

Lead Director Network ViewPoints

Issue 3 March 25, 2009



Responding to the changing regulatory and legislative environments

Introduction

The third meeting of the Lead Director Network (LDN) was held in Washington, DC, on March 3, 2009. Lead directors¹ met with Senator Evan Bayh (D-IN), a member of the US Senate Committee on Banking, Housing, and Urban Affairs, for a discussion of how corporate directors might interpret and respond to today's changing regulatory and legislative environments. Members also discussed their top public policy concerns. Senator Sam Nunn, a member of the US Senate from 1972 to 1996 and the presiding director of Dell, joined the discussion, providing his unique perspective as a senator and as a lead director.

The LDN brings together a select group of lead directors, presiding directors, and non-executive chairs drawn from *Fortune 500* companies for private discussions about how to improve the performance of their corporations and earn the trust of their shareholders through more effective board leadership.

ViewPoints reflects the network's use of a modified version of the Chatham House Rule whereby names of members and their company affiliations are a matter of public record, but comments made before, during, and after meetings are not attributed to individuals or their companies. Quotations from the meeting are shown in italics.² Senator Bayh has given permission for his comments to be attributed. For further information, see "About this document," on page 12.

The lead directors who participated in the meeting included:

- Peter Browning – lead director at Nucor and The Phoenix Companies
- Dan Carp – non-executive chairman at Delta Air Lines
- Pete Correll – lead director at Mirant
- Dan Feehan – presiding director at RadioShack
- Ray Gilmartin – lead director at Microsoft and presiding director at General Mills
- Bonnie Hill – lead director at The Home Depot
- Karen Horn – presiding director at Eli Lilly
- Phil Humann – presiding director at Coca-Cola Enterprises and Equifax
- Ed Kangas – non-executive chairman at Tenet Healthcare
- Bob Kidder – lead director at Morgan Stanley
- Mike Sullivan – lead director at Constellation Energy

¹ It is a practice of the network to use the term *lead director* to refer to three similar positions – lead director, presiding director, and non-executive chairman – except where otherwise stated.

² The remarks of LDN members and guests made during the meeting appear in italics; remarks made prior to the meeting are not italicized.

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King & Spalding representatives participating in the meeting were:

- George Crawford – senior government relations adviser, Government Advocacy and Public Policy Practice Group
- Lloyd Hand – senior counsel, Government Advocacy and Public Policy Practice Group
- J. Kelley – partner, Chair Corporate Practice Group
- Chris Wray – partner, Chair Special Matters and Government Investigations Practice Group

Executive summary

No American company remains untouched by the global financial downturn. The intensity of investor, public, political, and regulatory scrutiny of American companies is increasing. The potential impact on public companies is especially difficult to predict in view of Barack Obama's inauguration as the 44th president of the United States and the shift of power in the 111th session of Congress. In this context, lead directors were interested in discussing potential regulatory, legislative, and governance changes that may impact both US companies and the struggling US economy more broadly.

- **Corporate directors' top public policy concerns** *(Page 3)*

LDN members prioritized a number of key public policy concerns, including the spillover effects of the Troubled Assets Relief Program of 2008 (TARP) on executive compensation, the Employee Free Choice Act (EFCA), "Buy American" provisions, cap-and-trade legislation, and changes in taxation.

- **The board's response to regulation and legislation** *(Page 7)*

LDN members emphasized that there is no single, standardized approach that boards should take to respond to possible regulation and legislation. However, most companies, regardless of their sector, are finding it prudent to keep their boards fully informed regarding pending legislation. Boards should ensure they are aligned with management, and particularly the CEO, on public policy questions. Some members discussed the possibility of addressing the unintended, detrimental effects of certain regulation and legislation by engaging directly with legislative- and executive-branch officials, but only at the request of the CEO.

