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What's on Your Mind?

Join Our Continuing Peer-to-Peer Exchange Exploring the Latest Corporate Governance Trends

Governance Committee Hot Topics
November 14, 2012
1:00 p.m. – 2:15 p.m.

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NATIONAL DIRECTORS INSTITUTE EXECUTIVE EXCHANGE
GOVERNANCE COMMITTEE HOT TOPICS

Panelists: Steven R. Barth, Laurie J. Champion, Thomas F. Kissinger, Mark J. Sifferlen, Peter C. Underwood, Steven W. Vazquez

Time: 1:00 p.m. to 2:15 p.m.

1. Conflict Minerals

   - Public companies must develop strategies to address conflict minerals and the related required public reporting. Such strategies should align with their respective brands and other corporate social responsibility initiatives.

   - The impact of gathering and reporting the information required for conflict mineral reporting can be costly and require a significant investment of time by both corporate and supplier personnel.

   - Public companies should seek to ensure that key stakeholders in their organizations collaborate to incorporate regulatory considerations, such as the conflict minerals reporting rules, into mergers and acquisitions, expansion plans, sourcing decisions or new product development.

   - Key compliance and monitoring programs must be well aligned with the new conflict minerals reporting rule and other social responsibility expectations, in order to ensure timely and accurate public reporting in a manner that does not damage the corporate brand.

2. Whistleblower Procedures – Compliance

   - Whistleblower mechanisms are vital components of an organization's anti-fraud and loss prevention programs; yet, implementation requires much more than setting up a toll-free number.

     - Public companies must carefully consider what features should be included in an effective whistleblower program.

     - Those overseeing whistleblower programs must determine what channels are to be employed for the reporting of information (email, telephone hotline, etc.).

     - The existence and features of a whistleblower program must be communicated effectively to individuals in an organization in order for such a program to be effective.

     - An effective whistleblower program requires that the program is supported by an organization's leadership.

     - Organizations must determine the appropriate method and extent of record keeping in order to reinforce the credibility and effectiveness of a whistleblower program.

     - The effectiveness of a whistleblower program should be evaluated from time to time by those overseeing the program and by management. Management should report the results of such assessments to the board of directors in a timely manner and suggest areas to be targeted for improvement.

3. Corruption/Bribery

- Many believe that the risk of bribery and other related violations of the Foreign Corrupt Practices Act (the "FCPA") have increased during the past five years.
- Organizations should ensure that appropriate controls are in place to deal with the threat of bribery or other FCPA violations.
- Organizations should encourage employees to report violations of the FCPA and similar laws and provide protections against the threat of retaliation for doing so.

4. Crisis Response Planning

- Boards of directors and management should place a high priority on creating and maintaining a crisis response plan, given the importance of having an effective plan when crises arise.
- A crisis response plan should designate outreach roles and messages for specific audiences (major investors, employees, the media, relevant regulators, stock exchanges, local communities).
- Boards of directors and management should consider the use of social media when preparing or updating a crisis response plan.
- Crisis response publicity firms can form an important component of a crisis response plan.
- A crisis response plan should clearly designate responsibilities, including distinguishing the role of the board of directors from that of management.
- Information security can be a critical factor in both crisis planning and response.

5. Governance Committee Oversight of ERM Governance

- It is important to establish an effective governance structure to oversee risk, including through effectively organizing the board of directors to oversee ERM and maintaining independence around the risk management function.
- It is important to approve and monitor an ERM policy that provides explicit risk-tolerance levels for key risks. This policy and the related risk-tolerance levels should seek to effectively match the board's overall risk appetite and ERM expectations.
- Organizations must evaluate the links between risk policies and compensation policies, such that compensation is structured in a manner that does not encourage the taking on of risks beyond that level acceptable to the board of directors.
- It is important to establish assurance processes to ensure that an effective ERM program is in place, including through the establishment of performance metrics for ERM and appropriate disclosure controls related to the disclosure of risk to investors, ratings agencies and regulators.

6. Ongoing Governance Committee Issues

a. Staggered Board / Annual Elections

- According to FactSet Research Systems, between 2000 and 2009, the number of S&P companies with classified boards declined from 300 to 164.
- Some view classified boards as an undue restraint on investors, activist and otherwise, to bring necessary change to the governance of public companies.
- Classified boards can form an important component of a public company's defense against coercive offers and can lead to greater stability and continuity on the board of directors.
- Some have argued that classified boards have greater independence than declassified boards.

b. Majority Voting

- There has been a trend in recent years to move to a form of majority voting for the board of directors from plurality voting.
- Some have argued that majority voting can foster better communication between shareholders and boards of directors.
- Counting "against" votes can provide shareholders with real power in determining who is elected to the board.
- Majority voting could be considered to be destabilizing to boards.
- Withhold votes can have symbolic power and an impact on corporate governance reform.

c. Overboarding

- In a report by research firm Equilar Inc., approximately 118 Fortune 1000 CEOs sit on at least three boards of other corporations, including there own.
- ISS will vote Against or Withhold from individual directors who:
  - Sit on more than six public company boards; or
  - Are CEOs of public companies who sit on the boards of more than two public companies besides their own.
- Some have argued that there is there a link between so-called busy boards (where many independent directors hold multiple board seats) and firm performance.
- Busyness may certify a director's ability and lead one to the conclusion that such directors are value enhancing.
- Overboarding can, in some instances, overstress CEOs and make it difficult for the leaders to concentrate on their "day jobs."
- In some cases, overboarded directors could detract from firm value.

- Age/term limits can come into play in dealing with overboarding.

d. Supermajority Voting Provisions

- Supermajority voting provisions are provisions in the charter or bylaws requiring a supermajority to remove directors, amend the charter or bylaws or approve major transactions, among other things. In 2011, among S&P 500 companies, there were 10 total shareholder proposals voted on relating to the elimination of supermajority voting provisions, seven of which passed. In 2012, among S&P 500 companies, there have been 9 total shareholder proposals voted on relating to the elimination of supermajority voting provisions, seven of which passed.

- Recently, there has been a decrease in shareholder proposals relating to the elimination of supermajority voting provisions.

- Supermajority voting can encourage continuity and stability on the board.

- Supermajority voting can, in some instances, better position the board to protect all shareholders from the coercive tactics of shareholders that are seeking a change in control of the company.

e. Special Shareholder Meetings

- The number of shareholder proposals relating to shareholder ability to call special meetings continued to decline to 17 in 2012, down from 30 in 2011 and 45 in 2010. Close to one-third of the shareholder proposals on special meetings passed; the average level of shareholder support of votes cast was 44%.

- The SEC permitted a number of these shareholder proposals to be excluded based on Rule 14a-8(i)(3), which allows exclusion of shareholder proposals that are "vague and indefinite." Those proposals called for an ownership threshold of 10% "or the lowest percentage of outstanding common stock permitted by state law," which language was found to be vague and indefinite. Interestingly, this was the same language in the proposals at most companies that chose the alternate route of seeking no-action relief based on introducing a management proposal.