Testimony
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The Conference Board

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I would like to thank the Committee for the opportunity to discuss The Conference Board's program on Corporate Governance Best Practices. After having spent eight years at The Congressional Research Service, as head of the Industry Analysis and Finance Section of the Economics Division, it is a pleasure to return to Capitol Hill today.

I first started analyzing corporate governance issues at CRS during the "takeover wars" of the early 1980s.[1] Then, in 1987, I co-founded, along with Ira M. Millstein and others, the Columbia Law School Institutional Investor Project, where I devised the methodology widely used today for tracking U.S. institutional investor assets, equity holdings and turnover and trading patterns. Subsequently, I founded The Global Corporate Governance Research Center after I arrived at The Conference Board in 1993.

The Conference Board's Global Governance Research Center is, to ensure objectivity, comprised of both major global corporations and institutional investors who gather together for seminars and to sponsor and oversee our research program (see Appendix 1 for a description of the Center and its research).

The Conference Board is a not-for-profit business membership organization, founded in 1916 to enhance the role of business in society. We now have more than 3,000 members in more than 62 countries of the world. We are non-advocacy and share "best practices;" therefore, do not make recommendations for or against any legislative proposal. At our Governance Center, we work extensively with companies on corporate governance matters and, in conducting our work, we hold confidential meetings, briefings and research interviews. If we wish to quote any company or executive, we must obtain written clearance permission; therefore, I am not at liberty today to refer to any corporation or executive unless they have participated in our research/clearance process.

I am, however, pleased to respond to the committee's request for an overview of:

1. the responsibilities and skills required of corporate directors;
2. board processes to ensure board effectiveness with special attention to methods directors can use to monitor corporate performance;
3. issues confronting directors who are obviously not full time with a company yet must "monitor" and "oversee" company activities.

[1] While at the Congressional Research Service, I authored numerous CRS and committee prints on Greenmail, Mergers & Acquisitions, Leveraged Buyouts, Junk Bonds, Institutional Investors, etc.

Enron: A Sea Change in Corporate Governance

Before examining the responsibilities, skills and board processes, a word about Enron is appropriate. I believe that, when the debate is concluded, the Enron bankruptcy will be seen as having caused a sea change in corporate governance generally and in how directors view their roles specifically. To this end, The Conference Board is undertaking a major Director/Senior Executive Roundtable project, with meetings to be held at Stanford Law School and the University of Delaware's Center for Corporate Governance which will invite input from the Delaware Chancery and Supreme Courts. The final meeting for this project will be held at TIAA-CREF (see Appendix 2).

We define "corporate governance" as a system of checks and balances between the board, management and investors to produce an efficiently functioning corporation, ideally geared to produce long-term value. Our global research at The Conference Board leads us to conclude that corporate governance models do not vary by country, e.g. there is no one "U.S." model of corporate governance compared to an "Asian" model, or a "European" model. Governance systems are largely determined by the ownership structure of the company, regardless of its global geographic location. Moreover, "best practice" elements, such as the number of "independent" directors, will vary depending on certain key ownership structures such as:

- Companies with widely held and dispersed shareholders;
- Companies which are closely held by blocks of investors;
- Companies which are family-owned businesses; and
- Newly privatized businesses where the government retains a residual investment.

Although each country's regulatory and corporate law system will shape the specifics of its corporate governance, our research finds a trend towards general convergence in global governance standards reflecting the following general principles:

- Director independence and effective oversight;
- Accountability to shareholders;
- Transparency and disclosure; and
- Protection of minority shareholder rights.

Thus, the Committee's focus on director responsibilities is central not just to U.S. governance but to global governance developments as well.

Corporate governance, as we think of it today, unfortunately started in an adversarial vein. Its first stage was prompted by attempts on the part of certain companies in the early 1980s to pay "greenmail" to get raiders to withdraw their hostile takeover bids. This raised concern on the part of large institutional investors such as the California Public Employees' Retirement System (CalPERS) that management was acting in its own behalf rather than for the benefit of shareholders. Numerous proxy voting efforts ensued as activist public pension funds used the proxy to sway public opinion and to attempt to influence management. A second wave of governance activism occurred during the late 1980s when individual investors such as CalPERS and the New York State Common Retirement Fund made more direct contact with management. They asked companies such as General Motors to provide information on specific board processes such as CEO succession.

