The Conference Board of Canada
Insights You Can Count On

Building Customer Trust
A Roundtable Discussion

Toronto, Ontario, Canada
October 31, 2007

Trust Measures and Indicators for Customers and Investors

Part II: Measuring Trust Indicators for Investors

Trust Enabling Strategies

Alex Todd
President & CEO, Trust Enabling Strategies
16 Rosewell Ave., Toronto, Ontario CANADA M4R 1Z7
http://www.trustenablement.com
Tel. +1 416.487.1497, Fax. +1 416.487.9646
AlexTodd@TrustEnablement.com

Abstract

The paper proposes a framework to help organizations monitor levels of trust for different stakeholder groups. Part I, contained in a separate document, examined various trust indicators to measure the relative presence or absence of trust, and the nature of that trust, in typical commercial relationships. It also introduced new trust concepts and proposed a novel framework for classifying conditions that indicate trust. Part II builds on these foundations and examines trust indicators for investors. Examples are used to demonstrate various ways the framework can be applied to measure trust indicators for investors with distinct needs.

Table of Contents

Abstract 2

Table of Contents 3

Introduction 5

Investor Confidence (Trust & Confidence) 7

Effects of Investor Trust and Mistrust 7

Trust Measures and Indicators 9

Assertions 10

Actions 11

Conditions 13

The Trust Enablement® Framework – a brief review 14

Applying The Trust Enablement® Framework to Indicate Trust 15

Assessing Investor Trust in the Economy 15

Predicting the Future 17

Effects of Altered Conditions for Trust 18

Monitoring Investor Use of Trust Enablers™ to Indicate Trust 18

Part II: Measuring Trust Indicators for Investors 21

Indicators for Investor Trust & Confidence in Capital Markets 21

Trust Indicators for Rebuilding Trust in Capital Markets 22

Trust Indicators in Sarbanes-Oxley 23

Trust Indicators in Media Recommendations 26

Comparing Trust Indicators 27

Priority Trust Indicators for Investors 30

Trust Indicators Used Through the Investment Process 30

Investor Types ____ 31

Equity Investors ____ 34

Investment Types ____ 35

Priority Trust Indicators for Committed (Institutional) Investors ____ 39

Trust Indicators for Strengthening the Demand-Side ____ 40

Corporate Governance ____ 42

Trust Indicators for Good Corporate Governance ____ 43

Indicating Trust from Corporate Governance Principles ____ 45

Governance Trust Indicators for Reducing Directors' and Officers' Liability Exposures ____ 47

Trust Indicators for Governance Practices that Improve Business Performance ____ 50

Investor-Facing Applications for the Trust Enablement® Framework ____ 53

Conclusions and Executive Summary ____ 55

 Trust Enabling Strategies

Introduction

In recent years, investors have suffered a crisis of trust. Tragic stock market corrections have shaken investor confidence in capital markets and even threatened the foundations of modern capitalism. The failure of institutions to uphold investor confidence in the liquidity, stability and value of their investments has initiated a wholesale review of the core assumptions that investors hold about the validity of customary business and economic practices. Previously sacred norms and widely accepted truths are being openly challenged. A groundswell of new ideas and business paradigms is emerging.

Trust is a term that until recently was virtually absent from business language. Today, it has surfaced from the world of social sciences as a driver of business design, on par with risk management. Whereas risk management is fundamentally a defensive posture for protecting corporate assets, Trust Enablement® is offensive. It helps companies get the resources they need to improve business performance.

Trust is more than governance, risk and compliance. Common management practices that serve as proxies for trust are also inadequate. Integrity, accountability, ethics, relationships, satisfaction, honesty and loyalty (even in the aggregate) fall short of creating sufficient conditions for trust and may even contribute to eroding it.

Financial analysts are starting to realize that the validity of their robust analysis depends entirely on trust in the proper functioning of the institutional systems that underpin all financial and economic transactions. Trust, in the developed world, is the product of highly developed institutional design, not primarily personal relationships. If an erosion of trust threatens capital markets and the foundations of capitalism, enhanced stakeholder trust will accelerate commercial transactions and economic prosperity.

Although we know trust when we feel it, its significance is so vital that it is no longer sufficient to rely only on gut feel and proxies for trust. The impact of various drivers for trust and their relative dynamics need to be understood as part of an integrated trust framework.

This paper examines the factors that affect investor trust and introduces novel approaches to indicate the presence or absence of trust, as well as the means to measure and compare trust indicators. It begins with a brief discussion of the significance of trust in business, followed by an examination of various approaches for indicating trust.

The recommended approach, based on the Trust Enablement® Framework, is used to attribute trust to investor actions by indicating conditions that contribute to the formation and preservation of trust. This paper begins by examining trust indicators for general investors, who rely on economic trends and the health of capital, and then analyzes the trust indicators critical to institutional investors with long-term stock holdings.

The case studies provide numerous examples of how the Trust Enablement® Framework can be used to measure trust indicators for investors, issuers and regulators. Issuers can use the recommended approach to optimize their business processes for specific investor trust objectives. Regulators can define industry codes that help generate more value in capital markets. Investors can benefit from embedding an integrated analytical framework into their evaluation tools to improve the validity of their investment confidence metrics.

Investor Confidence (Trust & Confidence)

The terms "trust" and "confidence" are often mistakenly used as synonyms. However, there are distinct differences. Although confidence is the overriding objective for investors, there are two ways for investors to become confident in their investments. Investors can attain sufficient levels of confidence in an investment either by trusting the issuer's management to optimize performance or by controlling management actions. Minority investors and investors of widely held public companies rely on trust. Entrepreneurs, family members of family owned businesses, venture capitalists and other private equity investors, on the other hand, often get their required level of confidence by exerting direct control over the board of directors and management. This paper discusses the trust indicators used by non-controlling investors.

Trust and control are strategic approaches to attaining confidence.

Effects of Investor Trust and Mistrust

The implications of public mistrust in capital markets can be catastrophic for national and global economies [i], and the long-term trend is alarming [ii] Large corporations are currently the least trusted institutions worldwide and their leaders even less so [iii]. Although public trust is returning in the wake of high profile corporate scandals over the past few years, the levels remain low, and some have argued that returning to previous levels of trust may no longer be sufficient [iv].

Trust is preferable.

Trust provides real economic benefits: it reduces transaction costs [v]; and is required for the efficient functioning of capital markets [vi]. The evidence proving the value of trust to both individual businesses [vii] and the economy [[viii]] is compelling. Institutions, large corporations in particular, play a significant role in creating and preserving conditions for trust [[ix]].

By contrast, the cost of transactions increases when laws, regulations and other controls respond to breaches of trust. According to a 2006 study discussed by OCEG [[x]], businesses are spending $1.1 trillion to comply with U. S. federal regulations. More significantly, breaches of trust contribute to a self-reinforcing propagation of mistrust [[xi]]. An organic property of trust is that trusting begets trust [[xii]] in a virtuous spiral of ever-increasing trust [[xiii]].

Trust Measures and Indicators

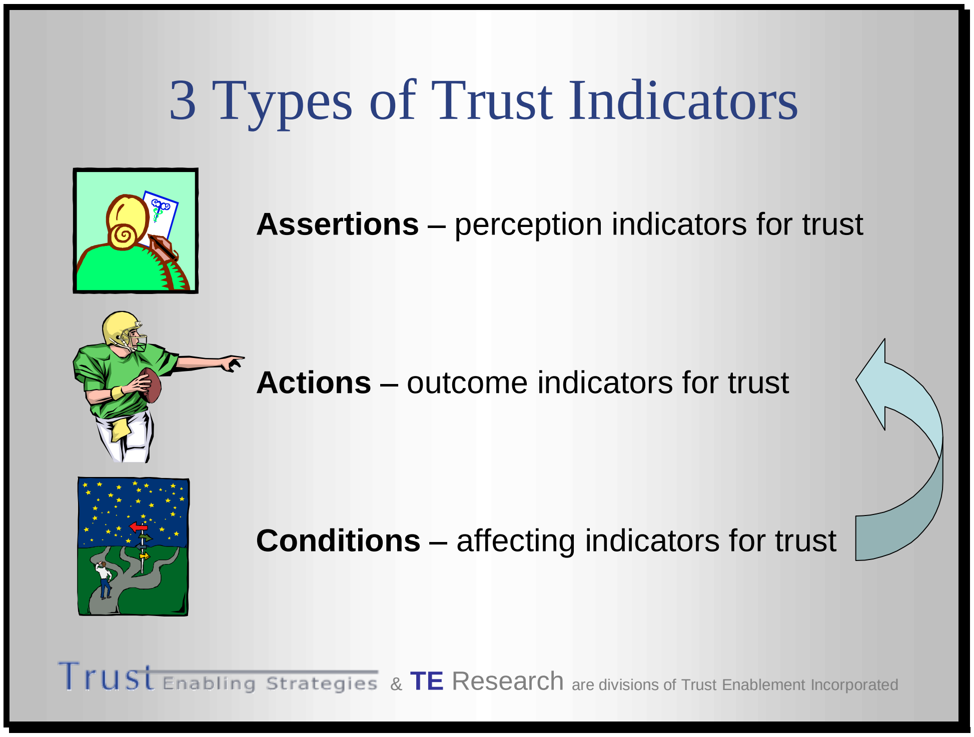
Part I of this paper, published in September 2007 discusses three ways that management can measure trust indicators for customers*. Here, in Part II, the discussion will focus on how the same methods can be used to measure* investor *trust. This section examines the use of the same methods to measure investor trust.*

Measurement matters [xiv]. A well-known maxim is "what gets measured gets done." All enterprise processes can benefit from measurement. Ideally, measurement of trust indicators will help organizations:

- demonstrate the results of trust optimization activities
- show how these results support enterprise objectives
- determine what works and what doesn't
- justify capital allocation
- promote accountability
- motivate and provide tangible feedback to employees
- enhance the value of stakeholder relationships
- drive business performance.

Trust measures matter for business performance.

Investors care about business performance. They also value the structures that provide them with valid indicators to trust in an issuer's past and future performance. These structures consist of sector-wide institutions and infrastructures, issuers' business processes, and investors' tools. Issuers have a significant role to play in helping to improve the trust indicators available to investors. They should also be motivated by the promise of higher and more stable share price valuations, less active shareholders, and lower liability insurance premiums that derive from high investor trust and confidence.



Assertions

Traditionally, the primary measure of consumer confidence and trust have been surveys like The Conference Board's monthly Consumer Confidence Index and Edelman's annual Trust Barometer. Although useful as a macroeconomic indicator of consumer sentiments, surveys are blunt instruments. They rely on what people say, rather than how they behave. Answers are influenced by what people have in mind when posed the questions, influenced by the way questions are phrased and the hypothetical scenarios they imagine for context.

Trust is the willingness to make oneself vulnerable. It is difficult for people answering a questionnaire to know how they will do until they are confronted with a real situation that forces them to act.

For example, studies show that nurses are more trusted than doctors. Does that mean cancer patients are more likely to rely on nurses to diagnose and treat them than oncologists? Clearly, a more precise question would produce a better answer. Nevertheless, closer observations may reveal that patients may seek second and third opinions from oncologists, but not so from nurses. This behaviour would indicate that nurses are sufficiently trusted by patients to provide adequate care, while oncologists, whose individual professional opinion patients find inadequate, are insufficiently trusted to diagnose and treat them.

Survey responses are biased.

Alternatively, game-theory-based studies have, in many cases, provided reliable simulations of trust in the real world. In fact, studies comparing people's survey results with their behaviour in games have produced conflicting results [xv], indicating biased survey responses.

Fortunately, capital market structures make it considerably easier to observe investor behaviour and rely less on surveys.

Actions

Behaviour is the best indicator of trust. Paying a premium for a product or service, making a large or longer-term commitment to a vendor, or forgoing prudent due diligence before buying -- all are behaviours that indicate higher levels of trust. Another good indicator of trust is when customers advocate for a vendor or recommend products and services to others. However, these actions, or their absence, cannot be attributed exclusively to trust or distrust.

Actions speak louder than words.

The best behavior indicators of investor trust are price/earnings ratios and the price investors are willing to pay for shares relative to the issuer's earnings. Higher price/earnings ratios generally indicate higher levels of trust in the future earnings of the issuer. However, even a high price/earnings ratio cannot be attributed exclusively to investor trust in the issuer's ability to maintain or grow historical earnings. A high share price may also reflect investor expectations about an impending acquisition, or may simply be due to sector-wide "irrational exuberance," a phrase made famous in 1996 by Alan Greenspan, U.S. Chairman of the Federal Reserve Board, referring to the fast-rising stock prices caused by the "dot-com" bubble phenomenon.