- **Corporate directors' thoughts on splitting the chairman and CEO roles** *(Page 11)*

Members revisited a key corporate governance question: when is it appropriate to split the chairman and CEO roles in US companies? Although there is currently no law or regulation that mandates this action, activist shareholders continue to press for the separation of these roles. Members of the LDN decisively reject the idea of requiring separation of the roles and believe that having an independent chair is warranted only in limited circumstances.

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Corporate directors' top public policy concerns

Both prior to the meeting and in the meeting itself, lead directors developed a list of priority issues. Lead directors report that their companies are actively monitoring these issues, and some companies have chosen to lobby Congress in support of their views.

The spillover effects of TARP on executive compensation

Members are concerned that TARP, and in particular its provisions relating to executive compensation, may have far-reaching implications for all companies, not just the financial services companies that are directly impacted. One member said, *“There is no way that these TARP provisions cannot impact the financial institutions, but the real question is the other industries. I think ISS (Institutional Shareholder Services)³ and all those other activists will recommend that [TARP provisions] flow through to airlines or railroads.”* In fact many companies, including non-TARP recipients, are experiencing spillover effects from TARP in the form of increased shareholder proposals such as say on pay, environmentally friendly provisions, and independent chairman proposals from activist investors, including certain pension funds and large unions.⁴

Monitoring federal restrictions on compensation is a top priority for LDN members: *“The real issue is designing compensation from the Senate,”* one member said. Another member stated, *“The notion of say on pay is of less concern, frankly. My concern is the Dodd amendment [restricting executive compensation for TARP recipients]. If Dodd’s provisions started to find their way into other industries, that would be a huge issue ... [The Dodd amendment] will destroy TARP recipients because top talent will flee to foreign firms.”*

Senator Dodd’s last-minute additions to the American Recovery and Reinvestment Act of 2009 (ARRA) restricted executive compensation for all companies receiving TARP money. Senator Dodd’s provisions also went beyond the White House’s TARP plan by giving shareholders of all TARP recipients, not just those receiving “exceptional” assistance, an annual non-binding vote on executive compensation. Senator Dodd’s executive pay restrictions include the following provisions for all TARP recipients:⁵

- **Bonuses, retention awards, and incentive compensation.** Provisions included in ARRA limit bonuses, retention awards, incentive compensation paid to certain employees of financial institutions receiving TARP funds. For institutions that received assistance totaling less than \$25 million, the restriction applies to the single most highly compensated employee; for those that received \$25–\$250 million, it applies to the top five employees; for those that received \$250–\$500 million, it applies to the senior executive officers and the next top 10 employees; and for those that received more than \$500 million, it applies to the senior executive officers and the next top 20 employees (or such higher number as the Treasury Secretary determines is in the public interest).

³ RiskMetrics Group acquired Institutional Shareholder Services (ISS) in January 2007.

⁴ David Ellis, “Angry shareholders demand change,” *CNNMoney.com*, February 27, 2009. Available at http://money.cnn.com/2009/02/25/news/companies/proxy_season/.

⁵ King & Spalding, “A New Era in Government Intervention,” *Client Alert*, February 23, 2009. Available at <http://www.kslaw.com/Library/publication/ca022309.pdf>.

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- **Say on pay.** Companies must institute say on pay or an annual shareholder vote on approval of executive compensation.
- **Compensation committee of the board.** The compensation committee, which must be composed exclusively of independent directors, must meet at least semiannually to evaluate employee compensation plans in light of risk posed to the company.
- **Policy regarding excesses or luxuries.** Companies must institute a policy regarding excessive or luxury expenditures, including entertainment or events, office and facility renovations, private jets, etc.
- **Compensation paid out wrongfully in the past.** The Secretary of the Treasury must review past compensation paid by TARP recipients to their top 25 employees and negotiate reimbursement if he believes those payments were not consistent with the public interest.

