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ENCOURAGING CORPORATE GOVERNANCE FOR THE CLOSELY HELD BUSINESS

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I. INTRODUCTION

Recent highly publicized problems in several large corporations have raised awareness to the importance of corporate management practices and oversight.[1] While steps have been taken to improve corporate governance in publicly traded corporations, little movement has been made to protect investors in non-publicly traded companies. The Sarbanes-Oxley Act of 2002 was enacted to enhance corporate governance procedures, protect shareholders in publicly traded companies, and in some cases, specifically prohibit questionable business practices. However, many of these same principles of corporate governance can and should be applied to non-publicly traded companies.[2]

II. BACKGROUND

The same potential for corporate mismanagement that occurred in public corporations exists in non-publicly traded companies. While an individual collapse of a non-publicly traded company would not have the same harsh impact as Worldcom's collapse, the financial problems caused by such a failure would not be without effect, because non-publicly traded companies play a major role in the United States economy.[3] C corporations accounted for only eleven percent of all U.S. firms by organization in 1997, despite accounting for seventy-five percent of all U.S. firms' receipts.[4] S corporations accounted for ten percent of all U.S. firms, and were responsible for sixteen percent of all firms' receipts that year.[5] In Mississippi alone, there were 49,016 total firms employing 937,023 people in 1998.[6] Of these firms, ninety-seven percent were small businesses (less than five hundred employees), and they accounted for 449,393 jobs.[7] With the number of jobs at stake in these small businesses, proper corporate governance in non-publicly traded firms may well be just as important to our economy as effective governance in publicly traded firms.

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* With grateful appreciation to my parents for their decades of encouragement, love and support.

1. *See* American Bar Association Task Force on Corporate Responsibility, *Preliminary Report of the American Bar Association Task Force on Corporate Responsibility*, 58 BUS. LAW. 189, 190 (2002) [hereinafter *ABA Task Force*] ("Few events in business history since the Great Depression have had the public impact of the stunning collapse of Enron Corp. and other major companies in the past year.").

2. *See* The Council of Institutional Investors, Corporate Governance Policies, *at* http://www.cii.org/dcwascii/web.nsf/doc/policies_index.cm (last updated Sept. Oct. 13, 2004) ("The Council believes good governance practices should be followed by publicly traded companies, private companies and companies in the process of going public.").

3. *See* The State of Small Business: A Report to the President, 17 (2001) [hereinafter "Small Business"], *at* http://www.sba.gov/advo/ stats/stateofsb99_00.pdf ("Small businesses represent [ninety-nine] percent of businesses, employ more than half of the American workwork force, and create two-thirds of the net new jobs.").

4. U.S. CENSUS BUREAU, U.S. DEP'T OF COMMERCE, COMPANY SUMMARY: 1997 ECONOMIC CENSUS 12 (Sept. 2001), http://www.census.gov/prod/ec97/e97cs-1.pdf.

5. *Id.*

6. Small Business, *supra* note 3, Table A.4 at 64.

7. *Id.*

A. What is Corporate Governance?

Corporate governance refers to those procedures established within a company's organization that allow director oversight of key officer decisions, provide disclosure of material facts to investors and other stakeholders, and allow for efficient and accurate decision making within the organization. Corporate governance describes "the legal rules relating to the respective powers and duties of directors, officers and shareholders."[8] "A good corporate governance structure is a working system for principled goal-setting, effective decision-making and appropriate monitoring of compliance and performance."[9]

B. The Importance of Corporate Governance to Close Corporations

Some argue that corporate governance is not as important an issue in a close corporation, because managers, as substantial owners of the business, are much more likely to act in the best interests of the business.[10] However, as corporations continue to compensate managers with ownership rights, such as stock options, there is much more alignment between ownership and control in publicly traded corporations. High level managers in public companies therefore have a substantial financial stake in their company and bear both the risks and rewards of their decisions. Thus, managers of publicly traded companies are probably just as likely as managers of close corporations to make decisions that they believe will most benefit their company. However, these decisions may not in themselves constitute good corporate governance.

"Good corporate governance should provide proper incentives for the board and management to pursue objectives that are in the interests of the company and shareholders and should facilitate effective monitoring, thereby encouraging firms to use resources more efficiently."[11] There is no one formula for effective governance, and no one standard that would necessarily fit the needs of both small and large businesses.