Trust is always contextual. What did investors trust about share prices in the Internet sector? They trusted the emergence of the Internet to be an unprecedented new economic growth opportunity. They also trusted their peer investors' "infectious greed," as Greenspan called it, to fuel the flames of share price inflation for as long as they could. Although their trust was well founded, it was not based on the intrinsic value of the shares. This was not trust, but "irrational exuberance." Behaviour that superficially appears to be the result of trust, such as high price/earnings ratios, can really be a consequence of other influences. In some cases, those influences can look very much like trust, but upon closer inspection may be something closer to blind faith.

Attributing actions to trust is difficult.

Trust is always contextual, and the context must be valid. It is therefore important to understand the conditions that indicate trust.

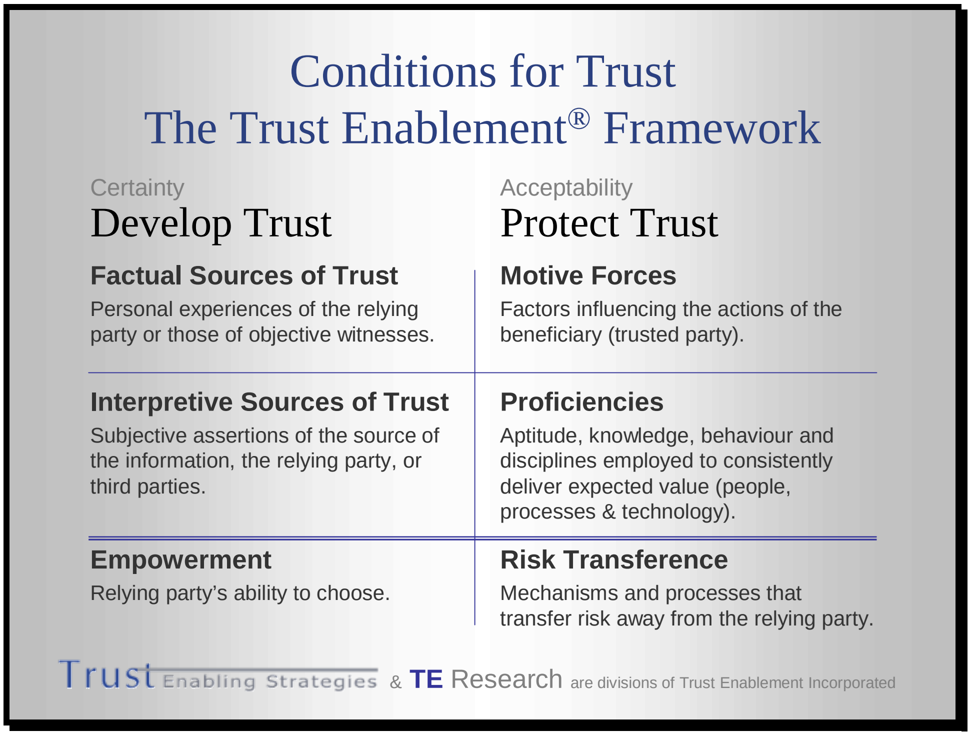
Conditions

To fully attribute investor behaviour to trust, management needs to examine all indicators of trust. Understanding the dynamics of the factors affecting trust, business will get valid answers to questions like, *"How is it that some issuers enjoy relatively stable share prices, despite experiencing setbacks, while others' oscillate nervously with every disclosure?"* or *"Why is it that eBay still traded at 143 P/E, as of June 20, 2002, or 420% of the industry average [[xvi]]?"*

Multiple conditions indicate trust.

The Trust Enablement® Framework was introduced in Part I of this paper, published separately. The principles are reviewed below to clarify the role of trust for the investment sector.

The Trust Enablement® Framework – a brief review



The Trust Enablement® Framework is based on a formulaic definition of trust, developed in Part I of this paper:

Trust = Acceptable Uncertainty

The framework is divided in half. Vertically, the Framework is organized according to conditions that indicate *certainty* (reducing and accepting risk) and contribute to *developing trust*, and conditions that indicate *acceptability* (mitigating risk) and contribute to *protecting trust.* Horizontally, the Framework classifies indicators according to how they contribute to attaining each of these two primary trust objectives. The top row, *Factual Sources of Trust* [[xvii]] and *Motive Forces*, indicate high, durable trust, while the second row

Trust reduces risk.

represents indicators for fast, transactional trust. The bottom row indicates trust remedies when trust is lost or deficient.

Applying The Trust Enablement® Framework to Indicate Trust

Going back to our "dot-com" example, the Trust Enablement® Framework provides insights into why high levels of investor trust, based on *Factual* and *Interpretive Sources of Trust*, evaporated at the first signs of fellow investors jumping off the bandwagon. There was virtually nothing on the right side of the Framework to *protect* from this erosion of trust; there were no earnings to justify share prices. Similarly, today, U.S. capital markets are skittish in the wake of a market correction down from record highs, precipitated by massive defaults on sub-prime loans. Can investors trust today's price/earnings ratios to be appropriate and sustainable, even though they are 35% lower now than they were in 2000?

This time, earnings have been strong, at least in a couple of broadly defined sectors (financial services, and energy, utilities and materials) [[xviii]]. A Trust Enablement® assessment can reveal the factors that influence how analysts make their projections and what conditions validate investor trust.

Assessing Investor Trust in the Economy

The Trust Enablement® Framework can be used to examine conditions for investor trust. For example (for illustrative purposes only):

- market volatility (*factual* source of trust) suggests an erosion of trust;
- tentative analysts reports (*interpretive* sources of trust) contribute to the distrust; extraordinary and disproportionate historical

earnings (*proficiencies*) in only a couple of sectors suggests they may neither be real nor sustainable;

- the *motive forces* driving business and economic policy in today's uncertain climate, for a variety of political and economic reasons, may be overly short-term focused;
- safe harbours to protect against capital erosion (such as money markets, real estate, utilities and natural resources) may not feel safe enough to underpin a recovery; and
- investors' ability to mount a recovery by choosing among investment alternatives in the domestic market may be limited to only one or two other high-performing, but relatively immaterial sectors, such as media.

A Trust Enablement® assessment indicates low trust in the value of U. S. capital markets.

This simplified, hypothetical Trust Enablement® assessment indicates low (insufficient basis for) trust in the continued performance of U.S. capital markets, and unless conditions for trust improve, does not portend well for the future. In Canada, by contrast, long-term commitments (*motive forces*) to massive capital investment in oil sands development (*proficiencies*) might indicate market and economic resilience.

Predicting the Future

Of course, the Trust Enablement® Framework is not a crystal ball. It analyzes known factors that influence trust. Although the Framework does provide leading indicators about likely effects on trust, the past is not a reliable indicator of the future. The future is unpredictable. Unexpected, external factors, such as terrorists crashing a commercial jetliner into the World Trade Center and the effects of a possible tsunami flooding a major commercial center such as Manhattan or London pose grave consequences for world economies. Similarly, a discovery of vast, economically accessible oil and gas reserves in the international waters of the Arctic could not only reduce prices, but also divert investment away from Canada's oil sands development and threaten Canada's economic prosperity. Sudden peace in the Middle East could cause the U.S. military and aerospace economic engine to grind to a halt and divert public attention to U.S. government debt. Disruptive and unpredictable changes often destabilize existing value production and open new investment opportunities. These disruptors have the most profound and long-lasting impact on economies - which rational investors can bank on (trust).

You can't trust the future - most of the time.

Global climate change is a good case in point. It is predictable. Current warming trends will continue. Popular opinion and public policy will drive investment in productive resources that mitigate this trend and its impact. For investors, the risk is minimal that current trends will reverse in the foreseeable future.

Effects of Altered Conditions for Trust

Nevertheless, the Trust Enablement® Framework can help issuers, regulators and market makers adjust the levers that alter conditions for trust. Using the Framework, management can identify specific trust objectives and then gauge whether they can be attributed directly to trust.

For example, a few years after Sarbanes-Oxley (SOX) legislation was implemented in the U.S., capital markets and public trust in corporations rebounded to all-time highs, as did trust in industry analysts' reports, but not necessarily in business leaders [[xix]].

Sarbanes-Oxley regulations don't deserve glory for new trust highs.

Our Trust Enablement® Framework was used to assess the SOX provisions in the Trust Indicators for Rebuilding Trust in Capital Markets section below. The assessment indicates that SOX creates conditions for "*fast trust*" and *protection* from future erosion of trust. However, it does not indicate rapid restoration of trust, and certainly not to new highs. Nor does it indicate, given the credibility loss suffered by business leaders, that certification of financial statements and internal controls by CFOs would be effective in developing "*fast trust.*" If valid, these predictors suggest that SOX may not deserve all the credit for the apparent trust highs indicated by studies and market valuations.

Monitoring Investor Use of Trust Enablers™ to Indicate Trust

Observers of investor due diligence can use the Trust Enablement® Framework to guide how they monitor and analyze investor behavior.

Trust Enablers™ are the Framework's mechanisms and instruments that create conditions for trust.

Usage patterns provide an additional and distinct trust indicator. For example, it is not trust but blind faith that motivates an investor to forgo due diligence, pass up *factual* and *interpretive sources of trust*, and rely on only one credit rating agency as a trustworthy source for valuing commercial paper.

Investors indicate trust by using - or not using - tools and resources that build confidence.

Trust deficiencies can be uncovered by an extensive use of tools that assess the relative performance of analysts. Also, observations that investors are *transferring risk* by hedging and selling short may indicate an erosion of trust. And investor activism promoting new laws and regulations (*motive forces*) would signal distrust (lack of confidence) in the future, such as with Sarbanes-Oxley legislation.

In summary, three complementary approaches can be used to measuring trust indicators: 1) Assertions of investors, such as through a questionnaire; 2) Actions associated with investor trust and distrust; and 3) Conditions known to influence investor trust and how investors rely on them. The third approach helps to both attribute trust to actions and identify trust requirements that further indicate the current state of trust. The Trust Enablement® Framework is used to classify conditions for investor trust according to their impact on trust perceptions and attribute investor actions more directly to trust, thereby making actions a more reliable indicator of trust.

Conditions for trust indicate levels of trust.

Armed with this knowledge, issuers and policy makers can devise new, more precise measurement tools for trust that rely less on survey biases. They can also adopt trust-optimizing practices that positively influence investor actions. The remainder of this paper applies the Trust Enablement® Framework to analyze *conditions for trust* in several case studies that indicate trust gaps and highlight opportunities for improvement.

Part II: Measuring Trust Indicators for Investors

Part I (in a separate document) examined ways to measure trust indicators for *customers*. Part II examines the similarities and differences of trust indicators for *investors*.

Applying the *conditions for trust* approach, based on the Trust Enablement® Framework, this section examines how trust indicators at a macroeconomic level contribute to rebuilding trust in capital markets. Investors are then grouped according to their investment preferences to determine the trust indicators that most impact their confidence levels. Finally, several *priority trust indicators* for institutional investors are examined using the same approach.

The Trust Enablement® Framework is used to measure and compare conditions that indicate trust.

The Trust Enablement® Framework classifies the conditions that affect trust in relation to how these conditions enable trust.

Indicators for Investor Trust & Confidence in Capital Markets

Our analysis of trust indicators begins with a macroeconomic perspective of investor confidence.

In *The Wealth of Nations* (1776), Adam Smith wrote that wealth is measured by the creation and consumption of goods and services, not by stockpiling them. It is the ebb and flow, not the accumulation of money that determines wealth [xx]. In fact, Gross Domestic Product (GDP) measures the size of an economy based on the flow of expenditures.

It stands to reason that if increasing this flow of transactions builds wealth, then the trust and confidence that promote the flow of transactions are key ingredients for wealth. In

Trust: The Social Virtues and the Creation of Prosperity (1995), author Francis Fukuyama writes, "*Social capital and the proclivity for spontaneous sociability have important economic consequences.*" In other words, economic prosperity depends on people being able to trust strangers in order to increase transaction flows. In *Trusting and Non-Trusting*, a 1999 paper by Boston University Professor Tamar Frankel, she wrote, "*Americans have expanded institutions to introduce trusting among total strangers located far apart.*"

Prosperity depends on institutions that enable strangers to trust each other.

Specifically, U.S. Federal Reserve Board Chairman Allan Greenspan told Congress, "*Our market system depends critically on trust -- trust in the word of our colleagues and trust in the word of those with whom we do business…. Lawyers, internal and external auditors, corporate boards, Wall Street security analysts, rating agencies, and large institutional holders of stock all failed for one reason or another to detect and blow the whistle on those who breached the level of trust essential to well-functioning markets*."

Legislators responded with sweeping new legislation to restore public trust and investor confidence in the institutions that were threatening the foundations of American capitalism.

Trust Indicators for Rebuilding Trust in Capital Markets

The start of the 21st century was marked by a crisis of trust in capital markets. After experiencing the back-to-back stock market shocks of the collapse of the dotcom boom and the governance scandals of numerous corporate institutions, such as Enron, investors became uncertain.