Under the ARRA, the Securities and Exchange Commission (SEC) has one year from the date of the ARRA's enactment to issue final rules or regulations. The ARRA legislation did not make clear whether the say-on-pay provision would be effective immediately. However, on February 20, Chairman Dodd sent a letter to Mary Schapiro, the SEC's new chair, indicating that he intended these provisions to be effective immediately after the bill's enactment.⁶ Shortly thereafter, the SEC provided additional guidance through its compliance and disclosure interpretations, which stated, "The Division staff is following the views expressed in Chairman Dodd's letter to Chairman Schapiro."⁷ The SEC must still issue final rules and regulations within one year of ARRA's enactment which will likely be subject to public notice and comment.

Senator Bayh defended these TARP provisions, explaining their importance in making the bailout more palatable to taxpayers: *"The government shouldn't normally be involved in pay, I agree, but we're talking about taxpayer money. On top of that, TARP bailout provisions were wildly unpopular. The emails were running at 20,000 to one against bailing out the financial industry. But when the Fed chair says the American financial system is going to collapse ... we had to act. The limitations on executive compensation for TARP recipients were something we had to do."*

In light of these developments, boards and compensation committees of TARP recipients as well as other public companies must reexamine many key areas of compensation. Boards are committed to providing management with the tools to properly motivate top talent, regardless of the state of the economy. However, one member stated, *"Compensating our people in this climate is going to be a huge problem."* Even prior to the passage of TARP, compensation committees and boards were considering how to address underwater options, set goals and targets for top executives, and determine peer group performance indicators.⁸

⁶ US Securities and Exchange Commission, "American Recovery and Reinvestment Act of 2009," February 26, 2009. Available at <http://www.sec.gov/divisions/corpfin/guidance/arrainterp.htm>.

⁷ Ibid.

⁸ For more details on their efforts, see Compensation Committee Leadership Network, "The economic and financial crisis: implications for the compensation committee," *ViewPoints*, February 5, 2009. Available at http://www.tapestrynetworks.com/networks/net_compensation.html.

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Employee Free Choice Act (EFCA)

The Employee Free Choice Act (EFCA) would allow workers to unionize through a “card check” process. The EFCA would require the National Labor Relations Board (NLRB) to certify a union as soon as it has secured a majority of signed authorization cards from employees, rather than by having the NLRB conduct an election by secret ballot. In addition, the EFCA would allow either the company or the new union to call for government mediation, and then mandatory arbitration, to set the terms and conditions of the union contract if the two sides cannot reach an agreement within 120 days.⁹ “Opponents have attacked the proposal’s intent to eliminate secret ballots in union elections, an idea they say is undemocratic. They also point to the weak economy ... and say the plan is especially threatening to small businesses.”¹⁰

Senator Bayh said it is unclear when this issue would likely come to a vote. Additionally, Senator Bayh said the EFCA is a divisive issue, but he believed the Obama administration was committed to “*getting something done*.” In fact on March 4, 2009, the president declared that his administration would seek passage of the Employee Free Choice Act.¹¹

Members are deeply concerned about the consequences of the EFCA’s passage into law. “*The EFCA is an enormous issue*,” one member remarked, and another noted that it is “*something we’re all thinking about*.” A director familiar with the situation noted, “*This EFCA has been around forever ... I believe President Obama will want to be saved from this provision. [But] if the EFCA passes, it will be a real problem*.” One member went so far as to say, “*This is one of the worst things that could happen to this country*.”

“Buy American” provisions

Members discussed ARRA’s “Buy American” provisions, which have attracted some controversy. In early February, those provisions sparked an international “war of words” between the European Union and the United States over the potentially disastrous consequences of a US ban on foreign imports. European leaders fear that the provisions will create an “economic Iron Curtain” and may incite a costly transatlantic trade war.¹² In response, the Obama administration has given some indication that it would not take a protectionist approach to trade. The administration has structured the ARRA to ensure that the “Buy American” provisions allow the United States to stay compliant with international trading regimes such as World Trade Organization rules. In addition, when President Obama traveled to Canada, he assured Canadian trading partners that the United States has no plans to renegotiate NAFTA.¹³

⁹ King & Spalding, “A New Era in Government Intervention,” 4.

