



Business Roundtable™

**Principles of Corporate Governance  
2010**

April 2010



## Business Roundtable™

Business Roundtable ([www.businessroundtable.org](http://www.businessroundtable.org)) is an association of chief executive officers of leading U.S. companies with more than \$6 trillion in annual revenues and more than 12 million employees. Member companies comprise nearly a third of the total value of the U.S. stock markets and pay more than 60 percent of all corporate income taxes paid to the federal government. Annually, they return more than \$167 billion in dividends to shareholders and the economy.

Business Roundtable companies give more than \$7 billion a year in combined charitable contributions, representing nearly 60 percent of total corporate giving. They are technology innovation leaders, with more than \$111 billion in annual research and development spending – nearly half of all total private R&D spending in the U.S.

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## Foreword and Introduction

Business Roundtable is recognized as an authoritative voice on matters affecting American business corporations and, as such, has a keen interest in corporate governance. Business Roundtable is an association of chief executive officers of leading U.S. companies with more than \$6 trillion in annual revenues and more than 12 million employees. Member companies comprise nearly a third of the total value of the U.S. stock markets and pay more than 60 percent of all corporate income taxes paid to the federal government. Annually, they return more than \$167 billion in dividends to shareholders and the economy. Business Roundtable companies give more than \$7 billion a year in combined charitable contributions, representing nearly 60 percent of total corporate giving. They are technology innovation leaders, with more than \$111 billion in annual research and development spending — nearly half of all total private R&D spending in the U.S. Only through sustainable, non-inflationary, long-term economic growth will America's citizens, communities and companies remain competitive in the rapidly changing international economy. Business Roundtable asserts that to do this, the United States must create policies that foster a flexible and available workforce, sustainable cost structures and fair rules.

Business Roundtable has long been a leading advocate of best practices in corporate governance. Past publications of Business Roundtable that have addressed corporate governance matters include *Principles of Corporate Governance* (May 2002, November 2005), *Executive Compensation: Principles and Commentary* (November 2003, January 2007), *The Nominating Process and Corporate Governance Committees: Principles and Commentary* (April 2004) and *Guidelines for Shareholder-Director Communications* (May 2005). Other publications from Business Roundtable that have addressed corporate governance include *Statement on Corporate Governance* (September 1997), *Executive Compensation/Share Ownership* (March 1992), *Corporate Governance and American Competitiveness* (March 1990), *Statement on Corporate Responsibility* (October 1981) and *The Role and Composition of the Board of Directors of the Large Publicly Owned Corporation* (January 1978).

Since November 2005, when Business Roundtable last updated its *Principles of Corporate Governance*, U.S. public corporations have continued to adopt best practices within the framework of strengthened securities market listing standards and legal requirements that developed beginning with the passage of the Sarbanes-Oxley Act of 2002. More recently, in the wake of the financial crisis, corporations have navigated an extremely challenging economic environment.

Business Roundtable continues to believe, as we noted in *Principles of Corporate Governance* (2005), that the United States has the best corporate governance, financial reporting and securities markets systems in the world. These systems work because of the adoption of best practices by public companies within a framework of laws and regulations that establish minimum requirements while affording companies the ability to develop individualized practices that are appropriate for them. Even in the challenging times posed by the current economic environment, corporations have continued to work proactively to refine their governance practices, and develop new practices, as conditions change and “best practices” continue to evolve.

Given the fundamental nature of the changes that have occurred during the past decade in the framework of laws and regulations related to corporate governance, in the economy, and in best practices, Business Roundtable believes it is appropriate, once again, to restate our guiding principles of corporate governance. These principles, we believe, should help guide the ongoing advancement of corporate governance practices and, thus, advance the ability of public corporations to compete, create jobs and generate long-term, sustainable economic growth. Although Business Roundtable believes that these principles represent best practices in corporate governance, we understand that variations exist among U.S. public companies and their shareholders. Accordingly, we believe that no one approach is right for all corporations. Each corporation should look to these principles as a guide in developing structures, practices and processes that are appropriate for it in light of its needs and circumstances. In addition, because transparency is a critical part of effective corporate governance, each corporation should provide complete and accurate disclosure about its governance practices so that shareholders and other interested parties can understand them.