> Good governance is not a 'checklist' of the '"ten most important best practices'," but to a large extent it is a state of mind – a considered balance between the need for the board to represent shareholder interests and the need to ensure management feels sufficiently free to focus on value creation.[12]

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8. American Bar Association, *Managing Closely Held Corporations: A Legal Guidebook*, 58 BUS. LAW. 1073, 1088 (2003). *See also* Robert W. Hamilton, *Corporate Governance in America 1950-2000: Major Changes but Uncertain Benefits*, 25 J. CORP. L. 349, 349 (2000).

9. THE BUSINESS ROUNDTABLE, PRINCIPLES OF CORPORATE GOVERNANCE, at 2 (May 2002) [hereinafter BUSINESS ROUNDTABLE], http://www.brtbusinessroundtable.org/pdf/704.pdf.

10. *See* Frank H. Easterbrook & Daniel R. Fischel, *Close Corporations and Agency Costs*, 38 STAN. L. REV. 271, 277 (1986) ("Where management and risk bearing are separate, as in publicly held corporations, managers' incentives to act efficiently are weak because they neither bear the costs nor reap the benefits of their actions.").

11. OECD PRINCIPLES OF CORPORATE GOVERNANCE 2 (Jan. 2004) [hereinafter OECD PRINCIPLES], http://www.oecd.org/dataoecd/19/29/23888981.pdf.

12. BOB FELTON & MARK WATSON, THE NEED FOR INFORMED CHANGE IN THE BOARDROOM 10, http://www.mckinsey.com/clientservice/organanizationleadership/service/corpgovernance/pdf/Director Opinion.pdf (last visited Oct. 15, 2004).

In this context, corporate governance should be adopted by both publicly owned and closely held corporations.

Of course, the level of corporate governance that any individual firm needs is a function of many different factors, not the least of which is the expense involved in complying with various corporate governance requirements. In one survey of chief financial officers, cost estimates for compliance with the requirements of Sarbanes-Oxley ranged from several thousand dollars to more than one million dollars.[13] While some corporate governance requirements are mandatory for publicly traded companies, closely held corporations should be able to balance their governance needs against their budgetary constraints. However, business owners should recognize that corporate governance to a business is like a parachute to a skydiver: one item on which you shouldn't mind spending a little extra money.

Corporate governance is also an effective management tool for all businesses. "'[C]orporate responsibility' should be understood to include behavior by the executive officers and directors of the corporation that conforms to law and results from the proper exercise of the fiduciary duties of care and loyalty to the corporation and its shareholders."[14] Since these duties are already incorporated in state law, an effective system of corporate governance will also ensure compliance with the business's pre-existing legal obligations, a concern for businesses of all types.[15]

III. SIMILARITIES BETWEEN CORPORATE GOVERNANCE NEEDS OF PUBLICLY TRADED CORPORATIONS AND CLOSELY HELD CORPORATIONS

Calls for increased standards in corporate governance are based upon bolstering investor confidence,[16] upholding our free-market system,[17] and preventing mandatory regulation through voluntary compliance.[18] Likewise, effective and meaningful corporate governance standards can be used by non-publicly traded companies to increase capital available from outside sources,[19] prevent the mandatory regulation that has been imposed upon public corporations, enhance their business operations, and also reduce potential liability to stakeholders.

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13. PROTIVITI, INC., INSIGHTS ON TODAY'S SARBANES-OXLEY AND CORPORATE GOVERNANCE CHALLENGES 8 (Sept. 2003), http://www.protiviti.fr/downloads/CFOSurvey.pdf.

14. *ABA Task Force, supra* note 1, at 191.

15. *But see* Kent Greenfield, *Using Behavioral Economics to Show the Power and Efficiency of Corporate Law as Regulatory Tool*, 35 U.C. DAVIS L. REV. 581, 581 (2002) (discussing that net social benefits are a better measure of corporate governance than benefit or harm to the firm).

16. *See ABA Task Force, supra* note 1, at 190-91 ("Investor confidence in the quality and integrity of public company corporate governance is compromised, and the pace of calls . . . for regulatory reform has quickened dramatically.").

17. *See Promoting Better Corporate Governance in Listed Companies, Report of AFEP AGREEF/MEDEF Working Group Chaired by Daniel Bouton, President of Societe Generale Bank, September 23, 2002*, 1372 PLI CORP 465, 468 (2003) ("[T]here can be no free-market system without an underpinning of trust in the rule of law.").

18. *See* Larry E. Ribstein, *The Mandatory Nature of the ALI Code*, 61 GEO. WASH. L. REV. 984, 996 (1993) ("[J]udges, legislators, bureaucrats, and others who impose or administer mandatory rules – have less information about governance needs of individual firms than do firm owners and managers.").