¹⁰ Michael Fletcher, “Battle Deepens Over Union Organizing,” *Washington Post*, December 9, 2008, A06. Available at <http://www.washingtonpost.com/wp-dyn/content/article/2008/12/08/AR2008120803408.html>.

¹¹ Kris Maher, “President Tells Unions Organizing Act Will Pass,” *Wall Street Journal*, March 4, 2009. Available at <http://online.wsj.com/article/SB123611995496723249.html>.

¹² Kirsty Walker, “Obama backs down over ‘Buy America’ after EU warns him not to start a global trade war,” *Mailonline*, February 4, 2009. Available at <http://www.dailymail.co.uk/news/worldnews/article-1134608/Obama-backs-Buy-America-EU-warns-start-global-trade-war.html>.

¹³ Jamal Simmons, “Business learns the politics of hope,” *Politico*, February 26, 2009, 2. Available at <http://www.politico.com/news/stories/0209/19321.html>.

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When asked about the administration's stance on free trade and the "Buy American" provisions, Senator Bayh said, *"Protectionism is not something we are going to consider, though enforcement is important. We are a trading nation. We are going to embrace free and fair trade and stay away from a trade war."*

Members expressed two primary concerns. How, members wondered, would the United States respond if foreign governments took protectionist measures of their own that created barriers for US goods? Members also expressed concern regarding the possible unintended consequences that the "Buy American" campaign might have on the US economy and corporations. The US Chamber of Commerce released a statement further reinforcing members' concerns: "If we refuse to buy foreign-made goods, then our trading partners will refuse to buy from us. And since we are the world's largest exporter, who will be hurt more?"¹⁴

Cap-and-trade legislation

Cap-and-trade regimes set limits on greenhouse gas (GHG) emissions and allow companies to buy and sell carbon credits. "The cap-and-trade program favored by President Obama would let companies trade pollution allowances on an open market to give them incentives for reducing greenhouse-gas emissions and moving toward cleaner technology."¹⁵

A number of members mentioned the potentially deleterious effects of cap-and-trade programs on certain industries. One member said, *"Cap-and-trade could be a very regressive form of taxation."* The Congressional Budget Office estimates that "most of the cost of meeting a cap on CO₂ emissions would be borne by consumers, who would face persistently higher prices for products such as electricity and gasoline. Those price increases would be regressive in that poorer households would bear a larger burden relative to their income than wealthier households would."¹⁶

On March 3, 2009, Senator Bayh, along with 15 other senators, signed a letter to the Obama administration urging that any cap-and-trade legislation "ensure that consumers and workers in all regions of the US are protected from undue hardship."¹⁷ At the LDN meeting, Senator Bayh laid out several conditions that the administration's cap-and-trade program would have to meet in order to gain his support: *"Cap-and-trade is a very important issue. If it is not done properly, it can do a lot of harm ... 15 of us signed a letter saying we would not support the previous cap-and-trade proposal. This will hammer the states which produce electricity from coal in the industrial Midwest and parts of the South. I am opposed to cap-and-trade regulations unless we deal with three issues: first, there is a disproportionate impact on states, and it has got to be equitable. Secondly, timing is an issue. The economy is doing badly, so is this really the best time to talk about it? Thirdly, we need a verifiable way to include China, India,*

¹⁴ "Buy American Rule Proposed for Obama Stimulus Plan," *San Jose Business Journal*, February 2, 2009. Available at <http://www.bizjournals.com/sanjose/stories/2009/02/02/daily20.html>.

¹⁵ Kim Chipman and Catherine Dodge, "Obama Plan has \$79 Billion from Cap and Trade in 2012," *Bloomberg.com*, February 27, 2009. Available at <http://www.bloomberg.com/apps/news?pid=20601087&sid=aDT1Ybl.PccE&refer=home>.

