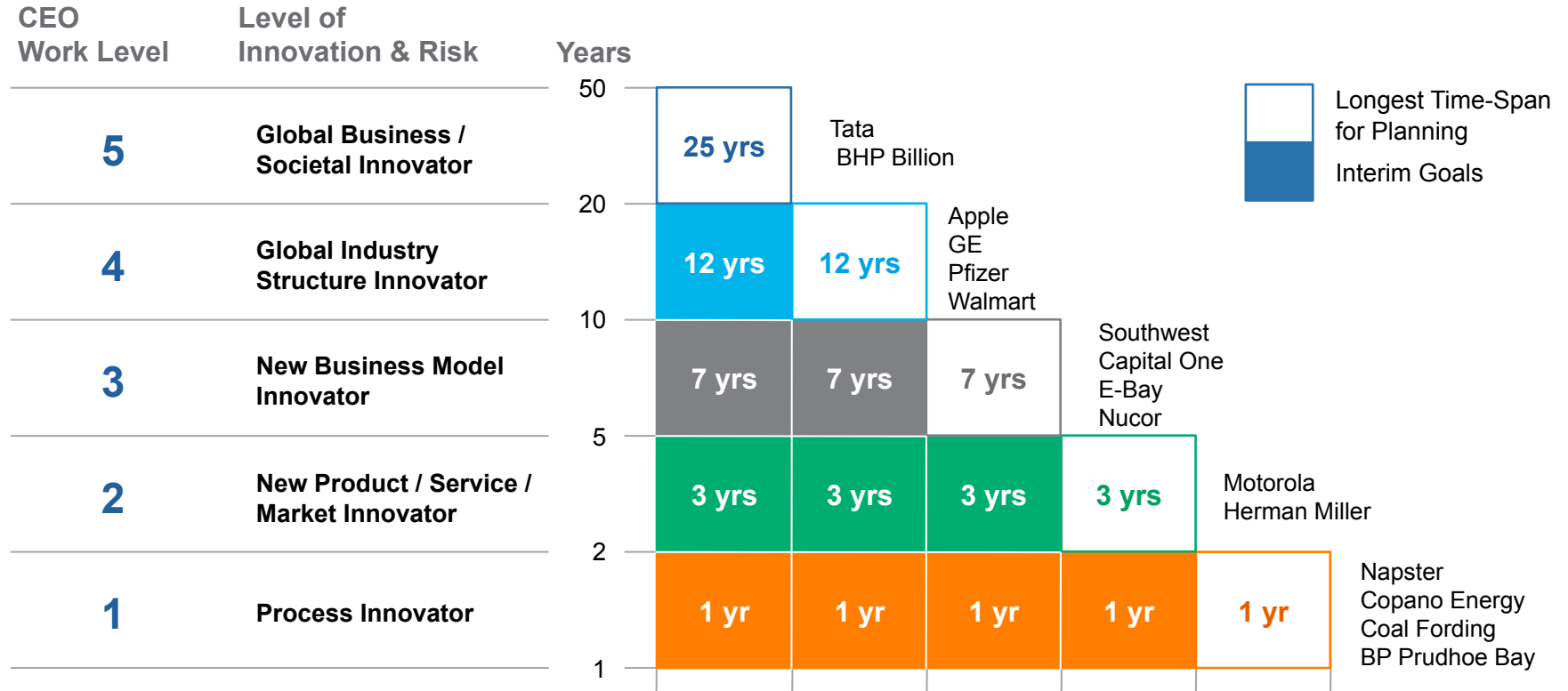


Credit to Luc Hoebeke for the  
3 Domains of Work Systems

# 5 Levels of CEO Work Across 3 Domains of Work Systems



# 5 Levels of CEO Work, Innovation & Risk Management



Based on 500+ MVC Interviews at the Global CEO, Group President, President, and VP/General Manager Levels of General Manager Leadership

# 5 Levels of CEO Work & Required 5 Levels of Corporate Governance

CEO Work Level	Level of Innovation & Value Creation	Time-Span for Risk Management	Governance for Whom?	Level of Governance
<b>5</b>	Global Business / Societal Innovator	20+ yrs	Humanity, Future Generations, Association of LT Owners	Sustainability, Capitalism, Contribution to Global Peace & Prosperity
<b>4</b>	Global Industry Structure Innovator	10 to 20 yrs	Individual Societies Worldwide	Stewardship of Business & Public Good
<b>3</b>	New Business Model Innovator	5 to 10 yrs	Community of Stakeholders	Business Model Strategy & Viability
<b>2</b>	New Product, Service, Market, Innovator	2 to 5 yrs	Association of Medium-Term Owners	Integrating Business Growth & Risk Mgmt Short to Medium Term
<b>1</b>	Process Innovator	1 to 2yrs	Regulators & Law Makers	Statutory Compliance