19. *See* Easterbrook & Fischel, *supra* note 10, at 277 ("Those who attempt to attract other people's money have incentives to adopt governance mechanisms that respond to potential investors' concerns.").

A. Increasing Sources of Available Capital through Effective Governance

The ability to attract additional outside capital is an important asset to many businesses, because it allows them to seize opportunities that could only be realized with additional investments. Frequent sources of new capital include both the sale of new stock and loans from outside investors. Companies can attract these stakeholders by lowering their perceived risk through implementation of effective corporate governance.

1. Effective corporate governance is a means to attracting and protecting stakeholders

A system of corporate governance is becoming an effective means of luring new investors while also increasing value for existing shareholders. "An overwhelming majority of investors are prepared to pay a premium for companies exhibiting high governance standards. Premiums averaged 12-14% in North America and Western Europe."[20] These numbers indicate that the capital required to implement a corporate governance system would be a wise investment by managers.[21] Likewise, failure to implement such a system could have just the opposite effect.

One recent survey indicates that a majority of investors would avoid specific companies with inadequate governance policies, and a third of those polled would avoid those companies altogether.[22] A majority of investors also place equal or greater importance on corporate governance as compared to financial issues.[23] These numbers indicate that companies which fail to adopt proper governance policies run the serious risk of driving potential investors away.[24]

Beyond attracting new capital, corporate governance should also protect stakeholders in the company. Just as holders of publicly traded stock need protections, so also do investors in non-publicly traded stock. Investors who own only a few shares in a publicly traded company will be less likely to become involved in that company's affairs, because if they dislike the direction the company has taken, they can sell their shares in the open market.[25] In a non-publicly

20. MCKINSEY & COMPANY, GLOBAL INVESTOR OPINION SURVEY: KEY FINDINGS 2 (July 2002) [hereinafter GLOBAL SURVEY], http://www.mckinsey.com/clientservice/organizationleadership/service/corpgovernance/pdf/GlobalInvestorOpinionSurvey2002.pdf. *See also* Greenfield, *supra* note 15, at 584 ("The assumption is that '[t]he price [of a company's securities] reflects the effects, good or bad, of corporate law and contracts . . . .'" (quoting FRANK H. EASTERBROOK & DANIEL R. FISCHEL, THE ECONOMIC STRUCTURE OF CORPORATE LAW 19 (1991)).

21. *But see* JOEL POPKIN & CO., ESTIMATION OF SMALL BUSINESS WEALTH, 36 (Sept. 12, 2002) ("[I]t would never be possible to determine what part of the market valuation of a firm is based on the underlying fundamentals and what part might be caused by 'irrational exuberance.'"), http://www.sba.gov/advo/research/rs217tot.pdf.

22. GLOBAL SURVEY, *supra* note 20, at 2.

23. *Id.*

24. *But see* Hamilton, *supra* note 8, at 364 ("[T]here is surprisingly little evidence in the hundred plus studies conducted since the 1970s that changes in corporate governance have had any significant effect on the bottom line, one way or the other.").

25. Kerry Shannon Burke, *Regulating Corporate Governance Through the Market: Comparing the Approaches of the United States, Canada and the United Kingdom*, 27 J. CORP. L. 341, 367 (2002).

traded corporation, however, there is no readily available market for a dissatisfied shareholder's shares. Since "the issue of [corporate] governance involves the protection of the minority shareholders from oppression by the control group,"[26] effective governance is very important in a close corporation, where overreaching by the majority shareholders is much more likely.[27]

2. Effective corporate governance is a means to attracting and protecting creditors

Businesses borrow a great deal of money. In 1999, non-financial corporations borrowed $480 billion, while non-corporate businesses borrowed $106 billion.[28] "While the supply of funds appeared to be adequate, the cost of borrowing remained high and became an increasing concern to small firms in late 1999. Commercial banks began to tighten credit standards and raised credit terms."[29] With the tightening of available resources, a business that has implemented solid governance standards would present less risk to a potential creditor than a similarly situated business without those same governance standards. Therefore, good governance could make a business more competitive in an economy where lenders demand higher credit standards and lower risk.

B. Preventing Mandatory Regulation with Voluntary Governance

As previously discussed, many chief financial officers estimate that the costs of implementing Sarbanes-Oxley will be substantial.[30] A system of voluntary compliance can be much more attractive to businesses because it allows them to control their costs and determine their own level of risk, commensurate with their level of governance.

