Prepared Remarks of Douglas K. Chia, Executive Director, Governance Center, The Conference Board to the Rutgers Center for Corporate Law and Governance 2016-17 Opening Session, Newark, New Jersey, September 14, 2016

THE ROLE OF BOARDS

Help Wanted: Public company board member

Job Description: Evolving and open-ended

Expectations: Wide-ranging and subject to change

We already talk a lot about the role of the board. We talk about the fiduciary duties and the business judgment rule. There is robust case law in this area. And there are already people much smarter than me who have taken a pretty good stab at defining the role of the board. Being the good lawyer that I am, I sat down and did some serious legal research into this… by doing a bunch of Google searches. Here are some of the things I found:

Here's something that was written in 1971:

> *directors serve as a source of advice and counsel, serve as some sort of discipline, and act in crisis situations*[1]

Here's something that was written in 1992:

> *set strategy, corporate policies, overall direction, mission, vision*[2]

Of course, I had to consult with the ultimate legal authority… Wikipedia[3]:

- *governing the organization by establishing broad policies and setting out strategic objectives;*
- *selecting, appointing, supporting and reviewing the performance of the CEO;*
- *terminating the CEO;*
- *ensuring the availability of adequate financial resources;*
- *approving annual budgets;*

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[1] Mace, Myles L. 1971. *Directors: Myth and Reality*. Boston: Harvard Business School Press, p. 178.

[2] Demb, Ada, and F. Friedrich Neubauer. 1992. *The Corporate Board: Confronting the Paradoxes*. Oxford; New York; Toronto and Melbourne: Oxford University Press, p. 44.

[3] *https://en.wikipedia.org/wiki/Board_of_directors*

- *accounting to the stakeholders for the organization's performance;*
- *setting the salaries, compensation and benefits of senior management;*

And here's something I found at a site called "Free Advice"[4]:

> *governing the organization by establishing its mission, policies and objectives; selecting, appointing, supporting and reviewing the officers; approving annual budgets; and accounting to the shareholders for the corporation's performance.*

So, you notice some similarities and some differences. What probably matters more than what is published on the subject is what people who are actually in the game think… investors, CEOs, general counsels, corporate secretaries, other thought leaders, and the directors themselves. But, I've found that when you ask these people "What exactly is a board member supposed to be doing in that job?" you get a huge range of responses.

On the one extreme, you have directors who see themselves in the very traditional role. "Noses in, fingers out." Deferential to management. For these people, they see their primary job as acting as an advisory group or sounding board to the CEO, and the heavy lifting comes when they have to pick a new CEO or faced with some kind of major M&A decision. If you suggest that they should meet with investors from time-to-time—since that's who elected them to be there—they get kind of indignant and tell you "That's not part of the job description." Investors who hear that are absolutely horrified. You all know the kind of director I'm talking about, and they are not a small minority.

On the other extreme, you have investors who think it's entirely appropriate to have directors decide how many breadsticks should be on the table and how much salt should be on each breadstick. Sounds crazy, but that's a real-life example.

Some investors want to put directors on the board who have their own separate staffs reviewing the board materials and presenting management with alternative business strategies—kind of like having a third-party consulting firm in the boardroom. And they think it's OK for some shareholder to pay certain of those directors extra for… who know what.

Some thought leaders think the board should be composed of a group of experts on specific subjects. You can find articles entitled "Why every board needs a _______ expert." Cyber-security, sustainability, supply chain, climate change, compliance, social

[4] *http://business-law.freeadvice.com/business-law/corporations/directors_officers.htm*

media, block chain… you name it. This is what I call the *baseball team* approach to board composition. "We need a power-hitting third-baseman." You sign one. "We need a left-handed middle-inning relief pitcher." You trade for one. I like to look at boards as *volleyball teams*. Every player on a volleyball team needs to know how to play every position. Each one has a certain strength—some are good servers, some are good spikers—but everyone has to rotate and play every position.

And then there are the thought leaders who, whenever something goes wrong at a company, they ask "Where was the board!?! They weren't doing their job! They were asleep at the wheel!" Compliance violation by a group of employees in Mexico? "Where was the board!?!" Cyber-breach? "The board didn't do enough to prevent it!" Large settlement with the government? "This is a poorly-governed company. Let's sue all the directors!" When you listen to these people, it's as if the directors are supposed to be cops on the beat being tasked with preventing anything bad from happening.