¹⁶ Bruce Bartlett, "A Carbon Tax Is Better Than Cap and Trade," *Forbes.com*, March 6, 2009. Available at http://www.forbes.com/2009/03/05/obama-carbon-tax-cap-and-trade-opinions-columnists_republicans.html.

¹⁷ John Fund, "Rust Belt in Revolt," *Wall Street Journal*, March 4, 2009. Available at <http://online.wsj.com/article/SB123612861928624585.html>.

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and other developing companies ... in this cap-and-trade discussion, or our sacrifice will be dwarfed by their growth.”

A director underscored the importance of businesses’ engaging in this debate: *“It is true that coal states are really going to be put at a disadvantage in this legislation ... A staggered approach to implementing cap-and-trade as it applies to coal is important. It is crucial for businesses beyond those in coal states to engage on this topic.”*

Changes in taxation

Speaking about the administration’s proposed tax increases, one member asked, *“What about the impact of tax increases on small businesses?”* According to President Obama’s tax plan, “the top two tax rates will increase to 36 percent and 39.6 percent in 2011, up from the current rates of 33 percent and 35 percent. These higher-income taxpayers also would not receive the full value of their itemized deductions, and they would see their capital gains and dividends taxed at a 20 percent rate instead of 15 percent. That’s bad news for small business owners who report more than \$200,000 in income as individuals or more than \$250,000 as joint filers.”¹⁸

“Taxes are likely to be raised,” Senator Bayh conceded. *“The president has gone on record saying this, particularly in the highest brackets where the rates will go back to where they were eight years ago. These rates are not new – they go back to the Clinton era. I would prefer that capital gains [taxes] didn’t go up.”* Members are concerned that these higher tax rates will negatively impact not only US small businesses, but the US economy as a whole.

The board’s response to regulation and legislation

One LDN member suggested that uncertainty in the current environment is constraining the board’s ability to take action: *“It is too early to ask the question of how boards are responding. Until directors understand what this [environment of regulatory and legislative change] means, you have to wait and see what will actually happen.”* Yet many members, particularly those from regulated industries, reported more frequent discussions between boards, management, and Washington, DC, offices regarding political and regulatory matters.

No one-size-fits-all approach

Overall, members stressed that there is no standardized response for boards in the face of possible regulation or legislation: *“This isn’t a one-size-fits-all model. At my company, we don’t have many legislative issues of any consequence. We don’t spend a whole lot of time on this because it hasn’t historically been at the forefront of our conversations. We decided to upgrade the talent of our board, and ‘political influence’ wasn’t listed in any of the priorities in terms of skills or experiences from board members. You have to do what’s right for your company.”*

¹⁸ Kent Hoover, “Business Leery of Obama’s tax plans,” *New Mexico Business Weekly*, March 8, 2009. Available at <http://www.msnbc.msn.com/id/29591172/>.

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Members discussed two possible approaches to dealing with public policy issues:

- **Full board discussion.** *“We talk about a variety of issues that are specific to our industry. We talk about these on a regular basis. If you talk about what’s important to the company, you’re talking about what’s important to the directors.”* Another member stated, *“We have [instituted regulatory and legislative updates] at both my companies, but it tends to be on specific issues rather than a regular update ... pending crises are always on our agendas.”*
- **Committee discussion.** *“We have a [specific board] committee that gets the Washington representatives into our meetings at least two to three times a year to bring us up to date on all the issues that affect the company.”* Before the meeting, another member said, *“Two of the boards I’m on have our Washington office head come and brief the governance committee every time we meet.”*

Another member stressed the importance of scenario planning in advance of possible legislation or regulation: *“You must examine your risk profile, given any major legislative changes that come about. We cannot discuss card check in a vacuum, for example. We have to talk about what happens if it passes. We, as directors, have to assume that the worst possible nightmare could become reality.”*