"Although voluntary codes and principles have the advantage of maintaining flexibility and avoiding excessive and costly legal regulatory measures, the question of their effectiveness does arise."[31] Voluntary regulation presents both enforcement and compliance issues.[32] At the same time, "imposing a single rule on all types of firms is fundamentally inconsistent with the adaptive nature of corporate governance."[33]

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26. Arthur R. Pinto, *Corporate Governance: Monitoring the Board of Directors in American Corporations*, 46 AM. J. COMP. L. 317, 317 n.3 (1998).

27. *But see* Julian Javier Garza, *Rethinking Corporate Governance: The Role of Minority Shareholders – A Comparative Study*, 31 ST. MARY'S L.J. 613, 636 (2000) ("Minority shareholders may not control the company, but their role in a corporation through minority rights, fiduciary duties, requirements of fair dealing and good faith, private agreements, and derivative suits influences corporate governance and makes minority shareholders significant players in the corporate world.").

28. Small Business, *supra* note 3, at 20.

29. *Id.* at 20, 22.

30. *See supra* note 13, and accompanying text.

31. *See* ORGANIZATION FOR ECONOMIC CO-OPERATION & DEVELOPMENT, SURVEY OF CORPORATE GOVERNANCE DEVELOPMENTS IN OECD COUNTRIES 32 (Dec. 2003) [hereinafter "OECD SURVEY"], http://www.oecd.org/dataoecd/58/27/21755678.pdf.

32. *See id.* at 32-33 (discussing voluntary compliance shortfalls in other countries).

33. Ribstein, *supra* note 18, at 996.

The opposing argument states that government regulation is needed, because companies simply will not voluntarily police themselves, citing Worldcom and Enron among others as examples that voluntary standards are ineffective. Proponents of this argument point to Sarbanes-Oxley as filling a large gap in state regulation.[34]

At the same time, a system of mandatory compliance does not guarantee that business managers will act with higher standards. "Policymakers need to identify compelling incentives to encourage family – and state – owned businesses voluntarily to upgrade their governance practices – just forcing change through regulations only creates a compliance, not a performance, mentality."[35] This can lead in turn to a process that merely hides improper behavior from the public rather than discouraging such behavior altogether.[36]

But consider that regulation can come from the courts as well as legislatures. "[T]he state courts that review the fiduciary duties of care and loyalty of directors and officers can be expected to identify and give effect to evolving expectations regarding oversight responsibility, conflicts of interest, and director independence . . . ."[37] Since business people prefer certainty over awaiting judicial interpretation, small businesses may want to voluntarily reform themselves before courts force reform.

C. Enhancing Business Operations with Corporate Governance

Effective corporate governance is also appropriate to the closely held corporation because it is a means of improving internal business operations. "To remain competitive in a changing world, corporations must innovate and adapt their corporate governance practices so that they can meet new demands and grasp new opportunities."[38] Thus, corporate governance creates more efficient corporate management. "[G]ood corporate governance – that is *accountable governance* – means the difference between wallowing for long (and perhaps fatal) periods in the depths of the performance cycle, and responding quickly to correct the corporate course."[39]

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34. *See* J. Robert Brown, Jr., *The Irrelevance of State Corporate Law in the Governance of Public Companies*, 38 U. RICH. L. REV. 317, 358 (2004) ("State law did not impose meaningful standards of behavior . . . [and] [t]he SEC's attempts to encourage higher standards through the use of disclosure had not worked."). *See also* Ribstein, *supra* note 18, at 987-88 ("The regulatory theory holds that, because corporate terms can be imposed on owners, states will compete in a 'race to the bottom' to provide corporate statutory terms that serve managers' rather than shareholders' interests."). *But see* BUSINESS ROUNDTABLE, *supra* note 9, at iv-v ("No law or regulation alone can be a substitute for the voluntary adherence to these principles by corporate directors and management . . . .").

35. MCKINSEY & COMPANY, EMERGING MARKET POLICYMAKER OPINION SURVEY: KEY FINDINGS 1 (Nov. 2002), http://www.mckinsey.com/clientservice/organizationleadership/service/corpgovernance/pdf/2002_Emerging_Market_Policymaker_Opinion_Survey_Corp_Gov.pdf.

36. *See* Burke, *supra* note 25, at 357 (discussing the advantages and disadvantages of permissive corporate governance guidelines).

37. *ABA Task Force, supra* note 1, at 197.

38. *OECD Principles, supra* note 11, at 4.

