

BEYOND THE CHARTER

Governance Theatre: When Compliance Structures Satisfy the Auditor but Not the Board

A Practitioner's Perspective on Substance and Its Absence in Post-Reform Corporate Governance



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1. Executive Summary

The twelve months behind us have brought the most sweeping change to the machinery of corporate governance in a generation. In the United States the Sarbanes-Oxley Act has rewritten the obligations of directors, executives and auditors; a new public oversight board now supervises the audit profession; and the exchanges have advanced listing standards that reach deep into board composition and independence. In the United Kingdom, the Higgs review of non-executive directors and the Smith review of audit committees have set a direction the Combined Code is about to absorb. The direction of travel is unmistakable, and in its intent it is right.

And yet, in organisation after organisation, I observe a response that should trouble us. Boards and executives, under real pressure and in good faith, are building governance structures at remarkable speed — new committees, revised charters, certification routines, control documentation, expanded reporting — while the actual quality of the decisions those bodies reach has barely moved. The structure satisfies the auditor. It satisfies the checklist. It does not satisfy the board's own private knowledge of how it really decides. This gap between the appearance of governance and its exercise is what I call governance theatre, and it is the defining risk of the current moment.

This paper argues four things. First, that theatre is not hypocrisy but the predictable product of a compliance-led response to reform. Second, that it is diagnosable, if you know the signs. Third, that it carries a real and compounding cost, precisely because it is so reassuring. And fourth, that the remedy is not more structure but a different test applied to structure: does this change a decision the board would otherwise have made? I close with a practical programme for boards that want substance rather than its likeness.

2. What Governance Theatre Actually Is

Let me be careful with the term, because it is easily misheard as an accusation of bad faith. It is not. The organisations I have in mind are not cynical. Their directors are diligent, often anxious, and sincerely committed to getting governance right. Theatre, in the sense I mean, is what happens when the form of good governance is adopted faithfully while the function is left behind — not deliberately, but because the form is what the reforms make legible and the function is not.

Governance theatre is distinct from fraud, and confusing the two leads to the wrong remedy. Fraud is the deliberate falsification of what is reported. Theatre is the sincere performance of a control whose outcome is preordained. The certification is signed, but

the process behind it was assembly rather than judgement. The audit committee meets for the prescribed hours, but the material reaches it too late and too polished to be interrogated. The risk register is complete, current and beautifully maintained, and it changes nothing about where capital is placed. Nothing here is false. Everything here is hollow.

The test of governance is not whether a structure exists, nor whether it operates as designed. It is whether the structure ever changes an outcome. A control that has never altered a decision, and could not, is not a weak control. It is a costume.

3. Why the Compliance Reflex Produces Theatre

Theatre is not an accident of lazy organisations. It is the natural output of a particular, and very common, way of responding to reform. When a wave of regulation and code revision arrives with the force of the past year's, the organisational instinct is to ask: what must we now be able to show? It is an understandable question — the penalties are real, the personal exposure of directors is real, and the auditor and regulator will ask to see evidence. But it is the wrong first question, and the papers that follow from it build the wrong things.

The reasons are structural, and they recur across sectors:

- Compliance is legible; substance is not. A charter can be produced, dated and filed. A genuinely sceptical audit committee cannot be filed. Faced with a demand to demonstrate governance, organisations build the parts that can be demonstrated.
- Auditors and regulators must examine what is examinable. External assurance necessarily attaches to artefacts — documents, minutes, sign-offs, control descriptions. This is not a criticism of auditors; it is the nature of assurance. But it means the path of least resistance is to produce artefacts, and artefacts are the raw material of theatre.
- Speed favours structure over culture. The reforms arrived with deadlines. Structure can be stood up in a quarter. The habits of genuine challenge take years and cannot be procured. Under time pressure, organisations build what can be built by the deadline.
- Everyone is watching the same script. When advisers, peers and auditors all converge on the same checklist of expected structures, adopting the checklist becomes the safe move — and the checklist describes forms, not behaviours.

