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Keys to Effective Corporate Governance -*October 27, 1999*
H. Stephen Grace, Jr., John E. Haupert, and Robert S. Roath -Grace & Co. Consultancy, Inc.

KEYS TO EFFECTIVE CORPORATE GOVERNANCE

By H. Stephen Grace, Jr., John E. Haupert, and Robert S. Roath

It has become increasingly obvious to most parties with a stake in good corporate governance that much improvement is needed and that the lead in this effort should come from the audit committee of the board. The authors have been saying, for some time, that improved audit committee performance is the lynchpin of effective corporate governance and have given much thought to how this can be accomplished.

The key to good corporate governance is to make sure that the key players of an organization are united into a cohesive unit to ensure the right steps are taken to protect shareholder value. On the surface this seems like a no-brainer and something every company should have at the forefront of its mission statement. The reality, however, is that competing interests, egos, misguided compensation arrangements, incompetence and sometimes outright criminal behavior can often pull staff in different directions and may ultimately undermine a seemingly successful company.

Who are the key players? In our judgement they are the board, audit committee, management, in-house counsel, and internal and public auditors. What is needed to make these players operate successfully? There are a host of basics that apply to each of the groups. Obviously they must all have a certain level of competence, commitment, and clear lines of authority and responsibility. Moreover, each player should have an appreciation and respect for the other players' role but should also maintain a probing attitude about all aspects of the business. The audit committee, in particular, should be continually challenging all the other players since it is the ultimate guardian of shareholder value. Finally, there must be adequate resources available for all to do their job properly.

Perhaps less obvious is the need for all of the players to have a clear picture of where the business is heading and a common understanding of how it plans to get there. One way to accomplish this is to create a management model that forces a company to continually reevaluate its fundamental targets, select the proper tools to hit its targets and use appropriate measurements techniques to evaluate performance. A good guide on how such a model can work may be found in a management strategy article entitled The Missing Management

Model in the Jan/Feb 1996 Financial Executive magazine.

The audit committee would well serve the organization by taking the lead in making sure the necessary ingredients for good corporate governance are in place. It is best situated to ask the right questions and to exert the necessary pressure to see to it that all of the key players have the tools needed to do the job and are all pulling in the right direction. Of course, the audit committee must itself be in good order before it can do that job. Here is where an outside review of audit committee performance can be invaluable. An objective examination by advisors with allegiance only to the committee can make sure proper oversight is being exercised and that the proper relationship with other players is established. The advisors would be in a very good position to suggest the changes necessary to bring about effective corporate governance, while recognizing the need to be sensitive to the tensions that can and should develop between the audit committee and other players.

H. Stephen Grace, Jr. is president of Grace & Co. Consultancy, Inc. John E. Haupert and Robert S. Roath are members of the board of advisors of Grace & Co. Prior to their respective retirements, Mr. Haupert was treasurer of The Port Authority of New York and New Jersey; Mr. Roath was CFO of RJR Nabisco Holdings Corp. and is Chairman of the Advisory Board of L.E.K. Consulting.

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