39. The California Public Employees' Retirement System, Corporate Governance Core Principles, *at* http://www.calpers-governance.org/principles/domestic/us/page01page02.asp (Apr. 1998) [hereinafter "CALPERS Principles"].

Effective corporate governance also encompasses internal management practices in addition to investor protections.

> The same internal control infrastructure that supports Sarbanes-Oxley compliance can also be leveraged to generate greater business success. A host of benefits could result – improved flow of information permitting better business decisions, better management of resources, streamlined operations, improved investor relations, and an enhanced reputation for leadership and integrity in corporate governance and reliable financial reporting.[40]

Another important reason to adopt good governance procedures is to prevent negative publicity. There is a growing trend to publicize companies that do not conform to generally accepted governance standards.[41]

These factors for enhancing business operations through improved decision making and avoidance of negative publicity translate equally to publicly traded or closely held corporations.

D. Reducing Potential Liability for Inadequate Governance

By voluntarily adopting the corporate governance standards required of publicly traded companies, close corporations can reduce their potential liability for violations resulting from inadequate governance systems. There is little doubt that, in the wake of recent scandals, stakeholders' expectations of management have risen. "While there is no change in the fundamental legal principles applicable to the duties and responsibilities of the boards of directors, there is a clear change in attitude by investors and the public at large that could manifest itself in adverse judicial decisions and further legislation."[42] And managers must be as careful with the actions they fail to take as with the actions they do take. "Today, the utter failure to follow the minimum expectations of the evolving standards of director conduct, the minimum expectations of Sarbanes-Oxley . . . might likewise raise a good faith issue."[43] As the Chief Justice of Delaware has further observed, "the issue of good faith may be measured not only by the evolving expectations of directors in the context of [the] common law fiduciary duty, but also against the backdrop of Sarbanes-Oxley and the [self-regulatory organizations'] requirements, even though there may be no express private right of action."[44]

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40. DELOITTE & TOUCHE, LLP, BEYOND COMPLIANCE: LEVERAGING INTERNAL CONTROL TO BUILD A BETTER BUSINESS, 3 (April 2003), http://www.fei/.org/download/beyond.pdf.

41. *See* The California Public Employees' Retirement System, Corporate Governance Business Plans, 5, *at* http://www.calpers.org//calendarapps/board/adhoc/adhoc/200401/item04%2D01eItem4-1e.doc (last visited Oct. 15, 2004) (discussing their intent to nationally publicize an annual "Dirty 30" list of the worst governed corporations).

42. Karen G. Krueger & David C. Karp, *Corporate Governance in Light of Sarbanes-Oxley and the NYSE Rules, in* PLI COURSE HANDBOOK (2002), *reprinted in* 1348 PLI/CORP 863, 911 (2002).

43. E. Norman Veasey, *Policy and Legal Overview of Best Corporate Governance Principles*, 56 SMU L. REV. 2135, 2141 (2003).

44. *Id.* at 2144.

The good news for managers is that this same shift in legal principles can also be used by managers to justify some actions that may not have made economic sense in the past, but which are required for good corporate governance.[45]

These increased standards expected of managers in publicly traded companies will not take long to seep over to close corporations. Therefore, an effective system of corporate governance is an appropriate means by which closely held corporations can reduce their potential liability to stakeholders.

IV. SUGGESTED CORPORATE GOVERNANCE MODELS

As previously mentioned, no one model of corporate governance may necessarily fit the specific needs of every business. Yet at the same time, the principles of stakeholder protection, deterrence of mandatory regulation, enactment of efficient business practices, and reduction in liability to stakeholders all apply to any form of business entity, whether public or private. While there are many different suggested models of effective corporate governance, there are several principles which appear in multiple models. These principles would therefore be appropriate for any business to follow, if possible.

A. Board of Director Duties

The Board of Directors is primarily responsible for selection and oversight of the Chief Executive Officer and supervision of management's overall performance.[46] In order to properly supervise those responsible for daily operations of the business, directors must know the business of their company, familiarize themselves with the company's financial statements, and understand the mission and strategic vision of their company. "The board should be engaged in *actual* governance and not merely act as advisors to the CEO."[47] These responsibilities require advance preparation by directors prior to all meetings.[48]

In order to best perform their functions, the board should ideally be comprised of a majority of independent directors. The New York Stock Exchange Corporate Accountability and Listing Standards Committee has modified its definition of "independent" so that "[n]o director qualifies as 'independent' unless the board of directors affirmatively determines that the director has no material relationship with the listed company (either directly as a partner, shareholder or officer of an organization that has a relationship with the company)."[49] Because it may be difficult for a closely held corporation to maintain a board with a

45. *See* David S. Ruder, *Public Obligations of Private Corporations*, 114 U. PA. L. REV. 209, 219 (1965) ("An additional area of business activity which can be justified according to business judgment concepts is corporate action taken either because the government is bringing indirect pressure upon the corporation or because pressure might be used by the government.").