Having used the proxy as a surrogate measure to try to improve board effectiveness, these investors now went straight to management with varying success. Certain companies did formulate corporate governance guidelines, and investors produced a "report card" on their efforts. But governance, as it developed throughout the 1990s, still tended to be generally more in response to external pressures than as a means company managements and boards universally saw would lead to improvements in their internal processes. External pressures included:

- Dialogue, media and voting pressures from investors;
- Pressures from the SEC requiring more disclosure especially in the area of executive compensation;
- Pressures from stock exchanges amending their listing requirements especially with regard to audit committees procedures and definitions of independence;
- Legislative pressures such as changes in the IRS code provisions 162(m) limiting the deductibility of executive compensation; and
- Pressures from the courts, especially those in Delaware, forcing directors to look more carefully at their roles.

It is fair to say, however, that many boards have begun to embrace good governance, although the collegial format that is the basis for board interaction tends to discourage open disagreement. Change therefore tends to come either if there is an individual director/CEO/senior executive who is a corporate governance champion or if there is a crisis. With Enron, I believe that companies are no longer looking upon corporate governance as something thrust upon them from the outside. In every boardroom around the country, directors are asking themselves questions such as:

- What processes do we need to put in place to make us more aware of "red flags" in company operations?
- How do we fulfill our monitoring role and yet rely on management and external accountants?
- How can corporate governance processes be used to help keep our company viable and restore public confidence in our accounting, lines of business, etc.?
- How will instituting corporate governance best practices reduce corporate risk?

Thus, corporate governance has finally moved from an external imposition to something boards can not afford to dismiss if they want to provide internal efficiencies in running the corporation and if they want properly to manage risk.

A. The Responsibilities and Skills Required of Directors

Corporate governance best practices are based on two basic legal requirements that shape director actions:

(1) **the duty of care** to be informed and exercise appropriate diligence in making decisions and to oversee the management of the corporation; and
(2) **the duty of loyalty** to put the interests of the corporation before those of the individual director.

According to the American Bar Association, the board's responsibilities include:

- reviewing and monitoring fundamental operating, financial and other corporate plans, strategies and objectives;
- selecting, regularly evaluating and fixing the compensation of the chief executive officer ("CEO") and the most senior executives;
- developing, approving and implementing succession plans for the CEO and the most senior executives;
- evaluating the performance of the corporation and its most senior management and taking action, including changing corporate plans, strategies and objectives and replacing management, when appropriate;
- adopting policies of corporate conduct and monitoring compliance with those policies and with applicable laws and regulations, as well as the adequacy of accounting, financial and other internal controls;
- reviewing the process of providing appropriate financial and operational information to decision makers (including board members) and shareholders; and
- evaluating the overall effectiveness of the board and its composition.[2]

The ABA Guidebook notes that, to be effective, a director should become familiar with the corporation's business to acquire sufficient knowledge to enable him/her to make an independent evaluation of corporate and senior management performance. This will allow the director to join with other directors to make changes and to challenge, support and reward management as warranted. Accordingly, a director should have a basic understanding of:

- the principal operational, financial and other plans, strategies and objectives of the corporation;
- the results of operations and financial condition of the corporation and its significant business segments for recent periods; and
- the relative standing of the corporation's significant business segments vis-à-vis competitors.[3]

The Conference Board has done considerable research into how boards work and has produced a practical Handbook, *Determining Board Effectiveness: A Handbook for Directors and Officers.* This Handbook has been used by numerous boards to facilitate discussion of their best practices and serves as the basis for a 10 step program on Board Effectiveness described in the next section of this testimony.

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[2] Section of Business Law, American Bar Association, Committee of Corporate Laws, *Corporate Director's Guidebook,* 3rd, 2001, p. 4.
[3] ABA Guidebook, p. 5.