Many recommendations were made to restore trust. Only some were enacted. However, neither the proposed nor the enacted trust indicators were based on a framework to optimize the rebuilding of investor trust.

Part II: Measuring Trust Indicators for Investors

This section examines trust indicators for investors at a macro level -- public trust in capital markets and investors at large. It demonstrates use of the Trust Enablement® Framework to measure and compare the popular recommendations made in the media for restoring trust in capital markets with those enacted by Sarbanes-Oxley legislation.

Neither media recommendations nor SOX legislation were guided by a trust and confidence framework.

Trust Indicators in Sarbanes-Oxley

The stated purpose of Sarbanes-Oxley legislation (SOX) is "To protect investors by improving the accuracy and reliability of corporate disclosures made pursuant to the securities laws, and for other purposes." It is interesting to note that it is intended to be a defensive measure that provides additional protection to investors, not to proactively restore trust in capital markets.

Approach

A simple approach to measuring trust indicators is to group them according to the categories provided by the Trust Enablement® Framework, then simply add up the number of indicators found under each heading. The most populous groupings indicate a bias toward a specific trust objective. This simple method is used to illustrate versatility and effectiveness of the Trust

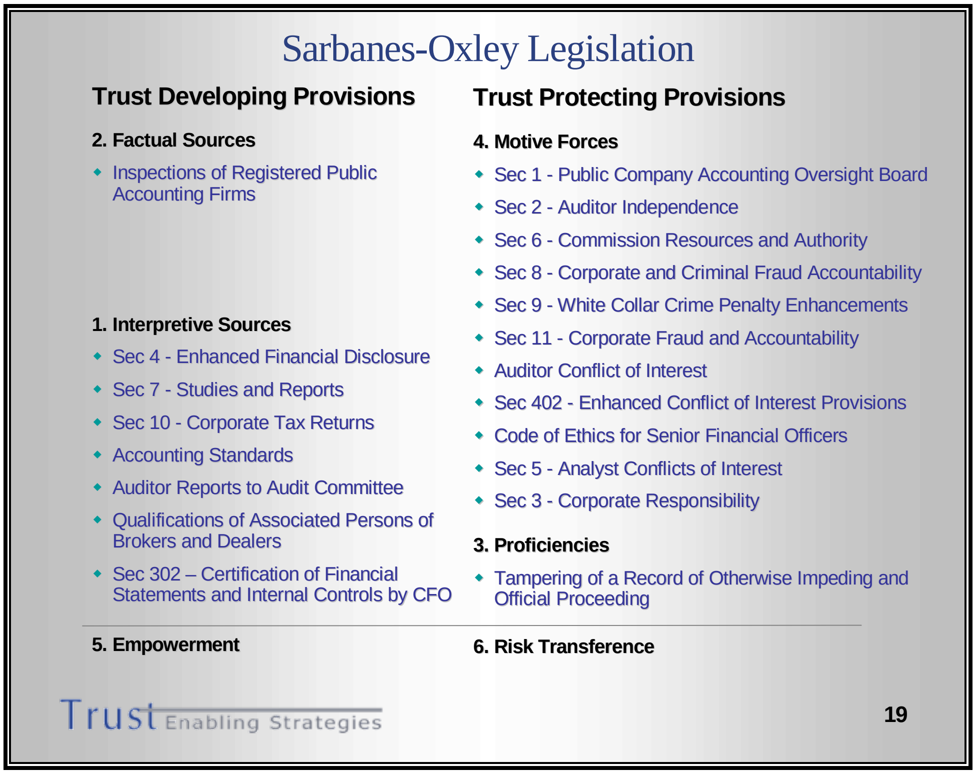
A simple measure of trust is the relative sum of the indicators allocated to each category of the Trust Enablement® Framework.

Enablement® Framework throughout the paper.

More sophisticated approaches would apply a weighting to certain indicators, depending on their relative importance or how they contribute to a trust objective. For example, an indicator that has an emotional impact on the investor may be weighted more than one that appeals to their rational cognition. Similarly, CFO and CEO certification of financial statements and internal controls may get one point toward developing trust, while low public trust in business leaders may justify taking half a point away from the score.

Findings

The Trust Enablement® assessment of provisions found in Sarbanes-Oxley legislation (SOX) reveals largest grouping in the *Motive Forces* category. There is also some concentration of provisions under *Interpretive Sources* [[xxi]]. Also notable are the categories that are virtually unaddressed by SOX.



Conclusions

A high-level Trust Enablement® Assessment of the Sarbanes-Oxley Act (SOX) reveals predominant emphasis on provisions in the *Motive Forces* category that serves to protect from long-term loss of trust, which is consistent with its stated purpose. The Act also introduces a few mechanisms in the *Interpretive Sources of Trust* category that serve to establish *fast trust*. It reveals predominantly a risk management approach (protecting from further erosion of trust) to building trust and confidence in capital markets. It primarily indicates less long-term erosion of trust.

SOX is rooted in risk management thinking.

Trust Indicators in Media Recommendations

A Trust Enablement® assessment was made of media-reported recommendations for restoring confidence in capital markets reveals greater emphasis on *developing* trust than was found by analyzing SOX provisions.

Findings

Media recommendations develop trust.

In contrast with SOX, the recommendations cover more categories of the framework in a more balanced manner. There is slightly more emphasis on *developing* trust than protecting it. It also addresses the need to compensate for trust deficiencies with recommendation in the *Risk Transference* category.

Conclusions

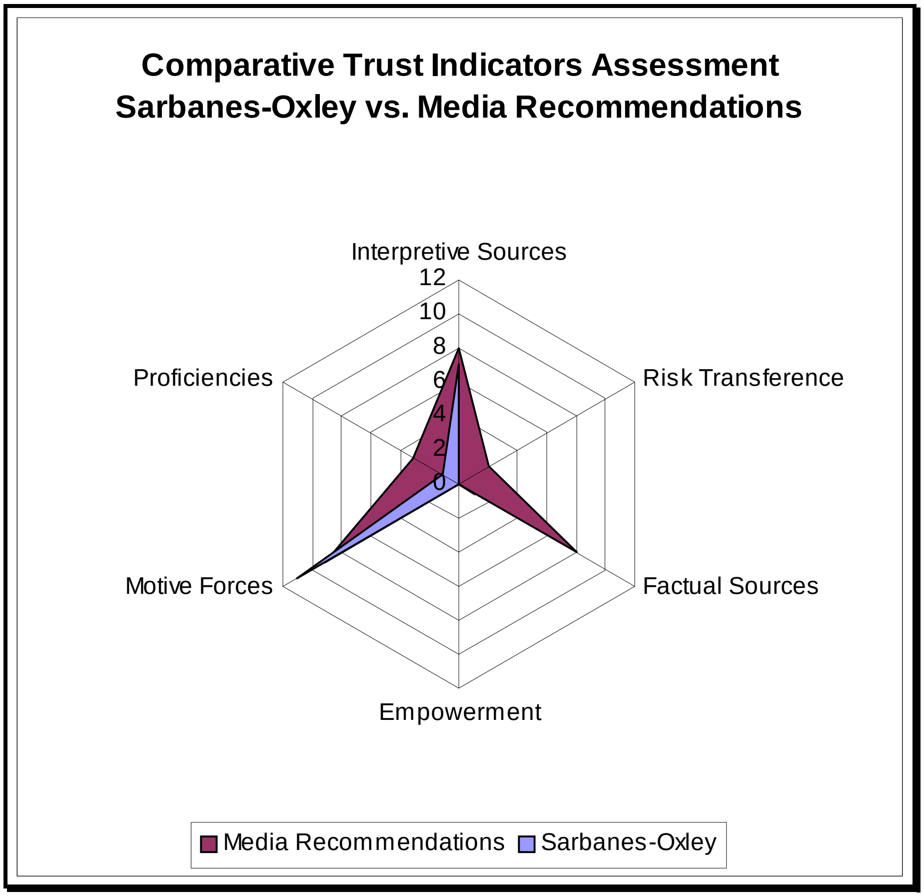
The assessment findings indicate a trust-oriented approach to investor confidence, with emphasis on leveraging more *Interpretive* and *Factual Sources of Trust* that help to develop high trust. The recommendations in the *Risk Transference* category also address the need to maintain a flow of investment transactions during the period of low trust as a foundation for accelerating the process of rebuilding trust.

Media recommendations compensate for lost trust.

Comparing Trust Indicators

The following chart superimposes the trust indicator measurements of Sarbanes-Oxley over aggregated popular opinions for restoring trust in capital markets.

Charting the categories for trust indicators from the Trust Enablement® Framework, provides a rough, high-level comparison of the nature of the two approaches for restoring trust and confidence in capital markets. Trust indicators that initially appear to be unrelated, and therefore not comparable, become both measurable and comparable when viewed through the lens of the Trust Enablement® Framework.



Recognizing that in many ways this is a comparison of apples and oranges, it is still possible to compare their characteristics (analogous to colour, texture, size, weight, sugar content, flavour, nutritional value, etc. in a recipe) especially when their purpose is similar (i.e. food for dessert). In our case the comparison is between two approaches to restoring confidence in capital markets.

Media recommendations address investor trust and confidence comprehensively.

Top three findings revealed by the chart:

1. Popular Recommendations provided a more comprehensive suite of trust indicators;
2. Popular Recommendations provide more trust indicators for *developing high trust*; and
3. Popular Recommendations provide more trust indicators to *transfer risk*, which helps to rebuild lost trust.

This comparative analysis suggests that regulators and industry coalitions could have done considerably more to rebuild trust in capital markets than was provided by SOX legislation.

Note that although this analysis demonstrates how trust indicators are both measurable and comparable, it says nothing about the validity of the information supported by the trust indicators (i.e. do we trust the information we need?). Measuring trust indicators alone is therefore not sufficient to conclude that one approach is more effective than another. To conclude about effectiveness, trust indicators need to be compared for reliance on comparable information used for similar purposes.

The examples above show that it is possible to discern the extent to which a set of conditions contributes to achieving specific trust objectives. These can be quantified with various levels of sophistication and then compared using common measurement criteria, as specified by the Trust Enablement® Framework.

The Trust Enablement® Framework makes trust indicators comparable.

Priority Trust Indicators for Investors

The previous example analyzed a generic macroeconomic scenario. Although the economy generally has a significant impact on most investments, investors have more power to choose between specific investments. To gain further insights into the indicators investors need to attain and maintain trust in their target investments, we need to consider both the investors' investment preferences and the process they use to make investment decisions.

The objective is to discern *priority trust indicators* for various kinds of investments in order to focus on the trust indicators that warrant measurement and analysis. In order to provide investors with indicators that optimize trust, issuers must understand the needs of their target investors.

As the following examples show, some investors rely more on technical analysis than fundamentals, many speculate on market momentums, while others prefer to hold their positions for a long time.

Trust Indicators Used Through the Investment Process

Investors are just like any customer, except that they try to buy appreciating assets. Investors go through the same general purchasing cycle as any customer does. Their investment purchases follow a standard transaction lifecycle -- moving from discovery to negotiation and order, to fulfillment, settlement and compliance, as discussed in Part I, Stages of Customer Purchase. At each step, investors' trust requirements change, just as they do for any customer. What differs is the nature of the information they rely on in each phase

Investors' requirements for trust indicators change as they step through their investment decision and purchase processes.

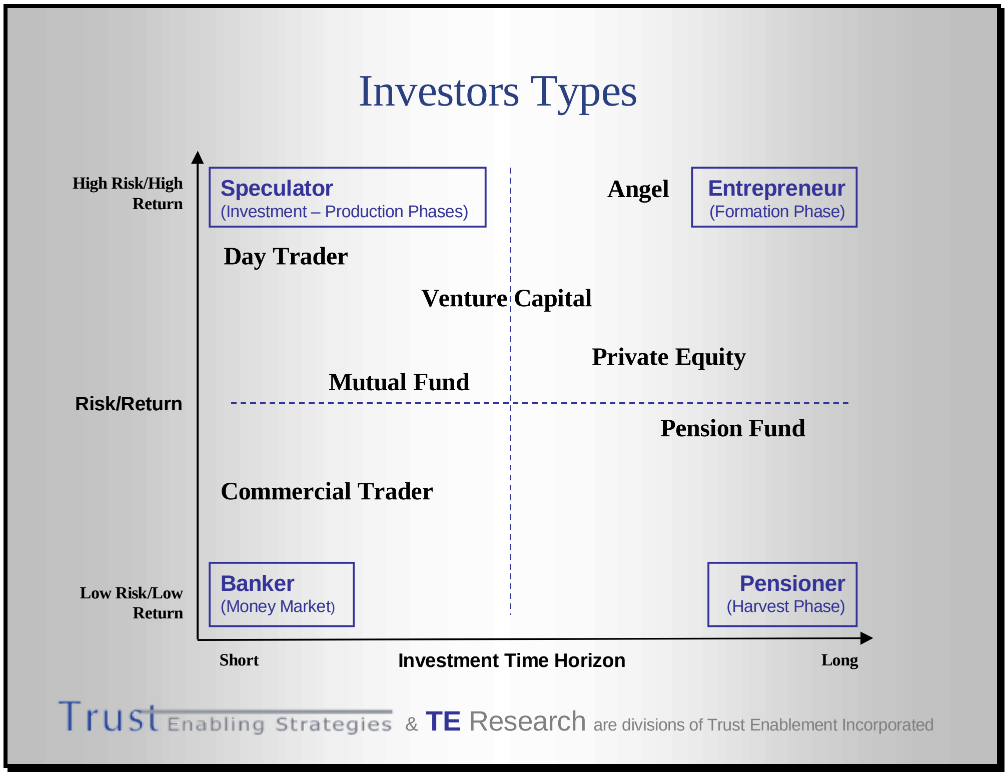
of the transaction, and the trust indicators they use to attain and maintain trust in that information taking the next step toward completing the transaction.