Business Roundtable supports the following guiding principles:

First, the paramount duty of the board of directors of a public corporation is to select a chief executive officer and to oversee the CEO and senior management in the competent and ethical operation of the corporation on a day-to-day basis.

Second, it is the responsibility of management, under the oversight of the board, to operate the corporation in an effective and ethical manner to produce long-term value for shareholders. The board of directors, the CEO and senior management should set a “tone at the top” that establishes a culture of legal compliance and integrity. Directors and management should never put personal interests ahead of or in conflict with the interests of the corporation.

Third, it is the responsibility of management, under the oversight of the board, to develop and implement the corporation’s strategic plans, and to identify, evaluate and manage the risks

inherent in the corporation's strategy. The board of directors should understand the corporation's strategic plans, the associated risks, and the steps that management is taking to monitor and manage those risks. The board and senior management should agree on the appropriate risk profile for the corporation, and they should be comfortable that the strategic plans are consistent with that risk profile.

Fourth, it is the responsibility of management, under the oversight of the audit committee and the board, to produce financial statements that fairly present the financial condition and results of operations of the corporation and to make the timely disclosures investors need to assess the financial and business soundness and risks of the corporation.

Fifth, it is the responsibility of the board, through its audit committee, to engage an independent accounting firm to audit the financial statements prepared by management and issue an opinion that those statements are fairly stated in accordance with Generally Accepted Accounting Principles, as well as to oversee the corporation's relationship with the outside auditor.

Sixth, it is the responsibility of the board, through its corporate governance committee, to play a leadership role in shaping the corporate governance of the corporation and the composition of the board. The corporate governance committee should regularly assess the skills and experience of the board and its members and engage in succession planning for the board.

Seventh, it is the responsibility of the board, through its compensation committee, to adopt and oversee the implementation of compensation policies, establish goals for performance-based compensation, and determine the compensation of the CEO and senior management. Compensation policies and goals should be aligned with the corporation's long-term strategy, and they should create incentives to innovate and produce long-term value for shareholders without excessive risk.

Eighth, it is the responsibility of the corporation to engage with long-term shareholders in a meaningful way on issues and concerns that are of widespread interest to long-term shareholders, with appropriate involvement from the board of directors and management.

Ninth, it is the responsibility of the corporation to deal with its employees, customers, suppliers and other constituencies in a fair and equitable manner and to exemplify the highest standards of corporate citizenship.

These responsibilities and others are critical to the functioning of the modern public corporation and the integrity of the public markets. No law or regulation can be a substitute for

the voluntary adherence to these principles by corporate directors and management in a manner that fits the needs of their individual corporations.

Business Roundtable continues to believe that corporate governance should be enhanced through conscientious and forward-looking action by a business community that focuses on generating long-term shareholder value with the highest degree of integrity.

The principles discussed here are intended to assist corporate boards of directors and management in their individual efforts to implement best practices of corporate governance, as well as to serve as guideposts for the public dialogue on evolving governance standards. As noted above, there is no “one size fits all” approach that will be suitable for all corporations. However, to the extent that a corporation follows governance practices that diverge from common practice, it should consider disclosing the reasons for this and why its practices are appropriate for it, consistent with its size, industry, culture and other relevant factors.



## **I. Key Corporate Actors**

Effective corporate governance requires a clear understanding of the respective roles of the board, management and shareholders, their relationships with each other, and their relationships with others that have an interest in the corporation and its well-being. The relationships of the board and management with shareholders should be characterized by transparency and appropriate engagement; their relationships with employees should be characterized by fairness; their relationships with the communities in which they operate should be characterized by good citizenship; and their relationships with government should be characterized by a commitment to compliance.