Boardroom dynamics are difficult to prescribe, as groups of people gather together to make informed decisions about the direction of the company. The level of knowledge, integrity and independence necessary to carry out the functions of director are difficult to summarize, but, based on our case study approach, The Conference Board Handbook describes the "behavioral" characteristics of a good director as follows:

- asks the hard questions
- works well with others
- has industry awareness
- provides valuable input
- is available when needed
- is alert and inquisitive
- has business knowledge
- contributes to committee work
- attends meetings
- speaks out appropriately at board meetings
- prepares for meetings
- makes long-range planning contribution
- provides overall contribution

B. Effective Board Processes

In defining a system of board practices that leads to board effectiveness, the Conference Board's Handbook makes clear that:

> **Instituting governance best practices will provide the company with an INTERNAL effectiveness structure and a tool to manage corporate risk.**
> **The key to accomplishing this is to make certain that the company's board is managed as well as the company itself is managed.**

Each board will be run differently according to the company's stage of development, ownership structure, size, mix, composition and personalities of the board. The "one size doesn't fit all" rule clearly applies. On the other hand, there are basic legal requirements as noted above, as well as "management" skills which boards can and should adopt no matter its configuration. The Handbook poses fundamental questions boards should ask themselves:

- Is our board managed as well as our company is managed?
- Does our board have the strengths it needs to achieve our strategic goals?
- How well does our board track our company's success in reaching goals?

In undertaking an assessment of their effectiveness, boards should collaborate, with input from management, to respond to the 10 questions that follow.

1) How Does Your Board Define Its Role and Duties? Prioritize Its Responsibilities?

- agree on the role of the board versus the role of management
- vary specifics of board's role with size, stage and strategy of company and talents and personalities of CEO and board
- discuss role of the board in monitoring strategy openly and regularly with CEO and in executive board session
- focus on oversight not micromanagement
- spend one "retreat" session per year on strategic oversight
- focus on creating long-term value

2) Does Your Board Have Sufficient "Independence" To Perform Its Duties?

- independence leads to objectivity in monitoring management
- notwithstanding definitions of "independence" by stock exchanges on paper, in reality, independence means the ability to ask the hard questions
- directors should exercise independence in reviewing actions by auditors & compensation consultants even if they are initially chosen by management
- all external experts such as auditors and compensation consultants should know that, on matters pertaining to the board, they are responsible to the board

3) Does Your Board Have the Right Size and Structure?

- tailor size of the board to the needs of the company and its stage of development
- tailor people to company goals
- develop board committee structure to best suit underlying responsibilities
- revise board committee structure as needed -- in addition to usual audit and compensation committees, some companies combine nominating committee with new corporate governance committee
- while some decisions should be taken by full board, but where committees are used, ensure that committees appropriately report to full board
- board has authority to hire experts and investigate any management activities it believes are required to fulfill board's duty of care

4) How Does Your Board Oversee Auditing And Compliance To Minimize Risk?

- ensure independent directors on audit committee with appropriate financial literacy and knowledge to ask the hard questions
- ensure audit committee charter is current
- board has responsibility to hire auditors, despite the fact that they interact extensively with management
- following the landmark Caremark decision[4], directors have affirmative requirement to ensure compliance personnel and program are in place
- external auditors should not be same as internal auditors
- board should have access to external/internal audit with management not present and should determine if there are any accounting issues which are questionable
- examine company practices with regard to whether auditors can/should perform other consulting services such as providing information technology services
- examine practices relating to whether external auditors should be rotated; examine hiring policies for "alumni" auditors
- affirm ethics program and ensure it is not suspended
- review related party transaction policies and ensure compliance among board and management to comply with duty of loyalty

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[4] According to noted legal scholar, Charles M. Elson, the board's role in ensuring corporate compliance with applicable law has expanded significantly in the past few years. The Delaware Court of Chancery, in its now infamous 1963 ruling in *Graham v. Allis-Chalmers Manufacturing Co.* [188 A.2d 125 (Del. 1963)], confirmed the traditional view that the board of a large enterprise was merely a policy-making entity and had no legal duty to enact a legal compliance program in the absence of certain warning signals. Today, the board's responsibilities in this respect are viewed entirely differently.

Boards that fail to establish effective corporate compliance procedures may face substantial liability. Two important factors are now causing boards to act prophylatically to ensure corporate legal probity:

- the creation of the federal Organizational Sentencing Guidelines, which impose more lenient treatment on companies having compliance manuals and programs; and more importantly

- the Delaware Chancery Court's landmark 1996 ruling in *Caremark International Inc.*, which imposes an affirmative duty on the board to create a compliance mechanism.