# 5 Levels of Corporate Governance

Not All Boards & Directorship Roles are Created Equal

Level of Governance (LOG)

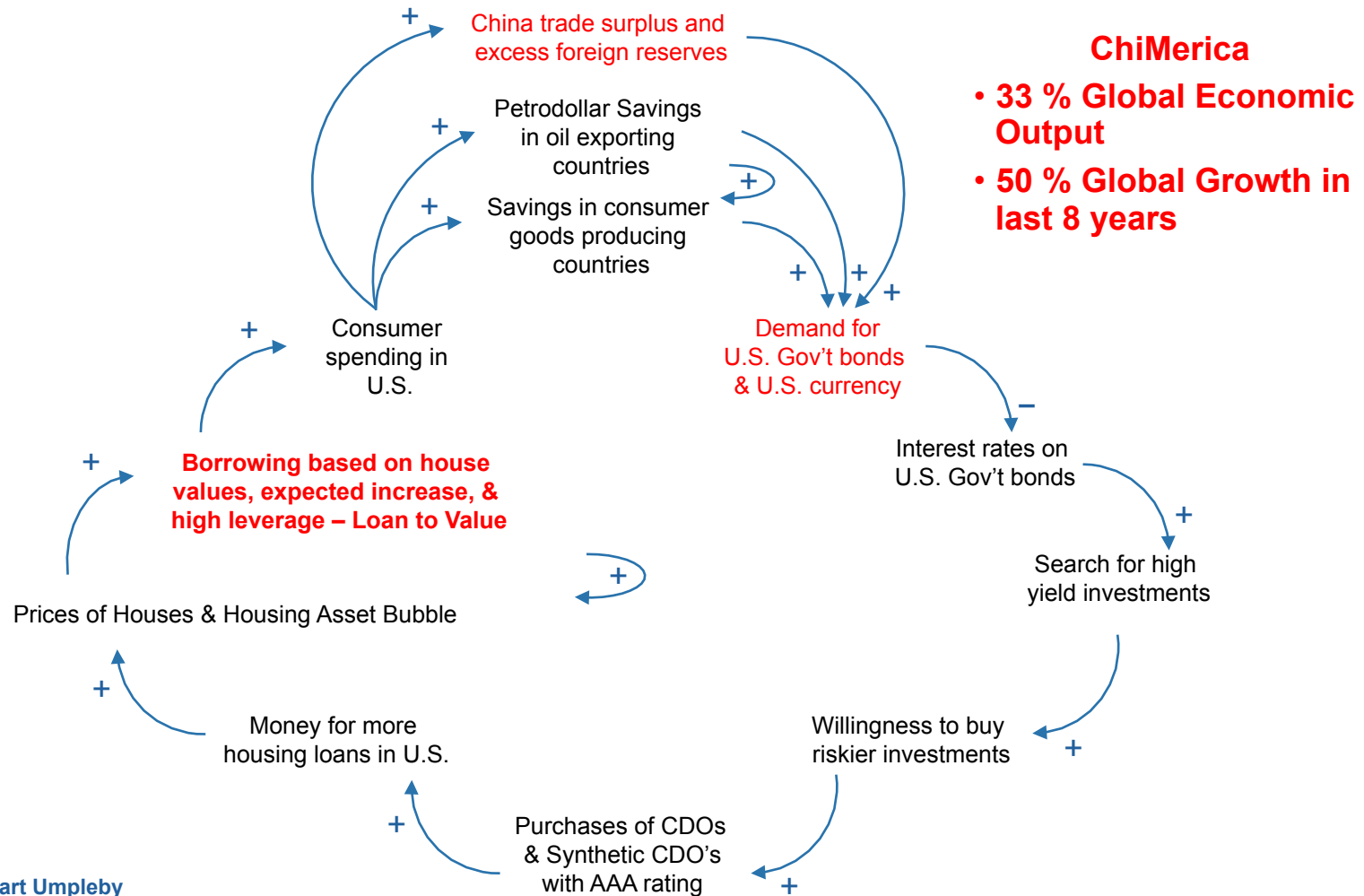
<b>5 Sustainable</b>	Enterprise Sustainability, Capitalism, Contribution To Global Prosperity					
<b>4 Ethical</b>	Stewardship Of Businesses, Citizenship & Public Good					
<b>3 Strategic</b>	Strategic Duty & Business Model Viability					
<b>2 Integrative</b>	Integrating Business Growth & Risk Mgmt Short to Medium Term					
<b>1 Compliance</b>	Statutory Compliance					
<b>Themes of Complexity of CEO Work &amp; Corporate Governance</b>		Process Innovation	New Product, Service, Market, Innovation	New Business Model Innovation	Global Industry Innovation	Global Business Societal Innovation
		<b>1</b>	<b>2</b>	<b>3</b>	<b>4</b>	<b>5</b>
		<b>CEO Work Level</b>				