46. BUSINESS ROUNDTABLE, *supra* note 9, at 1.

47. E. Norman Veasey, *An Economic Rationale for Judicial Decisonmaking in Corporate Law*, 53 BUS. LAW. 681, 699 (1998) (emphasis added).

48. *See* BUSINESS ROUNDTABLE, *supra* note 9, at 24.

49. Report of the New York Stock Exchange Corporate Accountability and Listing Standards Committee, 6 (June 6, 2002) [hereinafter NYSE Report], http://www.nyse.com/pdfs/corp_govreport.pdf.

majority of directors who meet this definition, closely held corporations should create and disclose their own definition of independence that will ensure their directors' ability to make independent decisions. This definition should ensure "a lack of conflict between the director's personal, financial or professional interests, and the interests of shareowners."[50] At a minimum, the following governance functions should be performed entirely by independent directors: auditing, director nomination, board evaluation, CEO evaluation and management compensation, and ethics compliance.[51]

Another method for minimizing conflicts between a director's personal interests and the interests of shareholders is to align directors' interests with those of shareholders through equity compensation. "Directors should be incentivized to focus on long-term stockholder value . . . [so] a meaningful portion of a director's compensation should be in the form of long-term equity."[52] Adherence to these guidelines should greatly improve the quality of corporate governance in any organization.

B. Senior Management Responsibilities

"The CEO and senior management are responsible for operating the corporation in an ethical manner . . . [and] should never put individual, personal interests before those of the corporation or its stockholders."[53] Senior management's responsibilities include reviewing financial statements, supervising internal controls, ensuring an atmosphere of ethical conduct, and providing a system of reporting misconduct. It is essential that the CEO, or other senior manager, communicates the status of these functions to the board. Senior managers should also make corporate governance visible by incorporating those principles in their company's mission statement. Such publication provides communication of these governance principles to shareholders and outsiders.[54]

Just as with directors, senior managers' interests should be aligned with the long term interests of their shareholders through the use of equity compensation. "Compensation programs are one of the most powerful tools available to the company to attract, retain, and motivate key employees, as well as align their interests with the long-term interests of shareowners."[55] To further ensure that shareholder interests do not conflict with senior management, and "[i]n order to provide checks and balances on the process of earmarking shares to be used for equity-based awards, and to provide shareholders a voice in the resulting dilution, . . . all equity-compensation plans, and any material revisions to the terms of such plans . . . should be subject to stockholder approval."[56]

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50. CALPERS Principles, *supra* note 39, at 4.
51. *See* CALPERS Principles, *supra* note 39, at 4.
52. BUSINESS ROUNDTABLE, *supra* note 9, at 25.
53. *Id.* at 9.
54. *See* NYSE Report, *supra* note 49, at 18-19 ("Given the importance of corporate governance, each listed company's website must include its corporate governance guidelines, the charters of its most important committees . . . and the company's code of business conduct and ethics . . . .").
55. CALPERS Principles, *supra* note 39, at 6.
56. NYSE Report, *supra* note 49, at 17.

V. CONCLUSION

"[N]ew prohibitions and mandates, whether adopted by the NYSE, the SEC or Congress, cannot guarantee that directors, officers and employees will always give primacy to the ethical pursuit of shareholders' best interests."[57] However, an effective system of corporate governance, which provides oversight of management by independent directors and where the interests of directors and managers are aligned with those of their stockholders, can significantly reduce the risk of overreaching by corporate executives and provide increased protections to all stakeholders. While there is a great deal of controversy concerning how much oversight is enough, companies like Worldcom and Enron have clearly shown how little is too little. "[I]t is a clear failure of corporate responsibility when outside directors, auditors, and lawyers, who have important roles in our system of independent checks on the corporation's management, fail to avert or even discover . . . the grossest of financial manipulations and fraud."[58] By recognizing that corporate governance is a continuing action, and by remembering their fiduciary duties to their stockholders, directors and managers of closely held corporations can stave off the negative publicity and loss of investor confidence that befell the public stock market.

57. *Id.* at 1.
58. *ABA Task Force, supra* note 1, at 192.