Board responses vary by industry

Members also contrasted the reactions of companies in heavily regulated industries to regulatory and legislative developments with the reactions of companies that are subject to less regulation. In many cases, boards of companies in heavily regulated industries already have established practices for responding to possible regulation and legislation. These include systematic approaches to engaging with Washington, DC, offices and political experts and ensuring the full board or individual committees of the board consider key regulatory issues. One member stated, *“In the regulated business, you have a full board presentation at every board meeting from political people to talk about the federal and state implications of regulations.”*

Several members on the boards of companies in less-regulated industries reported that their boards are attempting to raise their awareness of regulatory matters, but one member from a less-regulated company noted with concern that *“after an extensive [enterprise risk management] process where we listed the top 20 risks for our company, neither legislation nor regulation were one of the issues [presented to the board].”*

It appears that most companies, regardless of their sector, are finding it prudent to keep abreast of pending regulation and legislation. One member said, *“We put political strategy and the interface of our company with political strategy on the [board] meeting agenda. It is interesting to see how the Washington team can focus our agenda down to the few [political] priorities ... I don’t think they’ve ever done this before. Political strategy wasn’t typically a board issue.”*

Alignment between management and the board on key public policy issues

Members discussed the importance of ensuring that management and the board communicate and share perspectives on key policy questions. One member asked, *“As a director, what happens when your views*

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on public policy conflict with the views of management? How do you reconcile that within your management team and board?”

In response, another member shared his experience in a similar situation: *“As a board, we ended up having a number of discussions about whether we’re in agreement or support of [our CEO’s position on a key legislative issue]. The board has a point of view, like all things. And we don’t tell our CEO what stance to take on an issue. We just try to keep lines of communication open.”* Another member said, *“Hopefully, before a CEO goes public on issues, he will take that discussion to the board ... Issues pop up between board meetings, and you have to be able to discuss these questions as a board with the CEO. It may be that the CEO wins out on an issue, but at least the CEO has the opportunity to help the board understand his perspective.”* A third member agreed, *“We have good communication with our CEO. And if there’s an important issue, he will take it to the full board first to hear our thoughts.”*

Potential engagement with legislators

Members considered how boards might engage with elected and administration officials to share boards’ perspectives and communicate their concerns regarding unintended but nonetheless potentially devastating consequences of pending laws and regulation on American business. One member stated, *“My concern is no one is slowing the legislative process down enough to engage in a proper debate on these issues and the implications on American competitiveness and the impact on the US globally ... It feels like [American businesses] are guilty until proven innocent. Business is being vilified. Who in Congress is looking at competitiveness?”*

For example, reductions in so-called “corporate excesses”¹⁹ are directly impacting local and state economies. One member observed, *“I was in Las Vegas a few weeks ago ... They are losing jobs and the economy is suffering there because so many companies are canceling their business trips to Las Vegas.”* Speaking to the Detroit Economic Club in February, Thomas Donohue, president of the US Chamber of Commerce, noted that “meetings and events are responsible for 15% of all travel in America [and] create more than \$100 billion in spending annually.”²⁰ As companies continue to reduce discretionary spending in response to public criticism, the losses in corporate spending may contribute to further deterioration of the US economy.

Senator Bayh encourages greater director engagement with legislators

Senator Bayh commented, *“The more people we can get to engage with you directors, the more exposure legislators get to the private sector, and the better off the legislators will be [due to an improved dialogue with the private sector].”* Members were encouraged by Senator Bayh’s announcement that day that moderate Democrats in the Senate were meeting to coordinate their response to the budget and other fiscal issues. Senator Bayh stated, *“We are all stepping up on financial issues such as the budget, health*

¹⁹ Martha Neil, “Horrified by \$20B bonus bonanza, Senator Dodd calls for Wall Street to repay,” *ABA Law Journal*, Jan 29, 2009. Available at http://abajournal.com/news/did_taxpayers_help_fund_20b_in_wall_street_bonuses/.