In *Caremark*, Chancellor William Allen essentially overruled *Graham*, holding that a board, as part of its duty of care, has an obligation to "exercise a good faith judgement that the corporation's information and reporting system is, in concept and design, adequate to assure the board that appropriate information will come to its attention in a timely manner as a matter of ordinary operations." As the eminent corporate commentator, Charles Hansen, has pointed out, the facts of *Caremark* suggest that some form of "information gathering and reporting system be established at a very minimum. (See decision in re Caremark International Inc. Derivative Litigation, Civ A .No. 13, 670, 1996 WL 549894, at #8 (Del. Ch. Sept. 25, 1996)).

5) How Effectively Does Your Board Monitor Company Performance?

- measure strategic activities (such as quality, intellectual capital, customer satisfaction) which matter to the success of the company
- certain new metrics may have to be created, but most companies are already collecting about 70 percent of the data they require to track strategic performance measures
- strategic measures can be tangible and intangible
- agreement among boards, management and on-line personnel as to which measures track the strategic success of the company is just as important as which measures are actually chosen
- measures should be appropriate for level of oversight - board gets important "dashboard" indicators - managers get more detailed measures

Note: Appendix 3 describes The Conference Board's computerized "Dashboard" to track strategic performance measures. The dashboard, much like the dashboard on a car, provides key measures which enable the driver to know if he is likely to get to his destination. They are not like financial reporting, which is rather like looking in the rear view mirror. A board will have perhaps only the top 5 measures to track and see if they are in the target range or below it. Managers will "drill down" into the measures and how they are tracked throughout the company.

Strategic performance measures can provide an alternative to stock based compensation, as managers might be rewarded for quality improvements, or for reducing environmental impact and increasing compliance with health and safety requirements.

Strategic performance measures may also provide "red flag" warnings when critical success factors are out of alignment. Some of these measures move from being operational to being strategically important to the viability of the company. For instance, warrantee data on certain types of tires as they are installed on certain types of vehicles, may rise above operational information to become an issue for the board relating to corporate reputation and viability.

Finally, a Conference Board survey of 113 major global corporations concludes that, when companies institute strategic performance measurement (SPM) systems, they tend to outperform their peers in stock valuation.

6) How Does Your Board Conduct The CEO Appointment And Succession Planning Process?

- hiring the CEO is the primary function of the board
- CEO succession is a primary responsibility of the board and should be a continuous process driven and controlled by the board with CEO input
- develop succession requirements from corporate strategy
- find right leader at right time
- continuously build/develop talent pool
- avoid "horse race" which leads to loss of key deputies when new CEO chosen

7) How Does Your Board Best Structure And Utilize Its Nominating Committee?

- choose only independent members
- write a charter and director selection criteria
- review skill set of whole board against strategic needs and fill gaps
- remove the "blinders" in director candidate pool
- build an independent team with a diversity of backgrounds, skills and perspectives
- professional advice can be useful to widen the pool and affirm independence
- know when to involve the CEO
- provide formal and informal orientation for new directors

8) What Is Your Board's Role In Determining Director And Executive Compensation?

- compensation committee should be entirely independent directors without CEO
- in using external advisers such as compensation consultants, they should know that they report to the board, not to management
- compensation committees should become much more involved in the strategy of the company because of option dilution and the fact that compensation is increasingly related to capital formation
- boards should be briefed on new compensation techniques, perhaps by outside experts, although companies should make effective use of internal human resources department
- director equity compensation/executive equity compensation must be reviewed in light of new developments in compensation practices
- review stock options to ensure they provide proper incentives and avoid excessive dilution
- consider strategic performance measures rather than just options in compensation packages

Note: The Conference Board recently completed a report on The Compensation Committee of the Board (see Appendix 1) which delves into the changing responsibilities of the committee and how it can deal with external compensation consultants.

9) Does Your Board Have A Process to Evaluate Whether It Is Achieving Its Goals?

- start by discussing strategy and focus the entire board on the following question: can the board help the company achieve its strategy?
- at first do it collectively not individually

    - make it collegial
    - make it confidential

    To lead the process:

    - consider Chairman
    - consider head of nominating committee
    - consider general counsel or governance officer

- 90% of companies that evaluate their boards say the process makes their boards more productive …

10) What Are Your Top 10 Best Practice and Red Flag Processes?