# A Systems Look at Failing Corporate Governance:

- The Global Financial System & Credit Crisis
- USA Electric Utilities & Cleaner Energy Systems

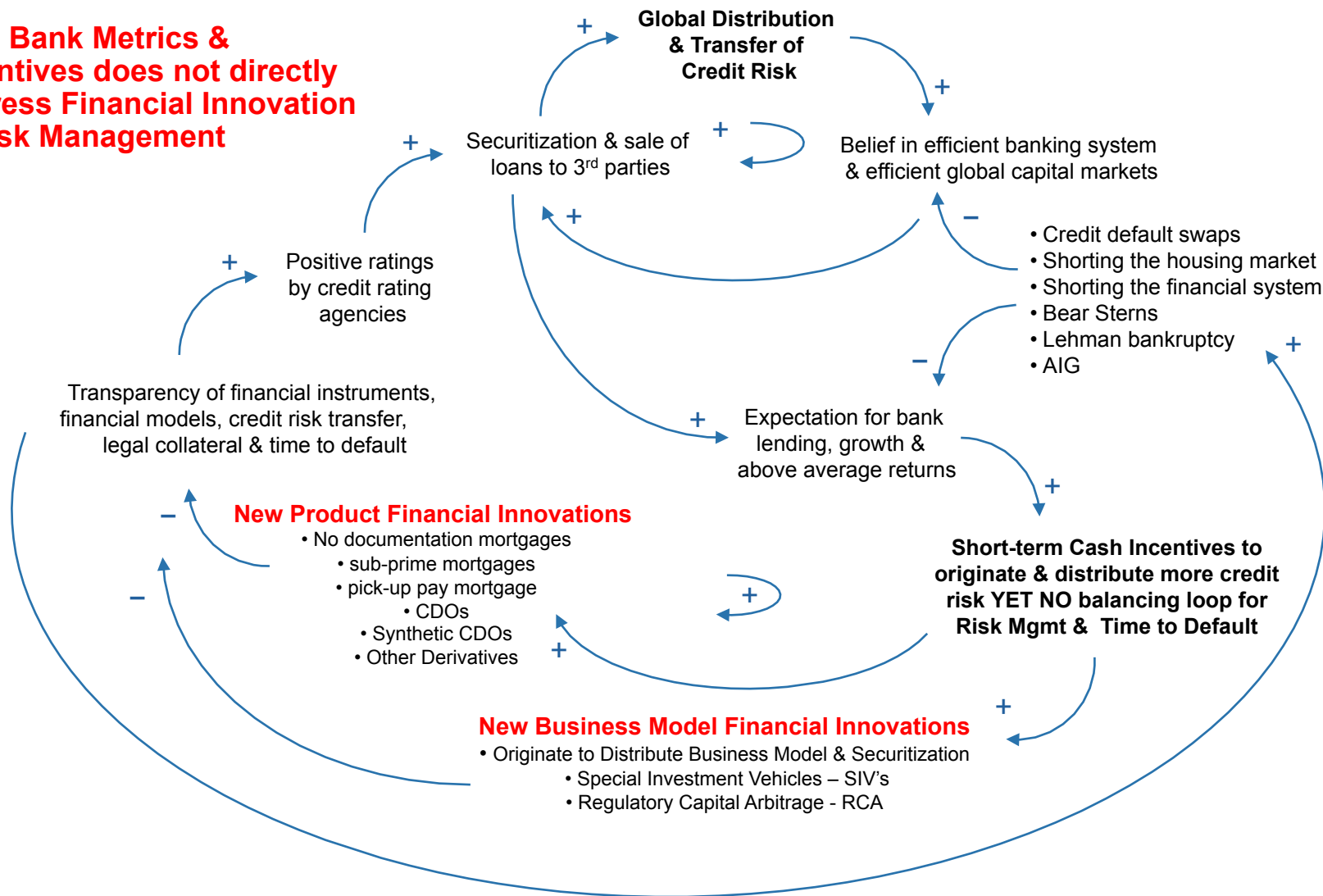
# China, America & the Global Aspects of the Super Credit Cycle