Investor Types

Investors are a diverse group. Although they all seek a satisfactory return on their investments, they have very different perceptions about what it means to be an investor and what return on investment would be satisfactory. They range from institutional investors -- such as pension funds, which invest in stable “blue chip” companies that can be relied upon to deliver a consistent return -- to day-trading speculators who buy and sell shares on momentum, and whose idea of a satisfactory return on investment is a similar to that of winning the jackpot in a lottery. Other investors include company founders, angel investors, venture capitalists, stockbrokers, mutual funds and hedge funds, to name the most common categories. Each have a distinct set of investment requirements, which makes it misleading to generalize.

Investors’ needs differ.

One way to group investors is according to their investment-time horizon and risk/return profile.



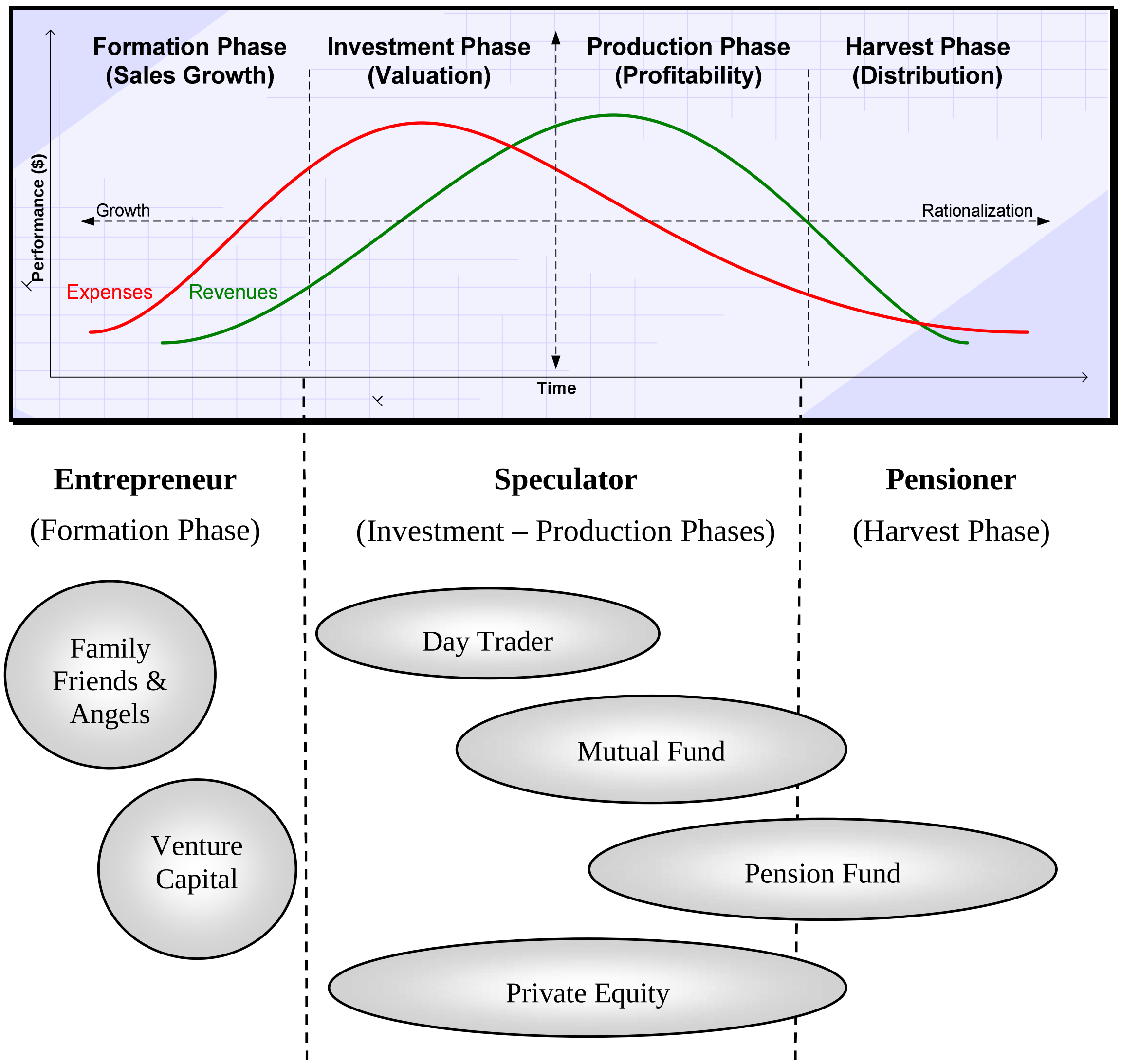
Investors can be classified according to the extent to which their investment styles fit four archetypal investor profiles: Speculators, Entrepreneurs, Pensioners and Bankers. Speculators and Entrepreneurs willingly accept high risks to achieve extraordinary returns. The former treat investments like commodities, buying and selling on momentum, while for the latter each investment is a life's commitment. Bankers and Pensioners are more risk-averse, satisfied with modest returns in order to safeguard their money. The former consists of people temporarily parking their money before reapplying it to business operations, while the latter seeks to protect their assets from eroding within an economic cycle.

Each type of investor also prefers distinct types of investment vehicles. Speculators and Entrepreneurs invest almost exclusively in equity securities, while Bankers and Pensioners tend to invest, at least in part, in debt, annuity and money market securities. Most investors are a hybrid of two or three archetypes, tending to lean more toward one of the archetypes, rather than being defined by it. Each of the equity investors prefers to invest in the securities of distinct types of issuers.

Archetypes define investors' requirements.

Equity Investors

Issuer can be classified according to their stage of maturity within a typical corporate lifecycle, from start-up to end of life. Companies in the Formation and Investment phases of the lifecycle are growth-oriented, while those in the Production and Harvest phases are rationalization-oriented.



Equity investors, based on their archetypal leanings, tend to invest in issuers at different stages in a corporate lifecycle. Knowing investors' preferences provides insights into the criteria they consider most important when making investment decisions. These, in turn, define their *priority trust indicators* that warrant measurement and analysis.

Investment Types

The objective of this and the following section is to determine the trust indicators that are most meaningful when investors purchase different kinds of investments to expedite the transaction. Issuers can use this information to strategically allocate resources of their trust optimization programs toward developing investors' trust and confidence in the areas that matter most when investing.

The previous sections distinguished between types of investors according to their investment preferences. The analysis found that these types tend to invest in issuers at different stages in the company's life.

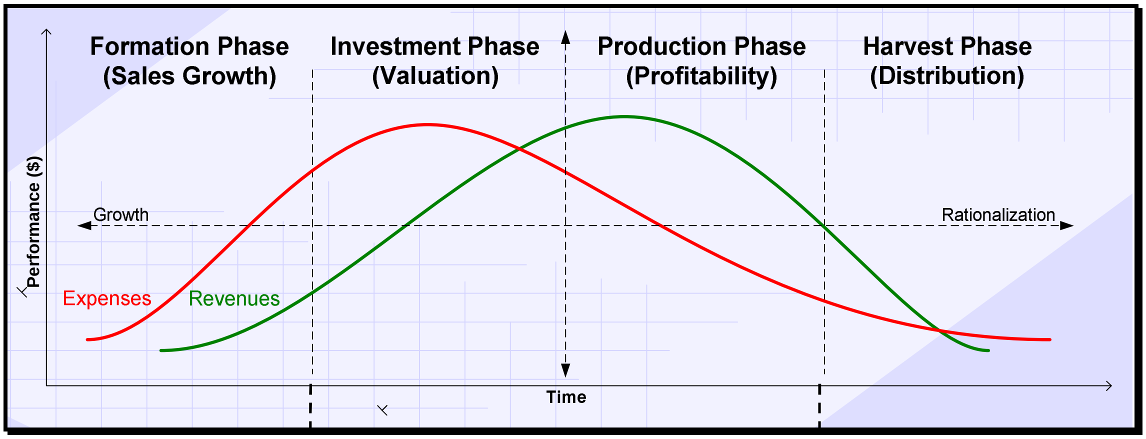
Investment characteristics determine the critical trust indicators investors need to make investment decisions.

This section organizes investment preferences using the same classifications used for customers in Part I of this paper, which will keep the labelling consistent and so that the same *priority trust indicators* can be applied with each associated generic purchase type to each kind of investments.

It may surprise some that investments can be classified generically for their *priority trust indicators*. As our examples below show, investments can be broadly classified according to a generic purchase classification system to determining the strategic trust indicators that most need to be satisfied to expedite a purchase. To recap, the nature of generic customer purchases were defined broadly using seven categories:

Generic Purchase Classification	Generic Purchase Description	Investment Description
A. **RISK PROFILE**	customer's preconceived perceptions about purchase	investor's investment style
B. **COMMODITY**	known, quantifiable and easily substitutable product	investments made based on technical analysis
C. **MAJOR**	sizeable purchase relative to total budget	consequential investments relative to total budget
D. **COMPLEX**	feature/function complexity	investments based on fundamentals, requiring expert analysis
E. **INTANGIBLE**	unknown or non-standardized value determination	investments in unproven issuers
F. **COMMITTED**	long-term commitment	long-term or illiquid investments
G. **SPECULATIVE**	starting with a negative perception	investments in a "bear" market

These generic purchases categories can now be associated with investors' preferences for issuers at particular stages in their maturity lifecycle. B. COMMODITY through F. COMMITTED are most relevant classifications for this analysis.



Investments that are liquid and largely undifferentiated (such as income trusts) and/or technical analysis oriented investors (in other words buy and sell on value and momentum) define commodities. Commodity investments make a clear promise either explicitly or based on track record or market trend (extrinsic factors belong to the *Interpretive* category). They *transfer risk* by guaranteeing a yield or limiting the duration of their holdings. Both FUND managers and DAY TRADERS purchase investment commodities.

B. COMMODITY

Factual	Motive Forces
Interpretive	Proficiencies
Empowerment	**Risk Transference**

Investors making a consequential financial commitment, such as VENTURE CAPITALISTS, apply considerable due diligence and closely monitor performance (*factual* sources of trust).

C. MAJOR

Factual	Motive Forces
Interpretive	Proficiencies
Empowerment	Risk Transference

Portfolio investors, such as MUTUAL FUNDS, rely on sophisticated analysis (*interpretive* sources of trust) about the performance of the issuer (*proficiencies*) when determining portfolio fit.

D. COMPLEX

Factual	Motive Forces
Interpretive	**Proficiencies**
Empowerment	Risk Transference

FAMILY & FRIENDS are often the first investors in an entrepreneurial venture. They invest more for social than financial reasons. Nevertheless, they need to see, feel, experience (*intrinsic* sources of trust) and intimately understand the entrepreneurial offerings. These investors rely mostly on the value of the reputation of the entrepreneur in the community to *transfer risk*.

E. INTANGIBLE

Factual	Motive Forces
Interpretive	Proficiencies
Empowerment	**Risk Transference**

Long-term, committed investors, such as PENSION FUNDS and MUTUAL FUNDS, need to know how management decisions will be made over time (*motive forces*). They need therefore to either trust the board of directors or control it.

F. COMMITTED

Factual	**Motive Forces**
Interpretive	Proficiencies
Empowerment	Risk Transference

These insights about the *priority trust indicators* for various kinds of investors allow issuers to focus on measuring and analyzing the trust indicators that matter most to their investors.

Institutional investors need to trust the *motive forces* of the issuer.