Based on data provided by the American Society of Corporate Secretaries two tables are constructed below. The first is the ASCS compilation of the most common board practices; the second is The Conference Board's assessment of the most frequent "red flag" practices.

Top 10 Board Practices

Rank and % companies adopting

1. Charter for Audit Committee - 97
2. Agenda item background information routinely distributed in advance of meetings - 95
3. Outside directors free to provide input to agenda - 90
4. Directors have access to management below CEO level - 88
5. Directors' compensation includes stock/stock options - 82
6. Director comp variable, dependent on meeting attendance - 79
7. Independence standard applied to screen outside directors - 79
8. Periodic board meetings devoted to overall company strategy - 74
9. Board/committee appoints committees and chairmen - 74
10. Nominating Committee plays a dominant role in the screening and selection of director candidates - 73

Top 10 "Red Flag: Board Practices

Rank and % companies adopting

1. Job description for Chairman or CEO only 50% adopting
2. Written guidelines on corporate governance - 44
3. No director with significant business sit on compensation committee - 40
4. Skills matrix to assess board composition and fill gaps when selecting new directors - 39
5. Written criteria for director selection - 37
6. No employee/former employee sit on nominating committee - 35
7. Regular meetings without CEO and management present to discuss issues other than CEO compensation - 33
8. Compensation committee charter - 30
9. No director with significant business sit on nominating committee - 24
10. Nominating/Governance committee charter - 10

C. Director Ability to Fulfill Responsibilities

While board members should be knowledgeable, and base their actions on duties of care and loyalty, some commentators have expressed concern that directors can not possibly exercise all that is required of them. In addition, some express concern that new director candidates will decline taking positions on boards in a new atmosphere of liability.

The ABA notes, however, that directors have the right to rely on others in exercising their duties:

> In discharging board or committee duties, a director is entitled to rely (absent knowledge that would make the reliance unwarranted) on management or board committees performing their delegated responsibilities. A director is also entitled to rely (absent knowledge that would make the reliance unwarranted) on reports, opinions, information and statements, including financial statements and other financial data, presented by (i) the corporation's officers or employees whom the director reasonably believes to be reliable and competent in the matters presented, (ii) legal counsel, public accountants or other persons as to matters that the director reasonably believes to be within their professional or expert competence or as to which the person otherwise merits confidence and (iii) committees of the board on which the director does not serve. A director who relies on others, however, has a responsibility to keep informed of the efforts of those to whom work has been delegated. The extent of this review function will vary depending upon the nature and importance of the matter in question.[5]

Finally, the ABA notes that directors should make inquiry into potential problems or issues when alerted by circumstances or events that indicate that board attention is appropriate.

[5] ABA Guidebook, p. 9.

APPENDIX 1

The Conference Board's Global Corporate Governance Research Center provides a unique opportunity for senior corporate executives and institutional investors to network in small, highly interactive, and non-adversarial settings. Together, these groups meet to advance cutting edge governance practices and participate proactively in landmark research on corporate governance issues. The Center's objective is to assist corporations to enhance their governance processes and thereby inspire confidence and facilitate capital formation in today's globally competitive marketplace.

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Convivium (UK)
DaimlerChrysler AG (Germany)
Deutsche Bank AG (Germany)
DSM N.V. (The Netherlands)
Electricity Supply Board (Ireland)
Hay Group (Spain)
Hermes Investment Management Ltd. (UK)
Institute of Directors (Belgium)
Norsk Hydro ASA (Norway)
Novartis International AG (Switzerland)
Powergen Plc. (UK)
Rabobank (The Netherlands)
Zurich Financial Services (Switzerland)

Affiliates and Host Organizations

American Society of Corporate Secretaries ASCS
Association of British Insurers
Australian Institute of Company Directors
Commonwealth Association for Corporate Governance
German Society of Investment Analysts and Portfolio Managers DVFA
The Institute of Chartered Accountants (in England & Wales)
Institute of Chartered Secretaries and Administrators ICSA (UK)
Investor Responsibility Research Center IRRC
National Association of Corporate Directors NACD
The National Association of Pension Funds NAPF (UK)
Pensions Investment Research Consultants Ltd. PIRC (UK)
The Royal Society for encouragement of Arts, Manufactures & Commerce RSA (UK)
The Swedish Corporate Governance Forum