Adapted from Stuart Umpleby

# Incentives, Innovation, Ponzi Finance & Credit Risk Transfer System

**2010 Bank Metrics & Incentives does not directly address Financial Innovation & Risk Management**



# 2007 Bank Safety & Soundness Metrics & Incentive Design

Safety & Soundness Performance Metrics (sample disclosed metrics)	Number of Banks	Specific Bank identified from 2008 proxy season SEC filing
Performance measurement and incentive design aligned to Tier One Capital Ratio and or Bank Liquidity	5	<ul style="list-style-type: none"> <li>• JP Morgan Chase</li> <li>• Wells Fargo</li> <li>• Morgan Stanley</li> <li>• Capital One</li> <li>• Key Corp</li> </ul>
	5 of 18 = 28 %	With Safety & Soundness Metrics

Based on the 18 largest US Banks still in operation in 2010 & filed proxy statements with the SEC

- Key Points**
- The US banking system in 2007 was not designed to hold executive management accountable nor incent them to manage bank safety and soundness
  - This does not include the largest financial institutions which have been sold or under went bankrupt in the last 36 months

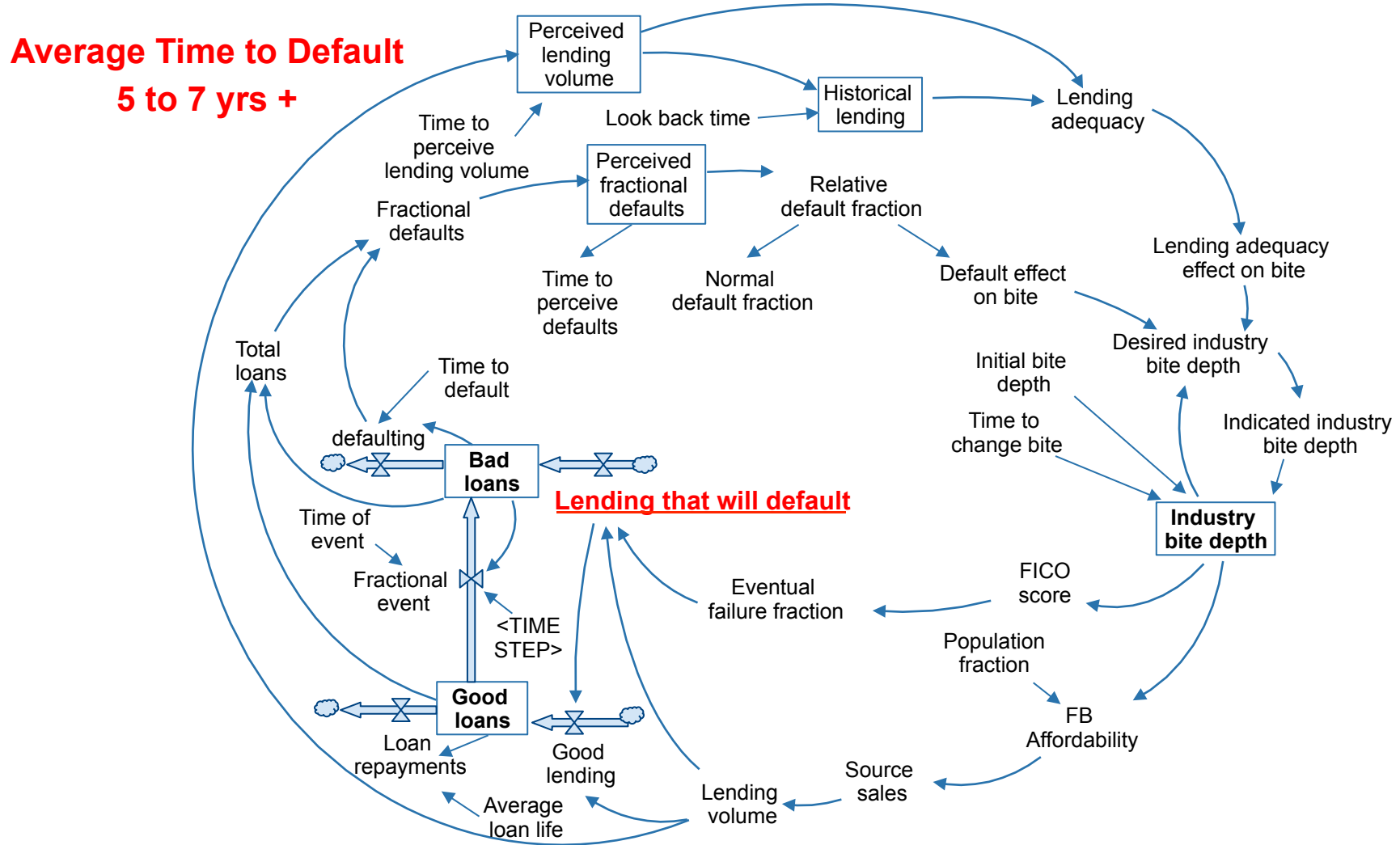
# 2007 Risky Growth, Innovation & Incentive Design

