

Good governance: critical for effective organisational leadership

Governance is the term used to describe the structures and disciplines that characterise oversight of an organisation. Corporate governance describes the boards, committees, control functions and supporting infrastructure of a company. Good governance is essential not just for effective company oversight, however, but for all types of organisations. Retirement funds, government, parastatals and foundations all benefit from effective leadership.

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South Africa plays a leading role in the development of effective governance. Our own Dr Merwyn King has lent his expertise to the principles of governance that bear his name, now in their fifth iteration. Organisations of all types and in many countries seek to apply the King IV or King V framework to their leadership structures. But why, you may ask, does governance have to be so complicated?

First, the principles underlying effective governance are not unduly complicated. We consider a few of them in this note. Second, though they are not guaranteed to avert difficulty, they work. An entity with good governance may not be perfect, but you can be confident that its counterpart with poor governance is simply not worthy of our trust. The news is full of such organisations.

Independence matters

One of the first principles underpinning effective governance is that independence matters. An effective board or oversight committee includes an appropriate mix of members who do not have a direct financial interest in the decisions made by that group.

This is important because such financial interests, as helpful as they may be in motivating appropriate behaviour, can skew effective decision-making. They tend to lead to short-term thinking, a preference for quick fixes over measured development. They may prioritise profit over investment or responsibility. Financial interests are more likely to lead to panicked responses to adversity. Pension fund trustees representing a particular group may put the interests of that group above the corresponding interests of the fund itself.

Independence on the management committee helps to mitigate the risk of skewed or biased thinking. It brings perspective and promotes objectivity. Independence is not only important at the level of the board, however. Control functions such as auditors and risk managers should also be characterised by independence, preferably supported by incentives linked to the quality

of their contribution to effective governance, not the financial outcomes of the entity that they serve.

Expertise matters

Companies, retirement funds, municipalities and universities are complex at the best of times. Preparing the financial statements of these entities is enormously challenging, how much more the requirement to ensure that these statements are a true reflection of the position of the entity?

Expertise matters. A board of directors or trustee body must have sufficient skill and experience in its ranks to put in place sound organisational structures, with checks and balances, that identify shortcomings in the processes and errors in the financial statements. This helps to explain the value of specialised sub-committees, like an audit committee, and control functions like auditors, that execute on a specialised mandate to ensure the accuracy of the information leading to financial reports.

We live in a world unfortunately in which so many people appear intent on hiding something, or misrepresenting the facts. Sound governance is critical to unearthing such behaviour, but the premium on the necessary expertise is greater under such conditions.

Integrity matters

In a world in which transparency seems to be so rare, integrity is critical. Integrity is perhaps that part of the governance framework that cannot be implemented by a set of rules. But it can be upheld by sound discipline.

If we put in place a set of rules and operate to them, integrity is more likely to be valued and upheld. If the records of our discussions are diligently captured and ratified, if decisions are implemented and their effectiveness monitored, if control functions to monitor compliance and risk management are respected and effectively utilised, then integrity is more likely to characterise the operations and decisions of an organisation. Integrity cannot be mandated, but it most certainly can be crushed, ignored or squeezed out.

The rules of effective corporate governance may appear to be extensive, but the principles underpinning them are not. They assist the leaders of good organisations to do better. They are critical to the oversight of otherwise poor organisations. But principles must be translated diligently into effective actions if they are to lead to trustworthy companies, retirement funds and state-owned entities.

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