Put these together and theatre is not a failure of the response. It is the response, when the response is led by the compliance question alone.

4. The Evidence: What Theatre Looks Like Up Close

Because theatre is sincere, it hides in plain sight. But it leaves marks, and a board willing to look honestly at its own workings can find them. Across the organisations I have observed adapting to the new environment, the same diagnostic signs recur.

Sign	What you see	What it reveals
The unopposed sign-off	Certifications and approvals that are never withheld, qualified or delayed	The control validates; it does not decide
The polished pack	Board and committee papers arrive complete, confident and late	Material is presented to be received, not interrogated
The standing register	A risk or issue log that is meticulously maintained and rarely acts on a decision	Risk is documented, not governed
The vocabulary of objection	New control language used mainly to slow or refuse, never to improve	Structure has become defensive, not generative
The absent counterfactual	No record of a decision the new governance actually changed	The performance runs, but nothing turns on it

The last sign is the decisive one. When I sit with a board that has invested heavily in its post-reform governance and ask a simple question — name one decision this new apparatus caused you to make differently — the quality of the answer tells me everything. In the organisations building substance, the answer is immediate and specific. In the organisations building theatre, there is a pause, and then a description of the apparatus itself. The apparatus has become the answer to a question about outcomes. That substitution is the whole of the disease.

5. Why Structure Satisfied the Auditor but Not the Board

There is a reason the phrase that best captures this moment is structures that satisfied auditors but not boards. The two audiences are asking different questions, and a structure can pass one while failing the other.

The auditor — and I mean this as a description of the role, not a complaint about it — asks whether a control is designed appropriately and operating as designed. Both can be true of a control that never changes anything. A quarterly review that always concludes no action required is, from an assurance standpoint, operating perfectly. The auditor's satisfaction is real and legitimate within its remit.

The board's question, if the board is honest, is different and harder: are we, because of this, deciding better than we did before? This question cannot be answered by inspecting the control. It can only be answered by the directors' own knowledge of their deliberations — whether the debate is sharper, whether uncomfortable information now reaches them in time, whether they have declined or reshaped anything they would previously have waved through. This is why so many directors will privately admit what they would never minute: that the new governance looks impressive and feels empty. They are satisfying the auditor and failing themselves, and they know it.

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6. The Cost of Theatre

If theatre were merely wasteful — an overhead, a tax of paperwork — it would be a manageable problem. It is worse than that, because theatre does not sit inertly alongside good governance. It actively displaces it, and it does so through the mechanism that makes it attractive: reassurance.

1. It manufactures false confidence. A board that has built impressive structures believes itself well governed. That belief is itself a risk, because it lowers vigilance precisely where vigilance is most needed. The most dangerous board is not the one that knows it is weak; it is the one that is weak and believes it is strong.
2. It consumes the scarce resource of attention. Directors and executives have a finite budget of time and seriousness. Every hour spent maintaining apparatus that changes nothing is an hour not spent on the judgements that do. Theatre is expensive not mainly in money but in the diversion of the organisation's best attention toward its least consequential activity.
3. It hardens into culture. A control that is performed rather than exercised teaches everyone who operates it that governance is a ritual to be completed, not a discipline to be practised. Repeated across quarters, the lesson sets. Restoring substance later means fighting a culture the organisation trained itself into.
4. It fails exactly when it is needed. Theatre works in calm weather, because in calm weather no control is truly tested. Its emptiness is exposed only when a real decision, a real risk, a real dissent arrives — which is to say, at the one moment governance exists for. A costume protects no one in the storm it was bought for.

The compounding of these costs is what makes theatre more than an inefficiency. An organisation can survive weak governance it recognises as weak. It is far more exposed by hollow governance it mistakes for strength.