For illustrative purposes, to demonstrate how issuers can measure the most meaningful trust indicators for their investors, the remainder of this paper examines trust indicators for F. COMMITTED investment purchases, namely those made by institutional investors, such as pension funds and mutual funds. The focus is on *developing* and *protecting* sufficient trust in the issuer's *motive forces* to secure long-term commitments to large securities holdings.

Priority Trust Indicators for Committed (Institutional) Investors

Investors making long-term commitments to holding securities have distinct trust requirements. They are primarily concerned with sustainable performance. They therefore seek to attain high levels of trust in the decision-making criteria of an issuer's board of directors and management. The composition of the board and management, and the issuer's corporate governance practices all play in an important role in assuring institutional investors about the consistency with which strategic business decisions will be made for the duration of their investment position.

Institutional investors look for trust indicators about the issuer's sustainability.

The role of institutional investors is primarily to serve the interests of individual investors, whose money is being invested. Trust consideration must therefore begin with the relationship between the originating investor and the investing institution. This chain of trust must be maintained by the issuer's board of directors and handed down to management.

Institutional investors must maintain an optimized chain of trust from the individual investor through the issuer's board of directors, to management.

This section of the paper examines various ways that trust is found and can be measured in the *motive forces* influencing the issuer's strategic decision-making. It begins with a look at how recommendations to improve the demand-side of the investment sector contribute to investor trust. The focus then turns to how corporate governance practices indicate investor trust and contribute to various aspects of business performance.

The first example illustrates how policy makers can use the Trust Enablement® Framework to optimize conditions for trust on the demand-side of capital markets, which will improve investor confidence and increase the volume, velocity and value of investment purchases. Subsequent examples show how the Trust Enablement® Framework can be used by issuers to improve corporate governance practices to fulfill the fiduciary duties of directors and officers, reduce liability exposures and improve business performance. Investors can apply the same criteria to assess the quality of the issuer's corporate governance practices to assess risk and determine their confidence levels in the sustainability of the issuer's performance.

Trust Indicators for Strengthening the Demand-Side

The first consideration is to strengthen the effectiveness of the so-called "demand-side" [[xxii]], which consists of various intermediaries that act as monitors and gatekeepers. These include analysts, auditors, stock exchanges, lawyers, media and other institutions that create conditions for investor trust and confidence. To this end, it is important to align the *motive forces* of investors with those of intermediary funds that make specific investment purchases on behalf of investors. Some have advocated expanding the fiduciary duties of intermediaries to the individual investors to reinforce their trust relationship and move away from contractual obligations that presume mistrust [[xxiii]]. Examples of prospective initiatives, beyond the provisions of Sarbanes-Oxley legislation, are presented in Table 1 [[xxiv]].

Fiduciary relationships are founded on trust and contractual relationships on mistrust.

[Table 1] **Examples of proposed Trust Enablement® Initiatives**

	Develop Trust	Protect Trust
INVESTORS	**Factual Sources of Trust** • Investigations by business school students • Reports by the media • Monitors at a distance, for objectivity, but lower quality information • Market trading professionals, as they are not susceptible to 'capture': o Arbitrageurs o Researchers o Brokers o Portfolio managers o Hedge fund managers	**Motive Forces** • A Board culture that challenges common beliefs and customs, with a thirst for new information and new sources of trust • Tax code to encourage short-selling • Commodity Futures Modernization Act of 2000 • Government regulators and policy analysts that facilitate true objectivity among outside monitors
	Interpretive Sources of Trust • Tax accounting records • Monitors close to the company, for high quality information, at the expense of losing some objectivity	**Proficiencies**
	Empowerment • Choice of multiple rating agencies and other sources of trust	**Risk Transference** • Short-selling • Single stock futures contracts

The above Trust Enablement® assessment of the proposals for restore trust in capital markets by improving the demand-side finds an emphasis on *developing* *high trust* and compensating for *low trust*. It indicates that adoption of these measures would help to accelerate the process of recovering from low trust and developing high trust.

Corporate Governance

The Priority Trust Indicator for Institutional investors (the F. COMMITTED category) is the *Motive Forces* category in the Trust Enablement® Framework. *Motive forces* protect trust in the long term by helping relying parties to anticipate how the organization can be expected to make decisions in the future. Good corporate governance represents the primary trust indicator used by institutional investors to indicate trust in the issuer's *motive forces*.

Trust is at the core of good corporate governance.

Trust is the core of good corporate governance [xxv]; shareholders must trust that the board of directors will exercise their fiduciary duties of *care* and *loyalty* [xxvi] to the corporation when monitoring, ratifying and sanctioning (reward and punishment) [xxvii] management (the agents of shareholders) decisions.

As well, directors must trust that corporate officers are managing the affairs of the corporation competently and with integrity [xxviii]. Investor confidence in capital markets depends on the soundness of this chain of trust. The sole measure and the definition of good corporate governance' [xxix] should be the level of trust and confidence shareholder**s** have in the board's effectiveness to develop and protect this chain of trust. Recent evidence suggests that good corporate governance is correlated positively with financial performance [xxx].

If good corporate governance is a primary trust indicator for *motive forces*, then what are the trust indicators for good corporate governance?

Trust Indicators for Good Corporate Governance

How do investors establish trust and confidence in a board's ability to execute its fiduciary duties of care and loyalty? There are two parts to the answer:

1. Directors must be loyal [[xxxi]] and exercise care when executing their duties;
2. Shareholders must have evidence of the board's loyalty and care.

Table 2 (below) outlines, in general terms, how these objectives are accomplished using the Trust Enablement® approach.

[Table 2] **Trust Enablement® - General Considerations**	
2. Develop Trust	**1. Protect Trust**
Factual Sources of Trust ***Objective Evidence*** (personal observation by shareholders, independent witnesses/monitors, recording and tracking devices, transparency, etc.)	**Motive Forces** ***Loyalty*** (laws, regulations, standards, by-laws, policies, culture, affinities, ethics, obligations, rewards, penalties, policing, recourse, self-esteem, personal power, wants/needs, personal mission/objectives, etc.)
Interpretive Sources of Trust ***Subjective Evidence*** (corporate/board self-assertions/statements and reports, fiduciaries' representations, corporate brand, board members' credentials and reputations, testimonials, certifications, analysts' opinions, ratings, audit reports, analysts' recommendations, proxies, honesty, etc.)	**Proficiencies** ***Care*** (general and specific knowledge, experience, cognitive and physical capacity, skills, time, resources, access, procedures, controls, technology, integrity, satisfaction, etc.)
Empowerment Choice and aggregation from alternative *interpretive* and *factual sources of trust* (evaluation of analysts' performance, director elections, etc.)	**Risk Transference** Liability limits, reduced share prices, incentives, guarantees, warranties, insurance, selling short, contracts, accountability, etc.

The first criterion is satisfied with provisions in the *Motive Forces* and *Proficiencies* categories on the *Protect Trust* side of the Framework. The second criterion is addressed by the *Factual Sources of Trust* and *Interpretive Sources of Trust* categories on the *Develop Trust* side of the Framework.

The *Empowerment* and *Risk Transference* categories on the bottom row of the framework are used to compensate for deficiencies in the previous categories, as in when there is insufficient trust in the loyalty and care of directors and officers.

A Trust Enablement® assessment provides investors with a trust indicator about the quality of an issuer's corporate governance practices.

This example suggests that, at least conceptually, the Trust Enablement® Framework can be used to analyze the effectiveness of corporate governance practices. The presence of a comprehensive suite of conditions for trust in each of the categories of the Framework would indicate higher levels of investor trust in the issuer's board of directors and their governance practices. An uneven distribution pattern would indicate a diminished basis for investor trust and therefore likely lower levels of trust.

Since optimizing trust is the essence of good corporate governance, Boards of Directors should do more to build shareholder and stakeholder [[xxxii]] trust and confidence. This responsibility may belong to Governance Committees, since they are responsible for board effectiveness, and ensuring that directors and officers comply with their fiduciary duties. Trust considerations can be codified in trust-enabling principles, policies and governance practices to parallel those for risk management.

The next case study uses this approach to determine trust indicators of an issuer's governance principles.

Indicating Trust from Corporate Governance Principles

The same frameworks are useful for assessing the extent to which existing corporate governance practices contribute to attaining these trust objectives. For illustrative purposes only, Table 3 applies the Trust Enablement™ Framework to assessing the *Corporate Governance Principles of Pfizer Inc*. [[xxxiii]]

[Table 3] **Trust Enablement™ Assessment**

Corporate Governance Principles of Pfizer Inc.

	Develop Trust	Protect Trust
SHAREHOLDERS	**Experiential Sources of Trust** • The Chairman and CEO is responsible for establishing effective communications with the Company's stakeholder groups (i.e. shareholders, customers, company associates, communities, suppliers, creditors, governments, and corporate partners) • Directors may meet with shareholders directly, but mostly when accompanied by management	**Motive Forces** **All Directors:** • The Chairman of the Board and the Chief Executive Officer roles are held by the same person • The Executive Committee and Science and Technology Committee may be composed of dependent directors • When a Director's principle occupation changes substantially, must tender resignation • All Directors are expected to own stock in the company, in an amount that is appropriate for them, and they will receive part of their compensation in Stock Units, which they must hold for the entire duration of their service to the Board • The Board, and each committee, is required to conduct a performance self-evaluation at least annually **Outside Directors:** • Outside directors approve the Chairman & CEO's short-term and long-term goals, and evaluate his/her performance against those goals **Independent Directors:** • The Board consists of a majority of independent Directors • Directors are selected for their independence, and diversity of experience • The Audit Committee, Compensation Committee, and Corporate Governance Committee are composed of independent Directors
	Authoritative Sources of Trust • Management speaks for the Company • The Board of Directors recommend desirable board member candidates	**Ability** • Directors should not serve on more than four other boards • Directors are selected for their leadership ability to exercise sound judgement, and specific scientific experience, as well as prior government service, and familiarity with national and international issues affecting the business • Directors receive full orientation and continuing education **[DIRECTORS view omitted]**
	Empowerment • Shareholders elect members to the Board of Directors	**Risk Transference** • [unaddressed]

The Trust Enablement™ assessment in Table 3 indicates an expectation by Pfizer's Board of Directors that shareholders rely almost exclusively on corporate management as their source of trust in the efficacy with which directors and officers execute their fiduciary duties. It also illustrates how Pfizer's Corporate Governance Principles reflects a governance style that values control over trust for attaining required levels of shareholder confidence (as evidenced by the emphasis on *protecting* trust).

Pfizer's Corporate Governance Principles favour *control* over *trust*.

Governance Trust Indicators for Reducing Directors' and Officers' Liability Exposures

It stands to reason that increasing shareholder (and other stakeholder) trust [[xxxiv]] and confidence should improve shareholder attraction and retention rates, and enhance market performance. However, underwriters of Directors and Officers (D&O) Liability and Indemnification Insurance have been slow to recognize the value of trust. They still do not equate strong intermediary (or demand-side) monitoring systems to their metaphoric equivalent of monitored home alarm systems.

D&O insurance companies should reward trustworthy boards with lower premiums.

Homes with a monitored alarm system typically receive insurance discounts, but this is not the case for issuers who give shareholder (and other stakeholder) a richer suite of trust indicators. This continues to be the case, despite evidence that correlates distrust with market volatility [[xxxv]] and trust with improved business and share value performance [[xxxvi]].

Even so-called progressive insurance companies that take an individual “financial risk” or “quality of corporate governance” approach rather than a “portfolio risk” approach [[xxxvii]] give Boards of Directors and corporate officers few incentives to exceed regulatory standards. Table 4 provides an overview of the conditions that *develop* trust and reduce risks (rather than *protecting* trust to mitigate risks, which are therefore excluded from the table). The objective is to examine counterbalancing mechanisms to prevailing risk management approaches (and their control-oriented solutions) beyond those that D&O Liability Insurance companies typically assess when pricing policies [[xxxviii]].

[Table 4] **Trust Enablement® Assessment**

Directors & Officers Liability Insurance Criteria for Developing Shareholder Trust

SHAREHOLDERS

<table>
<tr><th>Develop Trust</th><th>Protect Trust</th></tr>
<tr><td>Factual Sources of Trust</td><td rowspan="2">Motive Forces

Trust Enablement® Assessment
Directors & Officers Liability Insurance Criteria for Developing Director's Trust

DIRECTORS
<table>
<tr><th>Develop Trust</th><th></th></tr>
<tr><td>Factual Sources of Trust
• Procedure for anonymous submission, receipt, and retention of complaints regarding accounting, internal accounting controls, or auditing matters [xliii]</td><td></td></tr>
<tr><td>Interpretive Sources of Trust
• Retention and use of external, independent advisors other than auditor [xliv]
• CEO and CFO certification of public company filings [xlv]
• The external auditor reports directly to the Audit committee [xlvi]</td><td></td></tr>
<tr><td>Empowerment
Board and all committees have full authority over use of outside advisors [xlvii]</td><td></td></tr>
</table>
</td></tr>
<tr><td>Interpretive Sources of Trust
• Corporate Management
• Published Code of Business Conduct and Ethics [xxxix]
• CEO and CFO certification of public company filings [xl]
• Reports on performance effectiveness of each committee of the board and method of evaluation [xli]
• Method for evaluating the performance of individual Board members [xlii]</td></tr>
<tr><td>Empowerment</td><td>Risk Transference</td></tr>
</table>

The example in Table 4 shows how corporate governance practices that are oriented toward regulatory compliance but intended for *developing* shareholder trust actually limit shareholder reliance almost exclusively to information provided by corporate management, and therefore may not be sufficient for building required levels of investor trust in the issuer's corporate governance practices (see endnote references in table). One exception to this is the formalized use of external auditors to attest to the accuracy of the corporation's historical financial performance.