Chief Governance Officers

American International Group, Inc.
Arch Chemicals, Inc.
Avon Products, Inc.
BP p.l.c. (UK)
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Computer Associates International, Inc.
CSX Corporation
Curtiss-Wright Corporation
Dana Corporation
Heidrick & Struggles International, Inc.
J.P. Morgan Chase & Company
Merrill Lynch & Co., Inc.
The Gillette Company
UtiliCorp United, Inc.

APPENDIX 1 (continued)

Research Program

Published Reports

The Compensation Committee of The Board: Best Practices For Establishing Executive Compensation	Report 1306-01-RR, 2001
Top Executive Compensation in 2000	Report 1305-01-RR, 2001
Directors' Compensation and Board Practices in 2001	Report 1304-01-RR, 2001
The Global Investor and Corporate Governance: What Do Institutional Investors Want?	Report 1297-01-RR, 2001
Corporate Governance: Global Trends Examined from an Asian Perspective	Special Report 00-2, 2000
Debating European Corporate Governance Issues	Special Report 00-1, 2000
Top Executive Compensation in 1999	Report 1281-00-RR, 2000
Directors' Compensation and Board Practices in 2000	Report 1280-00-RR, 2000
The Link Between Corporate Governance and Corporate Performance: Year 2000 Update	Report 1276-00-RR, 2000
Corporate Governance and Cross-Border Mergers	Report 1273-00-RR, 2000
Determining Board Effectiveness: A Handbook for Directors and Officers	Special Report 99-1, 1999
Aligning Strategic Performance Measures and Results	Report 1261-99-RR, 1999
Directors' Compensation and Board Practices in 1999	Report 1259-99-RR, 1999
Aligning Performance Measures and Incentives in European Companies	Report 1252-99-RR, 1999
Top Executive Compensation: Canada, France, the U.K., and the U.S.	Report 1250-99-RR, 1999
Globalizing the Board of Directors: Trends and Strategies	Report 1242-99-RR, 1999
Board Diversity in U.S. Corporations: Best Practices for Broadening the Profile of Corporate Boards	Report 1230-99-RR, 1999
The Link Between Corporate Governance and Performance	Report 1215-98-RR, 1998
Top Executive Compensation in 1998	Report 1227-98-RR, 1998
Institutional Investors and Corporate Governance	Irwin Publishing, 1997
Communicating Corporate Performance: A Delicate Balance	Report 1188-97-RR, 1997
The Corporate Board: A Growing Role in Strategic Assessment	Report 1152-96-RR, 1996
The Globalization of U.S. Institutional Investor Activism	White Paper WP-17, 1996
Directors' Retirement Benefits	Report 1161-96-RR, 1996
Corporate Boards: CEO Selection, Evaluation and Succession	Report 1103-95-RR, 1995
New Corporate Performance Measures	Report 1118-95-RR, 1995

Report Series

The Conference Board Institutional Investment Report, 3 issues per year

Issue 1: Financial Assets and Equity Holdings

Issue 2: Turnover, Investment Strategies, and Ownership Patterns

Issue 3: International Patterns of Institutional Investment

Upcoming Research Reports

Gaining Investor Confidence in India Corporates: A Handbook for Directors and Officers of Corporations in India

Gaining Investor Confidence: A Handbook for Directors and Officers of Corporations in Hong Kong

Gaining Investor Confidence: A Handbook for Directors and Officers of Corporations in Singapore

APPENDIX 2

Conference Board New Project

Director/Senior Executive Roundtable Project

Post Enron Post Mortem: Developing A Blueprint for Best Corporate Governance Practices and Early Warning Systems

Featuring Three Components:

1) **Roundtables: Directors and Senior Executives will meet in a series of Roundtables throughout the country to identify best practice improvements in corporate governance in the wake of the Enron situation.**

Participating companies can send any of their Directors and/or Senior Executives to any or all of the six Roundtable sessions:

#1	Thurs., June 13	Inaugural session at The Conference Board	New York City
#2	July (TBD)		Washington, DC
#3	Wed., July 31	Stanford Law School	Stanford, CA
#4	Sept. (TBD)	The University of Delaware's Center for Corporate Governance *	Newark, DE
#5	Sept./Oct. (TBD)		Chicago
#6	Wed., Oct. 30	Final Session – at TIAA-CREF To be held in conjunction with the Annual Fall Symposium of the Global Corporate Governance Research Center	New York City

* At Roundtable #4, Charles M. Elson, Professor of Corporate Governance at the University of Delaware, will invite input from the chancellors and justices of the Delaware Chancery and Supreme Courts.

