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OPENING REMARKS

I. INTRODUCTION

We should be pleased to be here today in each other's company, a group of more than 40 attorneys who experienced corporate governance close up – not media observers and commentators. There is a reason you all have been selected as initial members of the American College of Governance Counsel - - because you've been there and done that as far as boards are concerned. You are a special group of attorneys who have seen the inside of countless boardrooms, in good times and bad, advising on decisions that can impact both the future of significant corporations and the American economy.

As the College grows, thought will be given to including more inside counsel, as well as counsel for institutional investors and others in the governance community. When the College is perceived to be representative of the broad community of lawyers who are as knowledgeable as you are, when the College reaches consensus on different issues, it will carry the weight it deserves.

Balanced and transparent experience from hands-on practitioners, will trump media stars, econometrics and the governance cottage industry.

Briefly, I see, and this is a personal view, two generic roles for the College and its experienced practitioners.

First: After debate and consideration and if we reach consensus, the College can comment on whatever new "rules" suggested by Congress, the SEC, ISS, Glass Lewis, academics or anyone else, make sense, explaining ourselves transparently. This may be a lot to ask, but who else is experienced and balanced enough to be listened to, if our process is right and transparent?

Second: After some serious interplay amongst us, we may be able to suggest means by which boards will be more capable of acting in the interest of the corporation as a whole, rather than simply succumbing to market pressures. Some market pressures may make sense, others may not. The board should sort it out, openly and transparently, in a new board-centric model of corporate governance. This will require a long-term effort, not some magic bullets, but who else to help directors get there, if that's what we believe?

Those are my hopes for the College and why I signed on.

These two generic suggestions are based on the assumption that something needs fixing in the extant functioning of corporate governance. Larry Sonsini's excellent paper, verified by this week's article in The Economist, ("American Capitalism: Reinventing the Deal," The Economist, October 24, 2015, pgs 21-24) spell out the basics for that assumption which, obviously, I support.

II. FIXING

So what is it that needs fixing? I only have 15 minutes today so I can only highlight a few of the problems.

A. Conflicts of Interest through Investment Chain

Taking a closer look at the nation's entire investment chain, it is permeated with misaligned interests and conflicting motivations at virtually every juncture.

There has been a major shift in the landscape of corporate governance during the last decade, which, as Larry pointed out, "has contributed to shareholder activism with multiple agendas." Investment managers are not always aligned with the interests of their beneficiaries. Intermediaries, such as pension funds, hedge funds, mutual funds and the like, frequently have interests which conflict with those of their beneficiaries. These intermediaries charge "rents", while serving their own, rather than their beneficiaries, interests. This is the "double agency" dilemma which academics, Jeffrey Gordon and Ronald Gilson, for example, have identified at Columbia. These conflicts have to be faced by directors who may have to sort through, understand, and balance how they proceed to act for the corporation as a whole. Dean Clark at Harvard spotted this issue long ago.

B. Everyone Knows Best – Pressure from the "Market"

Let's take a closer look at how directors might deal with the external pressures of the market as a whole.

We all know that legally, directors are subject to the business judgement rule, under which courts are hesitant to second-guess the decisions of directors and hold them liable for business decisions that while prudent when made, turned out poorly. In essence, a court will not substitute its judgment for that of the board.

But the legal standard and the market standard are not in synch. There is certainly no market presumption in favor of directors in practice today. While the courts may not, the market often will try to "substitute its judgment for that of the board." The market standard seems to almost blindly follow ALI Principles of Corporate Governance 2.01, more than actual statutory or case law, whereby the purpose of the corporation is simply to maximize profit. And that's about it. Section 2.01 needs another look.

Moreover, market pressure needs another look as well. Where does it come from? Is it based on the knowledge of boardrooms which you have, or is it often based on self-interest, or even worse, some alleged expert's view, who may have no knowledge of why a board acted as it did, but only a preconceived notion of right and wrong.

But lack of real knowledge does not stop the critic from chastising director decisions or voting against them. Again, the board has the difficult job of sorting the chaff from the wheat, and attempting to avoid a herd response. Market pressure can be positive if knowledgeable, or disruptive if not. But boards need to take a deeper look at market pressure. Is there anyone who actually votes with full knowledge of the board's action?