Risk scores of progressive D&O insurance companies can be a valuable trust indicator for investors.

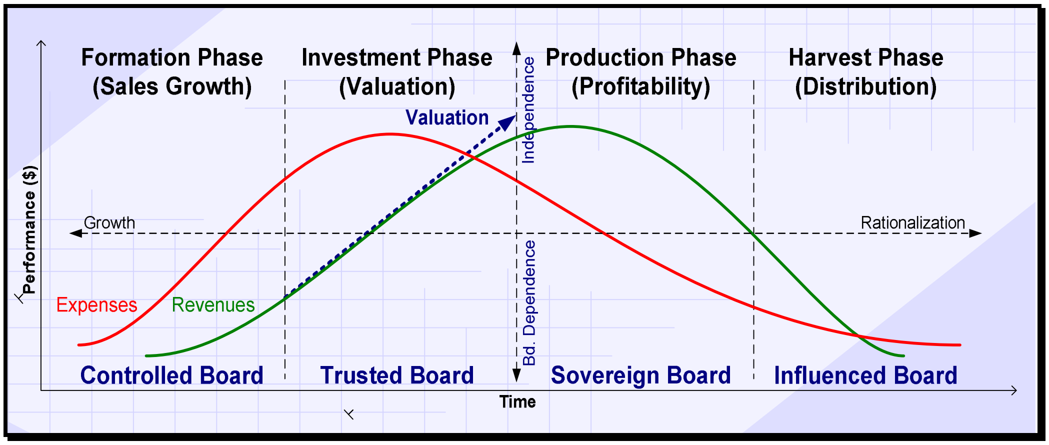
Institutional investors would be well served to use governance risk assessments from enlightened D&O insurance underwriters as an important trust indicator of *motive forces* and a means of averting the loss of trust when making long-term investment commitments to an issuer.

Trust Indicators for Governance Practices that Improve Business Performance

Although institutional shareholders need to manage the risks associated with their investments, their primary objective is to manage returns. Recent research that applied the Trust Enablement® Framework to corporate governance best practices

Good governance underpins superior business performance.

found specific governance styles to be associated with distinct measures of business performance [xlviii].



This diagram shows how different *governance styles* are associated with evolving business performance priorities through a typical corporate lifecycle:

- Management-controlled boards enjoy faster sales growth, which is typically a strategic priority for young companies in the Formation Phase of their corporate lifecycle;

- *Boards with practices that help establish investors and analyst trust are rewarded with higher share valuations*, which is typically a strategic priority for corporations preparing to raise capital on public markets and those seeking to leverage the value of their shares for mergers and acquisitions in the Investment Phase of their corporate lifecycle;

Trusted Boards enjoy higher valuations.

- Sovereign boards that are controlled by neither shareholders nor management preside over the most profitable companies – profit typically being a strategic priority for mature public companies in the Production Phase of their corporate lifecycle; and

- Outwardly, independent boards that are nevertheless influenced by management tend to distribute more cash to shareholders, which is typically a strategic priority for ripened companies in the Harvest Phase of their corporate lifecycle.

The *Trusted Board* style has seven out of eight governance best practices that contribute to *developing* trust. They include: the average options granted in the past three years as a percentage of basic shares outstanding did not exceed 3% - the option burn rate; Board members are elected annually; and the company either has no poison pill or a pill that was shareholder approved.

Investors can use *governance styles* as a distinct trust indicator of expected performance in two ways, by measuring the:

- strength of their Trusted Board style when seeking high share valuations; and
- trust indicators (both in governance and management practices) to optimize the value of relationships with the stakeholders strategic to their applicable lifecycle maturity phase (such as customers for companies in the Formation Phase).

Governance styles can indicate trust in various business performance measures.

Investor-Facing Applications for the Trust Enablement® Framework

How can issuers, regulators and investment institutions use the Trust Enablement® Framework? Here are a few examples:

- Regulators of capital markets can assess and refine their rules and regulations to optimize trust;
- Capital market facilitators, such as stock exchanges, can assess and optimize the conditions for trust provided by their instruments, tools and mechanisms that support the purchase and sale of securities;
- The governance committees of issuers' boards of directors can codify their commitment to shareholder (and other stakeholder) trust and confidence by using Trust Enablement® principles, policies and practices;
- Issuers' boards of directors can adopt governance styles that support strategic objectives and allocate resources to trust management programs to monitor and optimize conditions for trust around strategic stakeholders, such as investors;
- Institutional investors can incorporate trust analytics into their decision support tools, such as benchmarks of corporate governance styles associated with superior business performance;
- Directors' and Officers' Liability and Indemnity insurance providers can develop corporate governance evaluators and scoring systems that price policies based on conditions for shareholder (and other stakeholder) trust. They can also publish their results for investors to use as a trust indicator;
- Researchers and analysts can provide benchmarking reports for issuers' governance styles and trust indicators;

- Consultants can audit issuers' trust indicators and help their board and management optimize conditions for investor trust;
- Lawyers can incorporate trust-enabling provisions in contracts and more confidently begin to explore opportunities for their clients to benefit from fiduciary relationships.

Conclusions and Executive Summary

Trust can be indicated in a variety of ways. Most approaches, whether from survey responses or inferred from investor actions, produce uncertain results and are inadequate for refining trust indicators to optimize investor trust and confidence. As a result, trust could not be measured accurately. And from conventional wisdom, managers know that what cannot be measured cannot be managed. Hence, even though it is widely accepted that trust is not simply a virtue but an important driver of business performance, business managers have marginalized trust considerations.

Although universally acknowledged in concept, the term "trust" is only just beginning to be accepted into the mainstream lexicon of business. Still, terms such as accountability, integrity, ethics, transparency, satisfaction, relationships, honesty and loyalty are being used as proxies for trust. However, none of these management aspirations, either individually or in the aggregate, contributes to creating optimal conditions for trust.

The current prominence of risk management practices has been fuelled largely by regulatory compliance requirements. Although it has helped to shore up further erosion of trust, it has done little to enhance it. In fact, it can be argued that excessive risk management practices actually undermine trust, and the regulations that drive them increase transactions costs for business. It is not surprising, therefore, that risk management practitioners have found it challenging to make a strong business case for their management initiatives.

Similarly, a business case for trust can be based on the risk of business losses due to an erosion of trust. Fortunately, trust management initiatives can also be justified on the basis of business performance and competitive advantage, and the business case can be compelling [[xlix]] – provided that trust can be measured and tangible drivers for trust can be managed.

Part II: Measuring Trust Indicators for Investors

This paper, which began with P*art I: Measuring Trust Indicators for Customers* (in a separate document), introduces an approach that improves the accuracy of identifying and measuring factors that influence trust. This approach is subsequently applied to a variety of case studies that demonstrate its ability to guide measurement and comparison of trust indicators for customers and investors. It provides the critical, missing link between the business case for trust management and an executable Trust Enablement® strategy.

Trust and Confidence

The terms "trust" and "confidence" are not synonymous. Confidence is the ultimate objective that can be satisfied with "trust" or "control." Trust is the preferred approach, because it reduces transaction costs.

Effects of Trust and Mistrust

Trust provides the foundation for all economic activity. It drives prosperity by increasing the volume, velocity and value of commercial transactions, the sum of which defines a nation's Gross Domestic Product (GDP). In a capitalistic economy, wealth depends entirely on the generosity of self-interested individuals and businesses to willingly contribute their resources to others who need them to produce value. This cooperation is founded on mutual self-interest and facilities to trust strangers. Evidence about the value of trust for business and the economy is compelling [[1]].

Business Objectives

Corporations develop business strategies that prioritize and optimize for specific performance metrics at various stages of their lifecycle. While in the Formation Phase of their lifecycle, strategies are oriented toward revenue growth. These companies need to prioritize for customer trust and confidence. Corporations in the Investment Phase of their lifecycle strategize for enhancing business valuations and share prices. They need to prioritize for investor trust and confidence.

Measuring Trust

A well-known maxim is "what gets measured gets done." All enterprise processes benefit from measurement. Measurement of trust indicators allows organizations to address trust issues explicitly and implement trust management programs that demonstrate the results of trust optimization activities.

Trust Indicators

Since trust is simply an individual's perception, it is difficult to know how another feels. The most common means of measuring trust has, therefore, been surveys and questionnaires. However, people don't necessarily do what they say they would do. This is not because of deceit, but rather the differences in context and situations when answering questions versus taking consequential actions.

Action is ultimately the most meaningful indicator of trust. However, alone actions are insufficient to indicate trust, because the same action can result from a variety of influences, such as coercion.

Understanding which influences contribute to trust and their dynamics helps to attribute actions more directly to trust. In addition, observing customer and investor behaviour through various stages of their purchase can indicate their state of trust. For instance, significant due diligence prior to a purchase may indicate the need to attain higher levels of trust, while demands for guarantees may indicate mistrust.

Trust Enablement® Framework

The Trust Enablement® Framework outlines the factors that influence trust and their relative contribution to attaining trust objectives. The overriding trust objectives are to *develop* trust and *protect* trust. *Factual* and *Interpretive Sources of Trust* *develop* trust, while *Motive Forces* and *Proficiencies* *protect* trust. *Empowerment* and *Risk Transference* compensate for trust deficiencies.

Assessments of conditions for trust are examined according to contributing factors and how they satisfy the profile of each category in the Framework. The popularity of a grouping provides a simple measure for indicating trust. The most populous groupings signal a bias for a specific trust objective. The Framework provides a standardized means of comparing trust indicators from multiple assessments.

Framework dynamics allow trained practitioners of Trust Enablement® to analyze their assessment measures. This analysis provides additional trust indications by distinguishing between conditions that:

- develop trust from those that protect it;
- drive high levels of sustainable trust from those that facilitate transaction-oriented fast trust; and
- compensate for deficiencies in trust from those that support the primary conditions for trust.

Measuring Trust Indicators for Customers and Investors

Neither customers nor investors are homogeneous. Their trust requirements vary greatly depending on many factors, including the nature of their purchases and their stage of purchase completion. The Framework is equally useful for measuring and comparing trust indicators of e-commerce web sites, corporate governance practices and the institutional systems that facilitate capital market efficiencies.

Applications for the Trust Enablement® Framework

The Trust Enablement® Framework is a universal tool for measuring and comparing trust indicators. It is equally useful to policymakers when optimizing economic conditions and corporate boards of directors when optimizing governance practices for board effectiveness. Management can use the Framework to define their stakeholder trust management programs, and stakeholders, such as customers and investors, can use it to develop decision support tools that boost their confidence when making purchases.

Trust Enablement® is a novel and rigorous approach to assessing and designing trust measures and indicators. Trust optimizes stakeholder trust in any organization's value propositions. Trust creates conditions that build sustainable value.

---

[i] Ip, G. (July 17, 2002) “*Greenspan Gives Hopeful Outlook for Economy Despite Stock Swoon: Fed Chairman Warns That Loss of Trust Caused by ‘Infectious Greed’ Could Undercut Recovery*”, Wall Street Journal Online, Page One.

("Breakdowns in corporate governance could undermine the trust necessary for efficient markets…. That prospect, he [Alan Greenspan] said, threatened to "significantly erode" the economy's impressive gains in productivity.”)

The New York Times (July 17, 2002) "*Dr. Greenspan's Prescription*", The New York Times On The Web.

("The American economy "depends critically on trust," Mr. Greenspan declared. Investors who lack confidence in the system will be reluctant to buy stocks.")

Rich J. (2002) “*Golin/Harris Trust Survey*”, Golin/Harris International.

(“An America that is cynical or sceptical about business generally is a serious problem — more serious than any specific business scandal. Corporate misdeeds—or even perceptions of wrongdoing—cause direct and collateral damage to business as a whole, not only to specific industries”)

Accenture (2004) “*The business of trust*”, white paper referencing the World Economic Forum.