As you can see, this is an incredible range of views and expectations about the job of people who are not company employees and who meet as a group about six to eight times each year. And these are the views of people who are players in the system—the thought leaders. If you ask members of the media or the general public… or politicians… their expectations add a whole other dimension to this, and that's becoming more and more relevant.

The fact is that the role of the corporate director has been evolving for some time. Structural changes in our capital markets have contributed to this. Over the past 50 years, we've seen a dramatic shift in the ownership of public companies from individual retail shareholders to institutional investors, especially at the largest companies. That's definitely had an effect on what's expected of boards. Major corporate crises and the reforms in their aftermath have also impacted what's expected of boards and created cottage industries for governance professionals advising boards. Enron, WorldCom and Tyco led to Sarbanes-Oxley. Lehman Brothers, Bear Stearns and AIG resulted in Dodd-Frank.

One of the major governance reforms of Dodd-Frank was "proxy access," and that became a subject of fierce debate and long, drawn-out lawsuits. The fight over proxy access is in essence a fight over who has the right to choose who gets to sit on boards. The basic theme of my remarks today came to me when I was moderating a Conference Board event in Washington, DC about a year and a half ago.[5] The subject was proxy access. During the course of the discussion, there was talk about what kinds

[5] The Conference Board Governance Center Corporate/Investor Summit, Apr. 1, 2015, Washington, DC.

of people would be nominated using proxy access. There was talk about expectations. And people expressed a range of ideas similar to what I just outlined to you. At certain points, I thought to myself, "Do these smart folks really think that's what board members are supposed to be doing?"

At the end of the discussion, the organizers asked me to talk about what I thought was the biggest take-away from the discussion. And that's when it came to me. So, I said something like this: "We need to have a serious discussion on what exactly directors are supposed to be doing and come to some kind of common understanding. Some of you are describing a very different job than what it's been up until now. And maybe that is what we want going forward, but if that's the case, someone needs to explain that to the directors. We're spending all of this time debating who should have the right to appoint people to the board when *we can't even agree on what the job description is*!"

And so that was my number one idea I wanted to pursue when I started in this job at The Conference Board earlier this year: "What is the job description of the director? What are these people actually supposed to be doing?" There's no roadmap out there. There's the case law, but there's no real statutory guidance. There are various white papers and blue ribbon commission reports, but those are very high-level and give very general direction. And, due to the nature of how those things typically come together, some of them end up being lists of lofty aspirations or platitudes.

We need to have a real discussion in the marketplace about this. Of course, there's not going to be one answer. It's going to be different depending on what a company is facing—a company in a turnaround situation is going to need a board that's much different than a company that's running smoothly. The maturity level of a company is also going to matter—the board of a start-up company may have a very different job from a company that has been around for generations. And it may even be different for different industries. What we need is some kind of consensus on how we look at the job. You're never going to get everyone to agree, but it would help if we had some kind of principles that structure how we think about this in practice and analyze different situations.

And it's not only the governance types who need this. The directors need direction. They need to understand what is expected of them. They need to know what the job is and what they are tasked with doing.

I think it would be interesting for a board to begin the year by sitting down and having the chair or lead director ask, "What is our role here? What are we supposed to be doing for this company?" And then see what comes from that discussion. How many boards to do you think have actually done that?

I think this subject is so important because a lot of the issues we debate in corporate governance today trace back to this basic gap in the understanding of what the board's role is for things like:

- Time spent on strategy versus monitoring and compliance
- Shareholder engagement
- Risk management
- Product quality and safety
- Sustainability
- Political spending
- Board composition and diversity
- Financial reporting
- Cyber-security
- Compensation

… and also whether the chair and CEO roles should be combined or separate, what committees the should board have, who should be on those committees, etc. Unless we are able to find some common understanding on the job of the director, progress on these debates in corporate governance will be limited. That's how fundamental this is.

And, so, I plan to continue thinking and talking about this subject from my perch at The Conference Board, and I invite you to join me in the discussion. That concludes my remarks for this evening. Thank you for having me.