²⁰ Thomas Donohue, “After Stimulus: Steps Needed to Lead Us Out of Crisis And Back on the Path to Prosperity.” Speech to the Detroit Economic Club, February 12, 2009. Available at http://www.uschamber.com/press/speeches/2009/090212_tjd_stimulus.htm.

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care, and energy policy to ensure that sensible voices are heard before any major changes are made and to ensure that we have real-world solutions that work.”²¹

One day after the LDN meeting, Senator Bayh reiterated his commitment to fiscal moderation in a *Wall Street Journal* opinion piece: “Our nation’s current fiscal imbalance is unprecedented, unsustainable and, if unaddressed, a major threat to our currency and our economic vitality. The national debt now exceeds \$10 trillion ... The solution going forward is to stop wasteful spending before it starts.”²²

Members consider the circumstances in which directors may choose to engage with legislators

One member posed a series of questions about the evolving role of directors in the current political environment: “*What can we do to advance our cause as corporate leaders? Who should we be talking to? If we don’t do something, we’ll end up being passive. I think this group or maybe another group should spend some time thinking about the question, ‘Who speaks for corporate America?’*”

Members felt Senator Bayh’s leadership of this group of moderates might help catalyze more board-level engagement with Washington legislators. One member said, “*This group of moderate Democrats is heartening. This is exactly the kind of action we need.*” Another added, “*This group of 15 moderates offers the opportunity for us to sit down and talk to these senators on bailouts or corporate governance. We must examine real-world consequences on the operations of corporations.*” One director continued, “*The business community has the extraordinary opportunity to weigh in on the economic climate of America and the world. This is a bigger opportunity than we’ve ever had ... The business community can move beyond just status quo and can come up with creative solutions and playing a real role in decisions.*” One member argued that a Congress and White House controlled by the Democrats could create greater opportunity for businesses to engage with legislators because “*Republicans tended to take [the business community] for granted.*”

However, many members remain hesitant about engaging with outsider stakeholders on these topics. Speaking before the meeting, one member said, “If the CEO asks me to go up and testify on the Hill, I would do it. I would do it with the CEO or experts from the company, but I would be very hesitant to go up there on my own accord.” Typically, members report they are only asked to reach out to certain policymakers on behalf of the company if they have personal connections with those individuals.

Lead directors’ role in the changing environment

LDN members stated that their core responsibilities – providing effective advice and counsel to the CEO, board of directors, and occasionally senior management – have not changed substantively in the current environment. However, if public policy issues were not formerly on their board agenda, many lead

²¹ During a meeting on March 3, 2009, the group met to discuss “how centrists ... can assert more leverage on the major policy debates that will dominate this Congress.” Congressional reporter Manu Raju continued, “Traditionally, senators are much more independent than House members, and much less likely to organize in caucuses of like-minded colleagues. But moderate Democratic senators seem intent on shaking up the culture of the upper chamber.” Manu Raju, “Conservative Dems Choke Over Spending Increases,” *Politico.com*, March 4, 2009, 2. Available at <http://www.politico.com/news/stories/0309/19587.html>.

²² Evan Bayh, “Deficits and Fiscal Credibility,” *Wall Street Journal*, March 4, 2009. Available at <http://online.wsj.com/article/SB123612545277023901.html>.

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directors have added them. One member said, *“I am going to put these regulatory and legislative issues on my board’s agenda ... I’m thinking that EFCA is an issue for us, and other pieces of legislation could be too.”*

In light of recent public outcry over CEO compensation, members briefly discussed the possibility of having lead directors publicly defend their CEO’s compensation package. One member said, *“Lead directors can play a more significant role [in publicly defending a CEO’s compensation]. First, because we’re not perceived as overpaid, directors have a little more credibility than CEOs. I think there are communications that could go to the country from the board through their lead directors or non-executive chairmen that could be viewed as more independent and less self-serving than CEOs’ [communications].”* However, most members would only consider speaking in defense of the CEO’s compensation under special circumstances.