(“Business today also needs the trust and confidence of society to operate successfully. Without this, governments are likely to regulate to limit companies’ freedom of action, which may in turn constrain the entrepreneurial spirit…. Yet one consequence of declining trust is that business has lost its advocates — few people now seem willing to put the positive case for business — and the legitimacy of business seems to have been eroded in the eyes of the general public. Business is no longer seen as the wealth-generating engine for the whole of society.”)

Miller, D. (November 2002) “*Voice of the People Survey*”, World Economic Forum, conducted by Environics.

(“Unless traditional institutions regenerate public trust, people will continue to search for new ways forward. The real cost of inaction may be greater system instability and a growing mandate for NGOs and new political parties.”)

Rhoads, C., (June 7, 2002) “*Long-Term Economic Effects Of Sept. 11 May Be More Costly*”, Wall Street Journal.

(“In response to the terror attacks, the insurance industry has increased risk premiums … could hinder the real-time supply-chain management that many firms have developed in recent years, encouraging them to carry more inventories … Developing countries, in particular, could suffer because they likely wouldn't be included in these new trading arrangements … the boost in recent months in defense spending by governments, particularly the U.S., and private spending on security measures could soon amount to a drag on the economy … The report estimated that doubling private security spending reduces potential output by 0.6 percentage points after five years, and lowers productivity by 0.8 percentage points in that time.”)

McKenna, B. (June 28, 2002) “*Bush Fears Return to Recession*”, The Globe and Mail.

("'I'm concerned about the economic impact of the fact that there are some corporate leaders who have not upheld their responsibility,' Mr. Bush said … economists caution that a deepening crisis of confidence gripping financial markets is likely to cool prospects for months to come. 'Even without another big scandal, it could take six months to a year to get out from under this cloud,' said Peter Morici, an economist at the University of Maryland in College Park, Md. … 'Weak investor confidence, and in turn declining stock valuations, will impede the economic recovery,' agreed economist James Glenn of Economy.com Inc. in West Chester, Pa.").

Ezekiel, Z. (2005) "*Rebuilding Trust in Canadian Institutions*", The Conference Board of Canada.

("A prolonged and widespread failure of trust in public and private sector institutions has the potential to affect economic growth and corporate success in Canada. Trust is the 'glue' that holds the economy together. In the absence of trust, investors hesitate, capital markets falter, employees withhold commitment, suppliers grow wary and communities become reluctant to grant companies their 'social licence to operate.'")

("Regardless of the academic and methodological debates, it is evident that public and private sector leaders take seriously the issue of public trust. Many of them fear that lack of public trust impedes their organizations' functioning. Examples of this concern abound: Trust was chosen as the theme of the 2003 annual meeting of the World Economic Forum in Davos, Switzerland. Canadian private sector executives feel that public distrust interferes with their ability to do their jobs.")

Luaszewski, J. E. (2002) "*American Business Faces a Crisis of Trust*", Golin/Harris International.

("'An America that is cynical or skeptical about business generally is a serious problem— more serious than any specific business scandal,' said Rich Jernstedt, CEO, Golin/Harris International. 'Corporate misdeeds—or even perceptions of wrongdoing—cause direct and collateral damage to business as a whole, not only to specific industries.")

Leonhardt, D. (July 17, 2002) "*Is Uncertainty the Only Thing That Is Certain?*", The New York Times.

("A barrage of corporate scandals, combined with a 37 percent drop in the broad stock market since the beginning of 2000, has caused a questioning of the country's economic and financial future.")

[ii] Accenture (2004) "*The business of trust*", white paper referencing the World Economic Forum.

("Business has a particularly big challenge on its hands if it is to reverse this trend and recapture public trust. Failure to do so could cause long-term damage both to business and wider society, far beyond the US.")

("If this trend continues, it will help fuel the backlash against business and reinforce the actions of anti-globalization activists; and it is likely to result in more rules and regulations. It is therefore imperative that business leaders act now to start rebuilding trust.")

Luaszewski, J. E. (2002) "*American Business Faces a Crisis of Trust*", Golin/Harris International.

("The erosion of trust indicated in the research is a call to action. And it must be heard loud and clear.'")

Fukuyama, F. (1996) "*Trust: The social virtues and the creation of prosperity*", pp. 321, Free Press Paperbacks.

(Fukuyama sounds an alarm about economic consequences of a decline in American social capital, saying, "Once social capital has been spent, it may take centuries to replenish, if it can be replenished at all.")

(“Robert Putnam has compiled data that point to a striking decline in sociability in the United States. Since the 1950s, membership in voluntary associations has dropped.” “Communities of shared values, whose members are willing to subordinate their private interests for the sake of larger goals of the community as such, have become rarer. And it is these moral communities alone that can generate the kind of social capital that is critical to organizational efficiency.”)

Rich J. (2002) “*Golin/Harris Trust Survey*”, Golin/Harris International.

("The erosion of trust indicated in the research is a call to action. And it must be heard loud and clear.’”)

Simons, R., Mintzberg, H., and Basu, K, (2002) “*Memo to: CEOs*”, Fast Company, pp. 117.

(Business -- and capitalism -- are at a crossroads. Newspaper headlines today suggest a gathering crisis, one of performance, values, and confidence. It's time for CEOs to rally around a new set of business truths. It's time for an agenda that restores faith in business, trust in business leaders, and hope in the future.”)

[iii] Ezekiel, Z. (2005) “*Rebuilding Trust in Canadian Organizations*”, The Conference Board of Canada.

(A cautionary note: “In other words, to determine individuals’ propensity to trust, it is more useful to measure what they have tended to do rather than what they *profess to think*.”)

Note: Lack of trust appears to be significant and widespread. See [Appendix].

[iv] Ezekiel, Z. (2005) “*Rebuilding Trust in Canadian Institutions*”, The Conference Board of Canada.

(“In 2002, a majority of Canadians polled by the Centre for Ethical Orientation agreed that trust is in decline. This survey found that ‘8 in 10 . . . Canadians agree distrust is growing,’ while 87 per cent ‘agree people are less trusting than in the past.’ Since then improvement, if any, has been slight. In 2004, a relatively optimistic survey suggested that public trust had rebounded somewhat from 2002, but it also noted that ‘companies and governments cannot be cheered by simply returning to [what were previously] historically low levels of trust.’”)

Accenture (2004) “*The business of trust*”, white paper referencing the World Economic Forum.

(“Such a decline could never be good news, but it is particularly worrying today because new ways of doing business depend on high trust levels.”)

[v] Fukuyama, F. (1996) “*Trust: The social virtues and the creation of prosperity*”, pp. 151, Free Press Paperbacks.

(“Now trust has a very important pragmatic value, if nothing else. Trust is an important lubricant of a social system. It is extremely efficient and it saves a lot of trouble to have a fair degree of reliance on other people’s word.” – quoted of Nobel laureate Kenneth Arrow”)

Ibid., pp. 321.

(“People who do not trust one another will end up cooperating only under a system of formal rules and regulations, which have to be negotiated, agreed to, litigated, and enforced, sometimes by coercive means. This legal apparatus, serving as a substituted for trust, entails what economists call ‘transaction costs.’”)

Cai, R. (Defended on May 5th, 2004) “*Trust and Transaction Costs in Industrial Districts*”, Major Paper submitted to the faculty of the Virginia Polytechnic Institute and State University.

(“In general, trust helps reduce these transaction costs and the input of transaction costs will in turn, changes the perception of trustee’s trustworthiness.”)

Shirley, Mary M., “*Institutions and Development*”, The Ronald Coase Institute, May 2004.

(“ [For economic development] encourage trade by promoting trust & lowering transaction costs…. Trust correlates with growth & development.”)

Moore, C., and de Bruin, A.(June 2004) “*A Transaction Cost Approach to Understanding Ethical Behaviour*”, World Congress of Social Economics, Albertville, France.

(“The presence of trust and an ethical mindset can substantially lower TCs [transaction costs]. Organizations may achieve TC economisation by applying trusting and ethical behaviours at both the firm and societal level.”)

(“Trust is just as crucial at the broader societal level as it is at the micro level of conducting business. Lower levels of generalized trust and morality in a society increase the TCs [transaction costs] of conducting business for all entrepreneurs in such a society.”)

[vi] Ip, G. (July 17, 2002) “*Greenspan Gives Hopeful Outlook for Economy Despite Stock Swoon: Fed Chairman Warns That Loss of Trust Caused by ‘Infectious Greed’ Could Undercut Recovery*”, Wall Street Journal Online, Page One.

("Breakdowns in corporate governance could undermine the trust necessary for efficient markets…”)

Ezekiel, Z. (2005) “*Rebuilding Trust in Canadian Institutions*”, The Conference Board of Canada.

(“Trust is the ‘glue’ that holds the economy together. In the absence of trust, investors hesitate, capital markets falter,…”)

[vii] Yankelovich (2004) “*State of Consumer Trust*”.

(“Trust increases retention, boosts spending, enables premium pricing and provides a lasting competitive advantage.”)

Note: The evidence is compelling that increased levels of trust are good for business in general, and specifically contribute to improving share value, investment, growth, revenue, price, profitability, business effectiveness, productivity, change and agility, innovation and entrepreneurship, efficiency, cost savings, sustainability, employee retention, stakeholder engagement, living values and good citizenship, and collecting private information. However, a culture of trust must be rooted in at the top, in corporate governance, in order for trust initiatives to have any hope of success and yield sustainable business benefits. See itemized benefits in [Appendix]

[viii] Keser, C., Leland, J., Shchat, J., and Juang, H. (2002) “*Trust, the Internet, and the Digital Divide*”, IBM Research Report.

(Knack and Keefer (1997) “found that a very measure of how trusting inhabitants of different countries are is a significant explanatory variable in regression of average annual growth rates in per capita income from 1980 to 1992. Moreover, the impact is large – a 10% increase in the measure of trust translates into a .8% increase in economic growth – a sizable increment given world average growth rates of 1% to 3% in the latter half of the 20th century.”)

Ip, G. (July 17, 2002) “*Greenspan Gives Hopeful Outlook for Economy Despite Stock Swoon: Fed Chairman Warns That Loss of Trust Caused by ‘Infectious Greed’ Could Undercut Recovery*”, Wall Street Journal Online, Page One.

("threatened to "significantly erode" the economy's impressive gains in productivity.")

McKenna, B. (June 28, 2002) "*Bush Fears Return to Recession*", The Globe and Mail.

("'I'm concerned about the economic impact of the fact that there are some corporate leaders who have not upheld their responsibility,' Mr. Bush said … economists caution that a deepening crisis of confidence gripping financial markets is likely to cool prospects for months to come. 'Even without another big scandal, it could take six months to a year to get out from under this cloud,' said Peter Morici, an economist at the University of Maryland in College Park, Md. … 'Weak investor confidence, and in turn declining stock valuations, will impede the economic recovery,' agreed economist James Glenn of Economy.com Inc. in West Chester, Pa.").

[ix] Frankel, T. (1999) "*Trusting and Non-Trusting: Comparing Benefits, Cost and Risk*", Boston University School of Law, Working Paper Series, Law & Economics, Working Paper No. 99-12.

(Americans have created a system which reduces the costs of trusting and maximizes its benefits. I believe that what makes America so successful is the method it has developed for resolving the conflict between necessary trusting on the one hand, and its culture and disadvantages of personal trusting on the other hand. Americans have developed an extraordinary degree of trusting in their institutions. In fact, this trust embraces both business and political norms and institutions. Cynical as they are on the interpersonal level, Americans revere their constitution and trust their banks, mutual funds, and insurance companies. This trusting relationship is the foundation of American capitalism.)

("Americans have expanded institutions to introduce trusting among total strangers located far apart. One institution uses intermediaries to ensure the performance of promises and sometimes the resolution of conflicts among the trading partners. The beauty of this arrangement is that the intermediaries' interests to execute the transactions no matter who wins or loses strengthens impersonal trusting.")

Fukuyama, F. (1996) "*Trust: The social virtues and the creation of prosperity*", pp. 321, Free Press Paperbacks.

(Societies with a high degree of generalized trust and, consequently, a strong propensity for spontaneous sociability, such as Americans' rich network of voluntary associations and community structures to which individuals have subordinated their narrow interests, have private sector firms that are significantly larger than familistic societies that provide no basis of trusting unrelated people. "There is a relationship between high-trust societies with plentiful social capital – Germany, Japan, and the United States – and the ability to create large, private business organizations.")

[x] Mitchell, S. L. (2007) "Making the Business Case: Integrating Governance, Risk and Compliance to Drive Principled Perfromance", http://www.oceg.org/webinars/2007/2007.01.25-BusinessCase/MakingBusinessCase.html.

[xi] Martin, R. L., Archer, M. A., and Brill, L., "*Why do People and Organizations Produce the Opposite of What they Intend?*", paper commissioned by The Walkerton Inquiry.