The board of directors has the important role of overseeing management performance on behalf of shareholders. Its primary duties are to select and oversee a well-qualified and ethical chief executive officer who, with other management, runs the corporation on a daily basis, and to monitor management's performance and adherence to corporate and ethical standards. Effective corporate directors are diligent monitors, but not managers, of business operations.

Management, led by the CEO, is responsible for running the day-to-day operations of the corporation and properly informing the board of the status of these operations. Management's responsibilities include strategic planning, risk management and financial reporting.

Shareholders invest in a corporation by buying its stock and receive economic benefits in return. Shareholders are not involved in the day-to-day management of corporate operations, but they have the right to elect representatives (directors) to look out for their interests and to receive the information they need to make investment and voting decisions. Shareholders also should expect that a corporation will be responsive to issues and concerns that are of widespread interest to its long-term shareholders.

Effective corporate governance requires a proactive, focused state of mind on the part of directors, the CEO and senior management, all of whom must be committed to business success through the maintenance of the highest standards of responsibility and ethics. Although there are a number of legal and regulatory requirements that must be met, good governance is far more than a "check the box" list of minimum board and management policies and duties. In addition, even the most thoughtful and well-drafted policies and procedures are destined to fail if directors and management are not committed to enforcing them in practice. A successful corporate governance structure for any corporation is a working system for principled goal setting, effective decision making, and appropriate monitoring of compliance and performance. Through this vibrant and responsive structure, the board of directors, CEO

and senior management can interact effectively and respond quickly and appropriately to changing circumstances, within a framework of solid corporate values, to provide enduring value to shareholders.

## **II. The Roles of the Board of Directors and Management**

An effective system of corporate governance provides the framework within which the board and management address their respective responsibilities. The board should regularly evaluate its governance framework and practices to assess whether they continue to be appropriate.

### **The Board of Directors**

- ▶ The business of a corporation is managed under the oversight of the corporation's board. The board delegates to the CEO—and through the CEO to other senior management—the authority and responsibility for managing the everyday affairs of the corporation. Directors monitor management on behalf of the corporation's shareholders.
- ▶ Making decisions regarding the selection, compensation and evaluation of a well-qualified and ethical CEO is the single most important function of the board. The board also appoints or approves other members of the senior management team.
- ▶ Directors bring to the corporation a range of experience and knowledge, but there are certain characteristics that all directors should possess. Every director should have integrity, character and sound judgment. In addition, a director should represent the interests of all shareholders; directors should not represent the interests of particular constituencies.
- ▶ Effective directors maintain an attitude of constructive skepticism; they ask incisive, probing questions and require accurate, honest answers; they act with integrity and diligence; and they demonstrate a commitment to the corporation, its business plans and long-term shareholder value.
- ▶ The composition of the board, as a whole, should reflect a mix of skills and expertise that are appropriate for the corporation given its circumstances and that, collectively, enables the board to perform its oversight function effectively.
- ▶ Directors need to have a thorough understanding of the corporation, its business and the industry in which it operates. Directors should keep abreast of any relevant developments. Directors can gain and maintain this understanding through briefings from management, reviewing industry journals and press and analyst reports, participating in educational programs, etc.