Corporate directors’ thoughts on splitting the chairman and CEO roles

LDN members spent a portion of the meeting discussing whether US companies should consider separating the chairman and CEO roles. Members engaged in a lively discourse on the merits of this potential governance shift, but ultimately opposed separating the two roles except in certain specific situations.

In many situations, members believe that having a separate chairman and CEO causes confusion for employees, investors, and analysts as to who is really leading the business. One member said, *“As a chairman, you must go to great lengths to ensure that the CEO, employees, and all outsiders see the chairman as the chairman of the board, not the chairman of the company. A co-leadership model is poisonous to a company.”* One member summarized the views of members: *“We value our corporate governance, and we believe the structure of a merged chairman and CEO best accomplishes our corporate governance goals. When the CEO and chairman are one role, management is aligned with the board, and the lead director speaks for the board. The lead director is able to maintain his independence.”*

Members did mention certain circumstances in which companies could consider splitting the CEO and chairman roles:

- **When a new CEO is selected.** One member said, *“I think it is appropriate to separate the chairman and CEO roles when you’re making a transition with a new CEO. With a new CEO, it’s not as if you’re taking away the ‘chairman’ title from a sitting CEO. Instead, you’re making the shift before the new CEO is in place.”* In practice, after some years as CEO, it may be a natural or planned transition for the CEO to assume the chairmanship title as well.
- **When a company is distressed and outside stakeholders advocate the split.** A member recalled, *“We were in a terrible situation. We were close to shutting down [our company]. It was important [to have] a strong chairman to meet with stakeholders and others to stabilize the company.”* Another member said, *“If a creditor’s committee or the government demands a separate chairman, that is one time where you’ve got to do it, at least for a while. You have to address the perception issues it creates when you don’t separate the chairman [and CEO titles].”*

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The issue may gain greater prominence in the coming months, given, for example, that The Corporate Library predicts that companies will see “a significant rise in proposals that limit CEO power by splitting the CEO and chairman roles.”²³ As a result, LDN members will continue to discuss it. As one member commented, *“I think [splitting the chairman and CEO roles] is something we should be talking about. Even though this issue isn’t the drumbeat we might have expected it to be, it is important for us to look at it. It could be an emerging topic.”*

Conclusion

As the government grows increasingly involved in American business over the next four to eight years and as businesses seek to recover from the financial crisis, lead directors and boards are striving to respond appropriately and improve company performance in a very dynamic and challenging environment. Members discussed the implications of various pieces of legislation and regulation for American businesses and concluded that boards needed to focus on political developments as part of their role in developing strategy. While lead directors believe management and the CEO should take the lead on issues of politics and public policy, lead directors can provide value to their companies by ensuring the quality of internal discussions among directors and management on these topics.

About this document

ViewPoints is produced by Tapestry Networks to stimulate timely, substantive board discussions about the issues confronting lead directors. The ultimate value of *ViewPoints* lies in its power to help all constituencies develop their own informed points of view on these important issues. Anyone who receives *ViewPoints* is encouraged to share it with those in their own companies and with their colleagues at other companies. The more board members, members of management, and advisers who become systematically engaged in this dialogue, the more value will be created for all.

The Lead Director Network (“LDN”) is sponsored by King & Spalding and convened by Tapestry Networks. The LDN is a group of lead independent directors, presiding directors, and non-executive chairmen drawn from America’s leading corporations who are committed to improving the performance of their companies and to earning the trust of their shareholders through more effective board leadership. The views expressed in this document do not constitute the advice of network members, their companies, King & Spalding, or Tapestry Networks.

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²³ Annalisa Barrett, “What to Expect for Proxy Season 2009,” *Analyst Alert*, December 4, 2008. Available at <http://www.directorship.com/stuff/contentmgr/files/3/79097ca4cd106c4a1a753ced61b025e0/misc/corplibrary.pdf>.