Innovation & Future Growth Performance Metrics (sample disclosed metrics)	Number of Banks	Specific Bank identified from 2008 proxy season SEC filing
<p>Total Return to Shareholder – TSR - as a key performance and incentive metric to drive growth and financial innovation</p> <p>YET</p> <p>NO balancing performance metric for ensuring Bank Safety and Soundness including minimum:</p> <p>Tier One Capital Ratio</p> <p>and</p> <p>or Bank Liquidity</p>	<p><b>9</b></p>	<ul style="list-style-type: none"> <li>• Bank of America</li> <li>• Citicorp</li> <li>• American Express</li> <li>• US Bancorp</li> <li>• PNC</li> <li>• Bank of NY Mellon</li> <li>• Sun Trust</li> <li>• Fifth Third</li> <li>• M&amp;I</li> </ul>
	<p><b>9 of 18 = 50 %</b></p>	

- Key Points**
- Over 50 % of the banks and their Named Executive Officer roles were measured and incented on growth and Total Shareholder Return with No Regard for Risk Management and or Bank Safety and Soundness
  - The world got what the banking system was design to measure and reward

# The Lending / Credit System

Good Loans, Bad Loans, Market Share & Time-Delayed Feedback Loops



Source: SACU – San Antonio Federal Credit Union used with permission

# 2009 Longest Accountable Performance Period For Incentive Reward Average 2.2 yrs

Longest Accountable Performance Period for Named Executive Officers	Number of Banks	Specific Bank identified from 2010 proxy season SEC filing
3 yrs	10 (54%)	<ul style="list-style-type: none"> <li>• Wells Fargo</li> <li>• Morgan Stanley</li> <li>• US Bancorp</li> <li>• PNC</li> <li>• Capital One</li> <li>• Sun Trust</li> <li>• BB&amp;T</li> <li>• Comerica</li> <li>• Fifth Third</li> <li>• M&amp;I</li> </ul>
2 yrs	2 (12%)	<ul style="list-style-type: none"> <li>• American Express – credit for next year – 3 yrs currently one yr 2009 – was 6 yrs in 2008</li> <li>• KeyCorp</li> </ul>
1 yr	6 (34%)	<ul style="list-style-type: none"> <li>• Bank of America</li> <li>• JPMorgan Chase – disclose look longer-term i.e the business cycle - no clear perfm periods</li> <li>• Citicorp</li> <li>• Goldman Sachs</li> <li>• Bank of New York Mellon</li> <li>• Regions Financial</li> </ul>
<b>Total</b>	<b>18</b>	
<b>Averaged Weighted Performance Period for 90 Named Executive Officers = 2.2 yrs</b>		

- The US banking system in 2010 still has a major systemic failure with the Average Accountable Performance Period of 2.2 years YET Average time to Credit Default at 7 to 10 yrs +
- Boards & Shareholders are confusing longer-term pay delivery vs. Accountable Performance Cycle

# 2009 Customer / Stakeholder Performance Metrics & Incentive Design

Customer / Stakeholder Performance Metrics (sample disclosed metrics)	Number of Banks	Specific Bank identified from 2010 proxy season SEC filing
<ul style="list-style-type: none"> <li>• Customer Satisfaction</li> <li>• Customer Service</li> <li>• Customer Retention</li> <li>• Customer Development</li> <li>• Regulatory Relationship</li> </ul>	<b>6</b>	<ul style="list-style-type: none"> <li>• JPMorgan Chase</li> <li>• Citi</li> <li>• Morgan Stanley</li> <li>• American Express</li> <li>• Capital One</li> <li>• Regions</li> </ul>
	<b>6 of 18 = 33 %</b>	