The growing prominence of proxy advisors, ISS and Glass-Lewis, is filling a gap for index funds who can't conceivably know each company in the portfolio. An unintended consequence of the "must vote" rule.

Proxy advisors, by publishing one-size-fits all corporate governance policies, have somehow convinced the market that they in fact know what is best for each and every corporation. Basically, they apply the same wholesale policies to EVERY corporation, without scrutinizing each corporation's unique circumstances. And because they are not in the boardroom, proxy advisors do not have any inside knowledge of the corporation. Yet, if corporations don't adopt their policies, which in essence have become "mandates", rather than guidelines, the proxy advisors may recommend against voting for the directors in the next election.

And index-style investors, often referred to as “passive” investors, have seemed to jump on the proxy advisor bandwagon. Indexers can protect themselves on the voting issue by following the advisors and blindly voting the way proxy advisors recommend.

III. WHAT CAN WE DO?

So what should boards of directors do?

This is where all of you, as trusted outside counsel to directors, come in. Boards of directors count on you for your expertise, wisdom and experience. They trust your judgment and rely on your advice when making decisions. If you are true professionals you may be one of the only ones who don’t have conflicts of interest, trying to advance your own agendas.

With our unique vantage point inside the boardroom, we have the opportunity to shape the corporate governance practices at the corporations we counsel, not only for directors, but for everyone. Certainly not easy to do. We, as professionals, can help directors move. But specifically what can we suggest? This is where our joint effort can help.

What my over fifty years of practicing law has taught me is that there never is a straight forward answer. Each board, and each corporation, is unique, and therefore the advice you give them will need to be unique based on the surrounding circumstances.

A. Board-Centric Model

We can begin the process by going back to basics. The board is at the epicenter of managing the affairs of the corporation for the benefit of the corporation as a whole, not just by law, but as a practical matter. This means that the framework for corporate governance is "board-centric" - - the board plays the central role in managing or directing the corporation. The board is the only body that is empowered to direct the affairs of the corporation. They can, and should, delegate certain matters to management. But in the end, they are the ones that are charged with running the corporation. Not proxy advisors. Not the media. And certainly not shareholders.

With the board-centric approach in mind, I suggest our job is to encourage directors to have the courage to accept their roles and responsibilities, and make decisions that they, after being fully informed, believe are in the best interests of the corporation, as a whole, rather than succumb to external pressures.

B. Building Trust - - Full Disclosure (Comply Or Explain)

Another way is to help directors garner the trust of investors so that investors realize they have choices other than blindly following proxy advisor recommendations. In the UK, directors use a comply or explain approach, where the board either complies with the governance code, or explains the reasons for noncompliance.

The comply or explain approach never really took off in the United States, maybe because of our larger financial community, or maybe because of our corporate culture. But, we, as lawyers, can certainly encourage directors to be more transparent in an effort to build a bridge between the board and investors.

There are a few corporate governance guidelines that I believe are universally recognized as best practice in America. The General Motors Guidelines is one. The NACD Blue Ribbon Commission on Director Professionalism is another. There certainly are others. We can and should encourage directors to take a close look at these guidelines, and others, as best practice. I am not saying that we should advocate that boards wholesale adopt these guidelines. Rather, carefully think about each recommendation and if deviating from the guidelines, provide explanations as to why the board chose to depart from recognized best practices. And I don't mean the types of disclosures you usually find in footnotes. I mean with clear, easy to understand explanations.

I am confident that director transparency can build trust between directors and investors, and lead to a presumption by investors that directors make business decisions on an informed basis and with the good faith belief that the decisions will serve the best interests of the corporation. It will also curtail the need for investors to blindly follow proxy advisors recommendations based on one-size-fits all policies with no inside knowledge of boardroom decisions.

I know what I am asking of you today seems like a lot. But I don't think this is impossible for us. I truly believe that most directors want to do the right thing, and want what is best for the corporation. They just need to be told, by someone they trust, how to do it.