2) **Research: Focus groups and research will supplement the roundtables to produce several products:**

- A *Best Practice Blueprint* to be produced in a final report in Fall 2002
- An on-going inventory of practice and procedural changes participating companies are instituting in response to the Enron situation.
- White-paper *Executive Action Alerts* produced as the project progresses, to flag key issues in the accounting, compliance and insurance areas.

3) **Private Briefings: If Directors and/or Senior Executives are not able to attend any of the Roundtables, or if companies wish private briefings for their Directors and/or Executives during the course of the project, these can be arranged for a fee to cover time and travel.**

Background: The "Enron effect" has reduced public confidence in corporations generally and has lead to stock price erosion, even among some leading blue-chip companies. This failure of investor confidence poses a significant threat -- not only to companies with complex corporate accounting but to the whole corporate sector.

At the same time, developing case law has put greater burdens on Corporate Directors to be proactive. Directors are no longer given wide protections under the business judgment rule; rather, they must be proactive to ensure compliance programs and to question management if "red flags" arise or if they, as Directors, should reasonably have known that such "red flags" would lead to uncovering problems.

Many of the classic corporate disasters have occurred at companies where the trappings of good corporate governance seemed to be in place. They had outside "independent" Directors -- Directors who owned stock and therefore, in theory, had interests aligned with shareholders. By all external measures, they had active and "professionally-run" audit committees and compensation committees of the Board. Although the specifics of some of these classic corporate disasters are useful to examine for their corporate governance lessons, future corporate crises will inevitably take many new and varied forms. Corporate Directors and Senior Executives should address the fundamental issues detailed below to minimize the risk of a future crisis – *whatever form it takes*.

Oversight

- What are a Director's "red flags"? How can Directors be expected to know when something is wrong?
- What control processes does the Board institute to ensure it is effectively performing its oversight role generally and in key areas, such as overseeing the strategic direction of the company?

Auditing

- What is the responsibility of the Board with regard to auditing oversight? How well does the Board monitor the integrity of the financials?
- How can the Board and Management enhance audit committee practices to ensure credibility?
- How should companies handle rotation of auditors and the appointment of internal and external auditors?
- What is the relationship between an auditor's audit and consulting practices? What oversight does the Board have to ensure objectivity with respect to the audit?

Disclosure

- Does the company need to increase its level of transparency and disclosure? If so, how?
- Does the Board have procedures to review and disclose any special financial transactions and related party transactions?

Compliance and Ethics

- Do the Board and Management have an effective system to track and monitor compliance in all the necessary and expanding areas?
- What processes and procedures do the Board and Management have in place to deal with ethics issues?
- How can companies work to reduce conflicts of interest with external constituents, such as investment banks and legal and financial service providers?

Liability

- How are the boundaries shifting with regard to what Directors are expected to know about, have fiduciary control over, and be held liable for?
- What issues are facing the Director & Officer (D&O) insurance industry with regard to the protection of Directors?
- How is the shifting legal and insurance climate affecting the ability or willingness of outside Directors to serve on Boards?

Board Management Processes

- How does the Board define and ensure Director independence?
- Does the Board have an effective structure? Does it make effective use of such committees as audit, compensation, nomination and/or corporate governance?
- Has the Board developed key measures of its own management processes and success as a Board?