7. What Substance Would Require

The remedy is not to dismantle the structures. Most of them are, in themselves, sound — independent audit committees, honest certification, documented controls and clear charters are the right furniture for a well-governed enterprise. The error is to believe that assembling the furniture is the same as living in the house. Substance requires a different discipline layered onto the structure, and it begins with a change of question.

The compliance question is what must we be able to show? The substance question is what must we now decide differently? A board that leads with the second question builds the same structures but uses them for a different purpose, and the difference is visible within a single reporting cycle. In the organisations making this shift, I see a consistent set of practices:

- They subject every new structure to the counterfactual test. For each committee, control or routine, they ask: what decision has this changed, or could it change? A structure that cannot answer is either redesigned until it can, or retired. Nothing is kept merely because it looks expected.
- They engineer challenge deliberately. Substance depends on someone in the room being both willing and able to say no, and being heard. That does not arise from a charter. It is built through the composition of the board, the independence and expertise of its members, the timing and rawness of the information they receive, and

a chair who protects dissent rather than smoothing it away. Higgs and Smith point squarely at these behavioural conditions; the risk is that organisations adopt their structural recommendations and ignore their behavioural ones.

- They move information upstream and leave it rough. Theatre thrives on the polished, late pack that can only be received. Substance requires that boards and committees see the difficult material early, in draft, while it can still change an outcome – and while it is still uncomfortable enough to provoke real questions.
- They treat internal control as management thinking, not a documentation exercise. The control framework the profession has relied on since the early nineties was always meant to make organisations reason about risk, not merely catalogue it. Turnbull said as much for the British market. The substance test for any control is not is it documented? but has it ever caused management to act?
- They keep a record of what governance changed. The single most clarifying discipline I have seen is a standing note, reviewed by the board, of the decisions its governance actually altered in the period. Where the note is full, substance is present. Where it is thin, the board has caught its own theatre before the storm did.

8. A Recommendation Boards Can Act On

For a board that suspects it has built more theatre than it would like to admit, the path forward does not require another wave of restructuring. It requires an audit of a different kind – not of the controls' design, which the external auditor already examines, but of their consequence, which only the board can examine. I recommend three concrete steps, in sequence.

1. Run a consequence audit. Take each significant governance structure erected in response to the past year's reforms and require, in writing, one decision it has changed or is capable of changing. Structures that pass are affirmed. Structures that cannot answer are flagged – not abolished reflexively, but marked for redesign toward a decision they could influence.
2. Rebalance the investment. Wherever the audit reveals structure without consequence, shift effort from maintaining the apparatus to strengthening the conditions of judgement behind it: board composition, the independence and expertise of challenge, the timing and candour of information, the protection of dissent. These are harder to build and impossible to file, which is precisely why they were skipped.
3. Institute the change-log. Adopt the standing record of decisions that governance altered, and review it at each cycle. It is the cheapest and most honest instrument a board has for telling substance from performance, because it cannot be satisfied by structure alone.

None of this is in tension with the letter of the reforms. A board that governs with substance will clear every compliance bar with room to spare, because genuine challenge produces exactly the evidence the auditor seeks, as a by-product rather than a purpose. The reverse is not true: a board that clears the compliance bar may still be governing itself with scenery.

9. Conclusion

The reforms of the past year are a genuine advance, and the organisations rebuilding their governance in response deserve credit for the seriousness of their effort. But seriousness of effort is being spent, too often, on the wrong object. We are building structures that can be shown and mistaking them for governance that is exercised. The auditor is satisfied; the board, in its honest moments, is not.

The distinction that matters in this moment is not between organisations that have reformed and those that have not — nearly all have. It is between those whose reforms changed how they decide and those whose reforms merely changed how they appear. The first are safer than they were a year ago. The second are more exposed, because they have added to weak governance the most dangerous ingredient of all: the confidence that it is strong. The work now is not more structure. It is the harder, unfileable work of making the structure we have already built actually decide something.