- ▶ In performing its oversight function, the board is entitled to rely on the advice, reports and opinions of management, counsel, auditors and expert advisers. The board should use care in choosing advisers, be comfortable with the qualifications of those it relies on, and hold managers and advisers accountable. The board should ask questions and obtain answers about the processes used by managers and the corporation's advisers to reach their decisions and recommendations, as well as about the substance of the advice and reports received by the board. When appropriate, the board and its committees should seek independent advice.
- ▶ Shareholders and other constituencies should reasonably expect that directors will exercise vigorous and diligent oversight of a corporation's affairs. However, they should not expect the board to micromanage the corporation's business by performing or duplicating the tasks of the CEO and senior management team. Directors should be informed about the operation of the corporation's business, but they should not become involved with operational matters, which are the province of management.
- ▶ The board's oversight function carries with it a number of specific responsibilities in addition to that of selecting and overseeing the CEO. These responsibilities include:
  - *Planning for senior management development and succession.* The board should oversee the corporation's plans for developing senior management personnel and plan for CEO and senior management succession. When appropriate, the board should replace the CEO or other members of senior management. The board should review the corporation's succession plans at least annually and periodically review the effectiveness of the senior management development and succession planning process.
  - *Reviewing, understanding and monitoring the implementation of the corporation's strategic plans.* The board has responsibility for overseeing and understanding the corporation's strategic plans from their inception through their development and execution by management. Once the board reviews a strategic plan, it should regularly monitor implementation of the plan to determine whether it is being implemented effectively and whether changes are needed. The board should understand the relationship between strategy and risk and review the risks inherent in the corporation's strategic plans. The board also should be comfortable that the corporation's incentive compensation program is appropriately aligned with the corporation's strategic plan.

- *Reviewing and understanding the corporation's risk assessment and overseeing the corporation's risk management processes.* The board has responsibility for overseeing the significant risks facing the corporation and the processes that management has implemented to identify and manage risk. The board, together with senior management, should agree on the appropriate risk profile for the corporation, and the board should be comfortable that the corporation's strategic plans are consistent with that profile. The board should establish an appropriate structure for overseeing risk, involving assistance from committees as appropriate and the designation of senior management responsible for risk management. Whatever risk oversight structure the board adopts, that structure should enable the board to remain fully informed about, and understand, all of the corporation's major risks and the steps that the corporation is taking to manage them.
- *Reviewing, understanding and overseeing annual operating plans and budgets.* The board is responsible for reviewing, understanding and overseeing the corporation's annual operating plans and for reviewing annual budgets presented by management. The board should monitor implementation of the annual plans to assess whether they are being implemented effectively and within the limits of approved budgets and whether the annual plans are appropriately responsive to changing conditions.
- *Focusing on the integrity and clarity of the corporation's financial statements and financial reporting.* The board, assisted by its audit committee, should be satisfied that the financial statements and other disclosures prepared by management accurately present the corporation's financial condition and results of operations to shareholders and that they do so in an understandable manner. To achieve accuracy and clarity, the board, through its audit committee, should have an understanding of the corporation's financial statements, including why the accounting principles critical to the corporation's business were chosen, what key judgments and estimates management made, and how the choice of principles and the making of these judgments and estimates affect the reported financial results of the corporation.
- *Advising management on significant issues facing the corporation.* Directors can offer management a wealth of experience and a wide range of perspectives. They provide advice and counsel to management in formal board and

committee meetings, and they are available for informal consultation with the CEO and senior management.

- *Reviewing and approving significant corporate actions.* As required by state corporate law, the board reviews and approves specific corporate actions, such as the election of executive officers, the declaration of dividends and (as appropriate) the implementation of major transactions. The board and senior management should have a clear understanding of what level and types of decisions require specific board approval.
- *Reviewing management's plans for business resiliency.* As part of its risk oversight function, the board should oversee the designation of senior management who will be responsible for business resiliency. The board should periodically review management's plans to address this issue. Business resiliency can include such items as business continuity, physical and cyber security, and emergency communications.
- *Nominating directors and committee members, and overseeing effective corporate governance.* It is the responsibility of the board, through its corporate governance committee, to nominate directors and committee members, and to oversee the composition, independence, structure, practices and evaluation of the board and its committees. The committee should regularly evaluate the skills and experience represented on the board and oversee succession planning for the board.
- *Overseeing legal and ethical compliance.* The board should set a "tone at the top" that establishes the corporation's commitment to integrity and legal compliance. The board, acting through its committees as appropriate, should oversee the corporation's compliance program and be comfortable that the corporation has implemented systems that enable the board to remain informed about the program and any significant compliance issues that may arise. In this regard, the board should be knowledgeable about the corporation's compliance program and should be satisfied that the program is effective in preventing and deterring violations. The board, or an appropriate committee, should receive regular briefings about developments and significant changes relating to the program and about the corporation's compliance trends. In addition, significant investigations of possible misconduct, investigations of misconduct involving senior management, the conclusions from any such investigations, and the investigative and remedial actions being taken should be

presented to the board or appropriate committee. The board should pay particular attention to conflicts of interest, including related-person transactions.