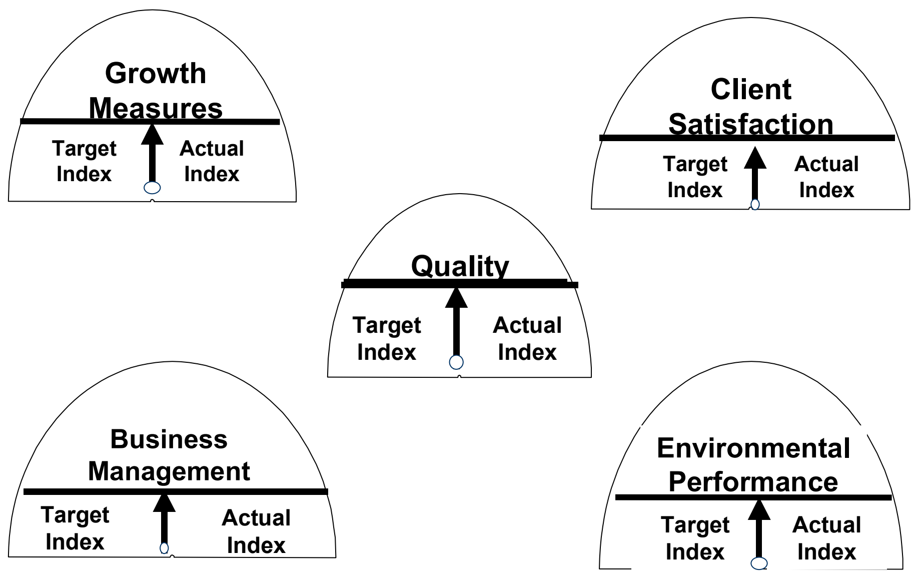
Communications

- How are Boards and Management reviewing their processes of communications to employees, shareholders and the public at large?

Note: The Conference Board Governance Center programs are ISS approved Director educational programs that provide ISS corporate governance ranking credit for companies whose Directors attend.

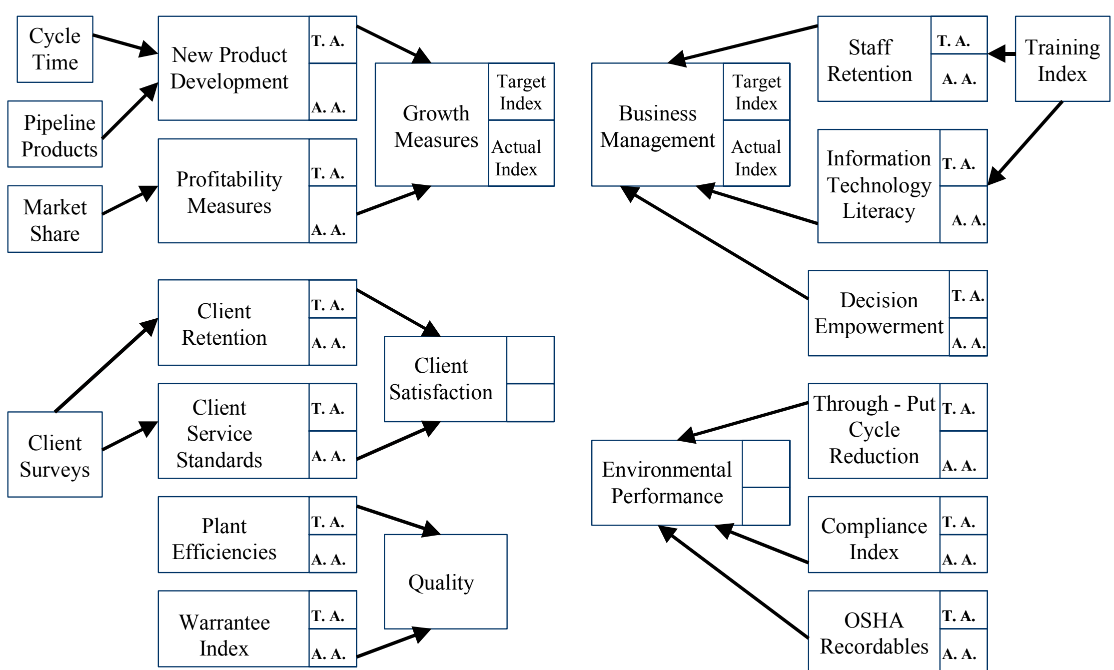
APPENDIX 3

The Conference Board's "Dashboard" of Strategic Performance Measures



Source: Global Corporate Governance Research Center

Computerized "Dashboard" To Track Strategic Measures



Source: Global Corporate Governance Research center