("Mistrust and cover-up breed more draconian formal fixes, which breed still more mistrust and cover-up and so on.")

Frankel, T. (1999) "*Trusting and Non-Trusting: Comparing Benefits, Cost and Risk*", Boston University School of Law, Working Paper Series, Law & Economics, Working Paper No. 99-12.

("trusting is crucial and benefits all parties, while mistrust is corrosive, and disadvantages all.")

Riegelsberger, J. (June 27, 2005 – Online version July 12, 2005) "*Trust in Mediated Interactions*", University College London, dissertation submission – Doctor of Philosophy, University of London.

("Adopting legalistic mechanisms may not only fail to restore trust, but may lead to an escalating spiral of formality and distance that increases distrust." {Sitkin & Roth, 1993, p. 385}.")

[xii] Zak, P. J., Kurban, R., and Matzner, W. T. (2004), "*The Neurology of Trust*", New York Academy of Sciences.

("We show that receipt of a signal of trust is associated with a higher level of peripheral oxytocin than that in subjects receiving a random monetary transfer of the same average amount. Oxytocin levels were also related to trustworthy behavior (sharing a greater proportion of the monetary gains). We conclude that oxytocin may be part of the human physiology that motivates cooperation.")

[xiii] Knack, S., and Zak, P. J. (2002) "*Building Trust: Public Policy, Interpersonal Trust, and Economic Development*", Forthcoming Supreme Court Economic Review.

"(Zak & Knack (2001) demonstrate that interpersonal trust has a considerable effect on economic growth as trust affects the transactions costs associated with investment.1 Their analysis shows that if trust is su±ciently low, so little investment will be undertaken that economic growth is unachievable, resulting in a low-trust poverty trap. Even in a growing economy, interpersonal trust is a powerful economic stimulant: a 15 percentage point increase in the proportion of people who report that others in their country are trustworthy raises per capita output growth by 1% for every year thereafter. Further, economic growth initiates a virtuous circle as income gains enhance interpersonal trust.")

Govier, T. (2004) "*Additional excerpts from "Trust, Precarious Treasure*", Harvard University, http://cyber.law.harvard.edu/trusting/govier2.html.

("A fascinating and distinctive aspect of social capital is that unlike other forms of capital, when it is used, the supply tends to increase rather than diminish: "The more two people display trust towards one another, the greater their mutual confidence." Social capital is intensely sensitive to virtuous circles (trust builds on trust) and vicious circles (distrust builds on distrust). In a rosy spiral, or virtuous circle, there is a benign equilibrium: we find high levels of cooperation, trust, reciprocity, civic engagement, and collective well being. In a vicious circle there is a stagnant equilibrium: defection, distrust, shirking, isolation, exploitation, and disorder.")

[xiv] Open Compliance & Ethics Group (2007) "*OCEG® Measurement & Metrics Guide – Executive Summary*", http://www.oceg.org/download/MMGExecSum.

[xv] `Huang, H., Keser, C., Leland, J., and Shachat, J. (2003) "*Trust, the Internet, and the digital divide*", IBM Systems Journal, Vol. 42, No. 3.

[xvi] IBM, eBay (2002) "*Trusted e-Business Innovation Consortium*", Dale Carnegie & Associates, Inc.

[xvii] Note: In earlier papers the *Factual Sources of Trust* category of the Trust Enablement® Framework was more accurately named *Experiential Sources of Trust*, because it addressed both factual and emotional considerations. This paper uses the new naming convention to maintain consistency with Part I, in which it was introduced to help improve reader understanding by making it logically congruent with the *Interpretive Sources of Trust* category. The author intends to revert to the earlier naming convention in his future work.

[xviii] Goedhard, M. H., Jiang, B., and Koller, T. (September 2007) "*Market fundamentals: 2000 versus 2007*", The McKinsey Quarterly.

[xix] Edelman (2007) "2007 *Edelman Trust Barometer*"

[xx] O'Rourke, P.J. (2007) "*P. J. O'Rourke on the Wealth of Nations*", Atlantic Books.

[xxi] Note: The classification process requires judgement to make valid category assignments. The examples are used only to illustrate use of the Trust Enablement® Framework for indicating trust. In many cases, valid arguments can be made for reclassifying items in different ways. It is critical that a well-defined context is applied consistently throughout the classification process in order to ensure that the results indicate trust for a specific purpose.

[xxii] Strouse, J. (July 7, 2002) "*Capitalism Depends on Character*", New York Times.

("Someone has to stand behind the fundamental accuracy of a company's financial statements in a legally responsible way, but derelict auditors, executives and boards of directors have defaulted, either by design or inexcusable ignorance. A second tier of guardians -- Wall Street analysts, rating agencies, the Securities and Exchange Commission -- failed to issue warnings of corporate deceit.")

[xxiii] Frankel

[xxiv] Macey, J. R. (2003) "*A Pox on Both Your Houses: Enron, Sarbanes-Oxley and the Debate Concerning the Relative Efficacy of Mandatory versus Enabling Rule*", Washington University Law Quarterly, vol. 81:329.

[xxv] Wikipedia, http://en.wikipedia.org/wiki/Corporate_governance#Definition.

("Corporate governance is the key mechanism through which this trust is maintained across all stakeholders.").

Wikipedia, at http://en.wikipedia.org/wiki/Governance#Corporate_governance.

("…provide the means by which each individual part of the organisation can trust that the other parts each make their contribution to the mutual benefit of the organisation and that none gain unfairly at the expense of others….")

[xxvi] Smith, J.H. (Summer 2003) "*The Shareholder vs. Stakeholder Debate*", MIT Sloan Management Review, vol. 44, No. 4.

("Jay Lorsch states that two principles for the nexus of directors' legal responsibilities: a duty of care and a duty of loyalty.).

[xxvii] Martin, R., and Bailie, J. (La Sapiniere, September 5 to 7, 2003, draft June 10, 2003) "*Background Paper on 'Confidence Control and Compensation in the Modern Corporation'*".

[xxviii] Ibid.

[xxix] Note: To clarify, as the reader will discern from the discussion on trust, the statement does not use the term 'trust' in the sense of a relationship between individuals, but instead as trust and confidence in the implicit and explicit promises or obligations of the respective parties.

[xxx] "*Article at a Glance: Better boards in Thailand*", The McKinsey Quarterly, http://www.mckinseyquarterly.com.

("Companies [listed on the stock exchange in Thailand] with strong corporate governance practices have higher market valuations.")

Thompson, M. (June 4, 2001) "*Better Corporate Governance Pays Off for Large Companies in Emerging Markets*", http://www.socialfunds.com.

(“In examining the 100 largest companies in emerging markets, researchers found a strong correlation between corporate governance and financial performance ratios.”).

The Financial Express (May 5, 2003) “*Corporate Governance and Performance – Expectations and Realities*”, The Financial Express, Corporate Governance Press Coverage, http://www.mckinsey.com.

(“Institutional investors are willing to pay a premium for well-governed companies.”).

Bauer, B., and Guenser, N. (April 2003) “*Good Corporate Governance pays off!”*, ABP Investments, http://www.deminor.org/.

(“Portfolios of companies with high corporate governance standards perform better than companies with worse standards. Investors value well-governed companies significantly higher.”)

(2001, 2003) “*Striking a New Balance” and “Institutional Investor Preferences: 2003 Second Quarter Results*”, Working Council for CFOs, PeopleSoft Presentation materials.

(“While investors penalize poor transparency … they reward good corporate governance efforts. [measured by “Opacity Discount” and “Corporate Governance e Premium”]).

Wikipedia at http://en.wikipedia.org/wiki/Corporate_governance

(“In its 'Global Investor Opinion Survey' of over 200 institutional investors first undertaken in 2000 and updated in 2002, McKinsey found that 80% of the respondents would pay a premium for well-governed companies. They defined a well-governed company as one that had mostly out-side directors, who had no management ties, undertook formal evaluation of its directors, and was responsive to investors' requests for information on governance issues. The size of the premium varied by market, from 11% for Canadian companies to around 40% for companies where the regulatory backdrop was least certain (those in Morocco, Egypt and Russia).

Other studies have linked broad perceptions of the quality of companies to superior share price performance. In a study of five year cumulative returns of Fortune Magazine's survey of 'most admired firms', Antunovich et al found that those ‘most admired’ had an average return of 125%, whilst the 'least admired' firms returned 80%. In a separate study Business Week enlisted institutional investors and 'experts' to assist in differentiating between boards with good and bad governance and found that companies with the highest rankings had the highest financial returns.

On the other hand, research into the relationship between specific corporate governance controls and firm performance has been mixed and often weak.”)

[xxxi] Note: Fiduciaries are a source of trust for third parties. However, directors’ and officers’ fiduciary duty of loyalty to the corporation is not a matter of trust. Loyalty is an obligation -- a control mechanism. The law implicitly gives corporations control over directors’ and officers’ motivations (*motive forces*). Corporations, therefore, do not need to develop trust in their directors and officers.

[xxxii] Note: A tug of war is being waged between the those who believe that corporations should be governed to maximize shareholder value versus those who believe that the only honest and efficient way to build value is by focusing on engaging the resources of key stakeholders to contribute to the value creation efforts of the organization. The following excerpt represents an example of the latter perspective.

Simons, R., Mintzberg, H., and Basu, K, (2002) “Memo to: CEOs”, Fast Company, pp. 117.

(“Of course, there is a half-truth in this mantra: Shareholders' interests are significant. The capital markets do need to work, and for that, shareholders need a fair return on their investment. But there is a larger truth to this half-truth: Maximizing shareholder value at the expense of all of the other stakeholders is bad for business and bad for capitalism. It drives a wedge between those who create the economic value -- the employees -- and those who harvest its benefits. Customers, too, recognize the cynicism of a company that only sees them as dollar signs. That may be one reason why the American Customer Satisfaction Index has declined steadily in almost every industry since the mid-1990s. "Maximize shareholder value" may be the job description that CEOs automatically recite -- but it is profoundly misguided.")

[xxxiii] The Conference Board (2005) *"Corporate Governance Handbook 2005: Developments in Best Practices, Compliance, and Legal Standards*".

[xxxiv] Armour, S. (February 5, 2002)"*Employees' new motto: Trust no one*", USA Today, published by Council of Public Relations Firms.

("More workers are suing employers for claims that basically amount to a breach of trust.")

[xxxv] Liesman, S. (July 18, 2002) "*The strange Disconnect Between The Stock Market and Econo*my", Wall Street Journal.

("Most economists will tell you that the current disconnect between stocks and the economy is - at least in the post-war era - historic…. The Market at the moment is doing its own thing for its own reasons. And not many - or even any - of those reasons concern the direction of the economy. Accounting scandals and corporate corruption, the war on terrorism - all provide sound reasons for what many say is a rethink of the multiple that investors will pay for future earnings. Part of what we're watching is the painful recalibration of risk.")

[xxxvi] Todd, A. (2006) "*Corporate Governance Best Practices: One size does not fit all*" at http://trustenablement.com/local/Corporate_Governance_Practices-One_size_does_not_fit_all.pdf;

Note: For research findings about trust trends and the business benefits of trust see "*The Facts on Trust*" at http://trustenablement.com/opt/The_Facts_on_Trust.pdf.

[xxxvii] Alwis, A., Kremerman, V., and Shi, J. (Winter 2005) "*D&O Reinsurance Pricing – A Financial Market Approach*", Casualty Actuarial Society *Forum.*

[xxxviii] Note: The author had access to additional material that was confidential to one insurance company that takes a 'quality of corporate governance' approach and could therefore not display it in the table, however the inclusion of that information would not change the results of the analysis.

[xxxix] OSC Corporate Governance Guidelines 58-201, SOX, Section 406 (Senior Financial Officers)

[xl] OSC Certification of Disclosure in Issuers' Annual & Interim Filings 52-109, SOX Section 302

[xli] OSC Corporate Governance Guidelines 58-201

[xlii] OSC Corporate Governance Guidelines 58-201

[xliii] OSC 52-110, SOX, Section 301

[xliv] OSC Audit Committee 52-110, SOX, Section 301

[xlv] OSC Certification of Disclosure in Issuers' Annual & Interim Filings 52-109, SOX Section 302

[xlvi] OSC Audit Committee 52-110, SOX, Section 301

[xlvii] OSC Corporate Governance Guidelines 58-201

[xlviii] Todd, A. (2006) "*Corporate Governance Best Practices: One size does not fit all*" at http://trustenablement.com/local/Corporate_Governance_Practices-One_size_does_not_fit_all.pdf

[xlix] Todd, A. (2006) "*A Tale of Two CEO's*", at http://www.trustoptimizer.com/A_Tale_of_Two_CEOs.htm

[l] Todd, A. (2006) "*The Facts on Trust*", at http://trustenablement.com/opt/The_Facts_on_Trust.pdf