## The CEO and Management

- ▶ It is the responsibility of the CEO and management, under the CEO's direction, to operate the corporation in an effective and ethical manner. As part of its operational responsibility, management is charged with:
  - *Operating the corporation.* The CEO and management run the corporation's day-to-day business operations. With a thorough understanding of how the corporation operates and earns its income, they carry out the corporation's strategic objectives within the annual operating plans and budgets, which the board reviews. In making decisions about the corporation's business operations, the CEO considers the long-term interests of the corporation and its shareholders and necessarily relies on the input and advice of others, including the board, senior management and outside advisers. The CEO keeps the board apprised of significant developments regarding the corporation's business operations.
  - *Strategic planning.* The CEO and senior management generally take the lead in strategic planning. They identify and develop strategic plans designed to create long-term value for the corporation, present those plans to the board, implement the plans once board review is completed, and recommend and carry out changes to the plans as necessary. As part of the strategic planning process, the CEO and senior management identify, evaluate and manage risks associated with the plans.
  - *Identifying, evaluating and managing risks.* Management identifies, evaluates and manages the risks that the corporation undertakes in implementing its strategic plans and in the course of carrying out its business. It also manages the corporation's overall risk profile, and senior management keeps the board informed on an ongoing basis about the corporation's significant risks and its risk management processes.
  - *Annual operating plans and budgets.* With the corporation's overall strategic plans in mind, senior management develops annual operating plans and budgets for the corporation and presents the plans and budgets to the board. Once the

board has reviewed the annual operating plans and budgets, the management team implements them and monitors them, making changes as appropriate in light of changing conditions, assumptions or expectations. The management team also keeps the board apprised of significant developments and changes relating to the annual operating plans and budgets.

- *Selecting qualified management and establishing an effective organizational structure.* Senior management is responsible for selecting qualified management and implementing an organizational structure that is efficient and appropriate for the corporation's particular circumstances.
  - *Accurate and transparent financial reporting and disclosures.* Management is responsible for the integrity of the corporation's financial reporting system, and the accurate and timely preparation of the corporation's financial statements and related disclosures in accordance with Generally Accepted Accounting Principles and in compliance with applicable laws and regulations. It is management's responsibility—under the direction of the CEO and the corporation's principal financial officer—to establish, maintain and periodically evaluate the corporation's internal controls over financial reporting and the corporation's disclosure controls and procedures. In accordance with applicable law and regulations, the CEO and the corporation's principal financial officer also are responsible for certifying the accuracy and completeness of the corporation's financial statements and the effectiveness of the corporation's internal and disclosure controls.
- ▶ The CEO and management are responsible for operating the corporation in an ethical manner. They should never put individual, personal interests before those of the corporation or its shareholders. Business Roundtable believes that when carrying out this function, corporations should have:
- *A CEO of integrity.* The CEO should be a person of integrity who takes responsibility for the corporation adhering to the highest ethical standards.
  - *A strong, ethical "tone at the top."* The CEO and senior management should set a "tone at the top" that establishes a culture of legal compliance and integrity communicated to personnel at all levels of the corporation.
  - *An effective compliance program.* Management should take responsibility for implementing and managing an effective compliance program and should report



regularly to the board on compliance matters. As part of its compliance program, a corporation should have a code of conduct with effective reporting and enforcement mechanisms. Employees should have a means of seeking guidance and alerting management and the board about potential or actual misconduct without fear of retribution, and violations of the code should be addressed promptly and effectively.