- Only 33 % ( 6 of 18 ) US banks post credit crisis are holding management accountable for and incenting them for developing & managing longer-term customer & regulatory relationships
- Possible failure to see banks with a broader economic development and public good accountability



# In 2010 - 44 % - US Banks Still Lack Safety & Soundness Metrics in Incentive Design: Not designed for Bank Viability nor Sustainability

Safety & Soundness Performance Metrics (sample disclosed metrics)	Number of Banks	Specific Bank identified from 2010 proxy season SEC filing
<ul style="list-style-type: none"> <li>• Tier One Capital Ratio</li> <li>• Liquidity</li> <li>• Non Performing Assets Ratio</li> <li>• Loan / Deposit Ratio</li> <li>• Credit Loss Risk Management</li> </ul>	<b>10</b>	<ul style="list-style-type: none"> <li>• JPMorgan Chase</li> <li>• Citicorp</li> <li>• Morgan Stanley</li> <li>• American Express</li> <li>• PNC</li> <li>• Capital One</li> <li>• Sun Trust</li> <li>• Bank of NY Mellon</li> <li>• Fifth Third</li> <li>• KeyCorp</li> </ul>
	<b>10 of 18 = 56 %</b>	With Safety & Soundness Metrics

- 3 years after the start of the global credit crisis 44 % of the largest US banks still don't not have Bank Safety and Soundness Performance Metrics & Incentives hardwired into their systems
- The US banking system performance metrics, performance periods and incentive design is as risky in 2010 as it was prior to the global credit crisis (2007) and is set up for another Boom and Bust cycle

From the  
Banking System  
to  
US Electric Utilities &  
Cleaner Energy Systems

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# 2009 Incentive Design & Cleaner Energy Not Aligned / Designed For Sustainable Planet

Analysis & Statistical Summary	Longest Disclosed Performance Period	Energy Efficiency	Renewable Energy or Renewable Portfolio Standard	SMART Grid & or Distribute Energy	New Clean Energy Technology Investment & or related R&D	Green House Gas Reduction
	<b>3 years</b> (Average Risk Horizon & Capital Cycle of 10 to 20 yrs peak to trough)					
Mentioned in CD&A but NO specific metrics or targets disclosed		7 of 32 or 21 %	3 of 32 or 9 %	0 of 32 or 0 %	1 of 32 or 3 %	2 of 32 or 6 %
Disclosed Specific Metrics, Targets & Incentive Design		1 of 32 or 3 %	1 of 32 or 3 %	1 of 32 or 3 %	1 of 32 or 3 %	1 of 32 or 3 %

- Only 3 % (1 of 32) largest US investor owner utilities in 2009 had performance metrics and incentive design for named officer roles directly aligned to creating a cleaner energy future
- Institutional shareholders including public pension funds and sovereign wealth funds have approved this accountability, performance and incentive design through their proxy voting

# Changing the Corporate Governance Paradigm

# From Compliance to Sustainable Governance

- Performance Measurement & Incentive Design in two key sectors are not designed nor aligned for longer-term Viability or Sustainability
    - Performance Metrics and Incentives Designed by Directors
    - Performance Metrics and Incentives Approved by Shareholders
  - Boards Need to Move from Compliance Governance to Strategic & Sustainable Governance
  - Pension Funds as Investors Need to Move from Compliance Governance which is too often “check the box” to Strategic & Sustainable Governance
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## Key Take Away's

- Application of systems thinking brings great potential to understanding systemic business / economic / regulatory problems and solutions
  - Limits to Global Growth, a Systems Approach & Triple Bottom Line
    - include true costs and pricing longer-term for Global Society / Planet
  - Need for a New Corporate Charter
    - From Shareholder To Stakeholder model
  - Need for Systems Thinking Applied to Corporate Governance:
    - Board / Management need a systems view of strategy and risk mgmt
    - Institutional Investors need a systems view for Portfolio Mgmt ,Risk-Adjusted Returns, insightful Proxy Voting & Strategic Board Engagement
      - ( i.e. BP risks non financial - cant just focus on Financial Indicators which are lagging performance indicators )
    - Regulators need a systems view to ensure policy and regulation recognizes the interdependencies across the entire system they govern
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# Key Contact Information



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