### **III. How the Board Performs Its Oversight Function**

Publicly owned corporations employ diverse approaches to board structure and operations within the parameters of applicable legal requirements and securities market listing standards. Although no one structure is right for every corporation, Business Roundtable believes that the corporate governance “best practices” set forth in the following sections provide an effective approach for corporations to follow. To the extent that a corporation does not follow common governance practices, it should consider explaining why the board believes the corporation’s approach is appropriate for it given the corporation’s size, industry, culture and other relevant factors.

#### **Board Composition**

Boards of directors of large publicly owned corporations vary in size from industry to industry and from corporation to corporation. In determining board size, directors should consider the nature, size and complexity of the corporation as well as its stage of development. The experiences of many Business Roundtable members suggest that smaller boards often are more cohesive and work more effectively than larger boards.

Directors should be elected by a majority vote. In addition, boards should adopt a resignation policy that requires a director who does not receive a majority vote to tender his or her resignation to the board for its consideration. Although the ultimate decision whether to accept or reject the resignation will rest with the board, the board should think critically about the reasons why the director did not receive a majority vote and whether or not the director should continue to serve. Among other things, the board should consider whether the vote resulted from concerns about a policy issue affecting the board as a whole or concerns specific to the individual director. If the board decides not to accept a resignation, the corporation should disclose the reasons for this decision promptly. In addition, when a director is elected but receives significant “withhold” or “against” votes, the board should consider the reasons for the vote.

Having a variety of backgrounds and experience, consistent with the corporation’s needs, is important to the overall composition of the board. Because the corporation’s need for particular backgrounds and experience may change over time, the board should monitor the mix of skills and experience that directors bring to the board and assess whether the board, as a group, has the necessary tools to work together in a productive and collegial fashion and perform its oversight function effectively. The board should consider implementing a structured framework for this ongoing process, such as using a skills matrix detailing specific qualifications and identifying the skills that current directors, and director candidates, bring to the board.

Directors with relevant business and leadership experience are beneficial to the board as a whole and to the corporation. These directors can provide a useful perspective on business strategy and significant risks and an understanding of the challenges facing the business. Corporations should assist directors who do not have significant background in a corporation's business or industry through orientation programs and otherwise. All directors should remain informed about issues and developments relevant to the corporation's business and industry by reviewing pertinent information provided by management and the corporation, subscribing to industry journals, reviewing analyst and press reports, and participating in educational programs.

As part of the ongoing assessment of board composition, the board should plan ahead for the nomination of new directors by engaging in succession planning. The board should conduct a forward-looking assessment to identify qualifications and attributes that the board may find valuable in the future based on the corporation's strategic plans, anticipated director retirements and evolving best practices in the corporation's industry. The board also should plan ahead for director departures, considering whether it is appropriate to establish or maintain procedures for the retirement or replacement of board members, such as a mandatory retirement age or term limits. The board should assess whether other practices, such as the assessment of director candidates in connection with the renomination process, annual board evaluations and individual director evaluations, may make a retirement age or term limit unnecessary. Many boards also establish a requirement that directors who change their primary employment tender a board resignation, providing an opportunity for the board to consider the desirability of their continued service in light of their changed circumstances.

Board independence is critical to effective corporate governance. Providing objective independent judgment is at the core of the board's oversight function, and the board's composition should reflect this principle. Accordingly, a substantial majority of the board's directors should be independent, both in fact and appearance, as determined by the board. Board independence depends not only on directors' individual relationships and outlook but also on their ability to question management, exercise constructive skepticism and express their views even when those views may differ from those of management or other directors.

The board should make an affirmative determination as to the independence of each director annually and should have a process in place for making these determinations.

- ▶ *Definition of "independence."* An independent director should not have any relationships with the corporation or its management—whether business, employment, charitable or personal—that may impair, or appear to impair, the director's ability to exercise independent judgment. The listing standards of the major securities markets

define “independence” and enumerate specific relationships involving directors and their family members (such as employment with the corporation or its outside auditor) that preclude a director from being considered independent.

- ▶ *Assessing independence.* The board should consider all relevant facts and circumstances when assessing directors’ independence, taking into account the requirements of the federal securities laws, securities market listing standards, and the views of institutional investors and other relevant groups. When evaluating whether a director is independent, the board should consider whether the director has any relationships, either directly or indirectly, with the corporation, senior management or other board members that could affect the director’s actual or perceived independence. Corporations must disclose in their proxy statements relationships that the board considered in assessing independence in accordance with the requirements of the federal securities laws. Many boards have adopted standards to assist them in assessing independence. These standards should be included in a corporation’s corporate governance principles.
- ▶ *Relationships with not-for-profit organizations.* The board’s director independence assessment should include a review of relationships that directors, and their spouses, have with not-for-profit organizations that receive support from the corporation. In conducting this assessment, the board should take into account the size of the corporation’s contributions and the nature of the relevant director’s relationships to the recipient organizations. Independence issues are most likely to arise when a director, or the director’s spouse, is an employee of the not-for-profit organization and when a substantial portion of the organization’s funding comes from the corporation. It also may be appropriate to consider contributions from a corporation’s foundation to organizations with which a director or a director’s spouse is affiliated.

## **Board Leadership**

Boards of American corporations have taken a variety of approaches to board leadership, with some boards combining the positions of CEO and chairman and others appointing a separate chairman or designating a “lead” or presiding director. No one leadership structure is right for every corporation at all times, and boards of different corporations may reach different conclusions about the leadership structures that are most appropriate for their corporations at any particular point in time. The board should decide whether to combine or separate the positions of CEO and chairman of the board based on its assessment of what is in the best interests of the corporation and its shareholders based on the corporation’s particular circumstances, and the board should evaluate its leadership structure periodically. In addition,

in connection with the CEO succession planning process, the board should consider the appropriate board leadership structure.

Whatever leadership structure a board chooses, independent board leadership is critical to effective corporate governance. To provide independent leadership for the board, the board should consider appointing a lead director (or presiding director with comparable responsibilities) if it combines the positions of CEO and chairman or has a chairman who is not independent. The lead director should be appointed by the independent members of the board and should serve for a period of at least one year. At some corporations the lead director is appointed annually, while at others the lead director serves for a longer term or an indefinite period of time.

Lead directors perform a range of functions, depending on the needs of the board. One of the primary functions of the lead director is chairing executive sessions of a board's independent or non-management directors. The lead director should have the authority to call executive sessions, and should coordinate and oversee appropriate follow-up on matters discussed in executive sessions to maximize the effectiveness of these sessions. Other key functions of the lead director may include chairing board meetings in the absence of the chairman of the board, reviewing and/or approving agendas and schedules for board meetings and information sent to the board, and being available for engagement with long-term shareholders as appropriate. The lead director also may play a key role in overseeing performance evaluations of the CEO and the board, and leading the board in crisis situations.

Depending on the responsibilities associated with the position of the lead director or independent chairman, the position may involve substantial responsibility and require a significant time commitment on the part of a director.

### **Board Organization**

Virtually all boards of directors of large, publicly owned corporations operate using committees to assist them. A committee structure permits the board to address key areas in more depth than may be possible in a full board meeting.

Decisions about committee membership and chairs should be made by the full board based on recommendations from the corporate governance committee. Consideration should be given to whether periodic rotation of committee memberships and chairs would provide fresh perspectives and enhance directors' understanding of different aspects of the corporation's business, consistent with applicable listing standards.

In connection with joining a committee, directors should participate in orientation to familiarize themselves in greater depth with the subject matter areas that the committee is responsible for overseeing. In addition, all committee members should be encouraged to participate in continuing education relating to the committee's areas of responsibility. For example, committees may benefit from periodic educational sessions, led by management or outside experts, which address recent developments and best practices relevant to the committees' duties. In this regard, committee members should be cognizant of how recent developments impact the corporation's own practices.

Committees should apprise the full board of their activities on a regular basis. Processes should be developed and monitored for keeping the board informed through oral or written reports. For example, some corporations provide minutes of committee meetings to all members of the board.

Business Roundtable believes that the functions generally performed by the audit, compensation and corporate governance committees are central to effective corporate governance. The listing standards of the major securities markets require corporations to have an audit committee that performs specific functions, and many corporations also are required to have committees that oversee executive compensation, director nominations and corporate governance matters. Business Roundtable does not believe that a particular committee structure is essential for all corporations. What is important is that the independent members of the board address key issues effectively. These issues include compliance, executive compensation, financial reporting, governance, risk oversight, director nominations and succession planning. Thus, the references below to the functions performed by particular committees are not intended to preclude corporations from allocating these functions differently, consistent with applicable listing standards.

Additional committees, such as finance, public responsibility or risk management, also may be used. Some corporations find it useful to establish committees to examine special problems or opportunities in greater depth than would otherwise be feasible.

The responsibilities of each committee and the qualifications required for committee membership should be clearly defined and set out in a written charter that is approved by the board and publicly available. Each committee should review its charter annually and recommend changes to the board as appropriate.

## Audit Committee

Every publicly owned corporation should have an audit committee of at least three members, who should all be independent directors.

Audit committees typically consist of three to five members. The listing standards of the major securities markets require that all members of the audit committee qualify as independent directors under applicable listing standards, subject to limited exceptions, and that they meet additional, heightened independence criteria.

Audit committee members should meet minimum financial literacy standards, as required by the listing standards of the major securities markets, and at least one member of the audit committee should be an audit committee financial expert, as determined by the board in accordance with regulations of the Securities and Exchange Commission. Audit committee members, as with all directors, should understand the corporation's business and risk profile and apply their business experience and judgment with an independent and critical eye to the issues for which the committee is responsible.

With the significant responsibilities imposed on audit committees under applicable law, regulations and listing standards, consideration should be given to whether it is appropriate to limit the number of public company audit committees on which a corporation's audit committee members may serve. Some boards have adopted policies that audit committee members may not serve on the audit committees of more than three public corporations, in accordance with applicable securities market listing standards. Policies may permit exceptions to this limit when the corporation's board determines that the simultaneous service would not affect an individual's ability to serve effectively on the corporation's audit committee.

The audit committee is responsible for supervising the corporation's relationship with its outside auditor. In performing this responsibility, the primary functions of the audit committee include:

- ▶ *Selecting and retaining the auditor and approving in advance the terms of the annual audit engagement.* The selection of the outside auditor should involve an annual due diligence process in which the audit committee reviews the qualifications, work product, independence and reputation of the outside auditor, and the performance of key members of the audit team. The committee should be mindful of the schedule, mandated by applicable law and regulations, for rotating the engagement and concurring partners and should begin the process of reviewing new partners sufficiently in advance of required rotations. In retaining the auditor, the audit committee should

oversee the process of negotiating the annual audit engagement letter and should scrutinize the terms of the engagement carefully.

- ▶ *Overseeing the independence of the outside auditor.* The audit committee should maintain an ongoing, open dialogue with the outside auditor about independence issues. The committee should consider its overall approach to using the outside auditor as a service provider and identify those services, beyond the annual audit engagement, that the outside auditor can provide to the corporation consistent with applicable law and regulations and with maintaining independence. In pre-approving services to be provided by the outside auditor, as required by applicable law and regulations, the audit committee should decide whether to adopt a pre-approval policy or approve services on an engagement-by-engagement basis.

The audit committee also is responsible for overseeing the corporation's financial reporting process. The audit committee should review and discuss the corporation's annual financial statements with management and the outside auditor, and should review the corporation's quarterly financial statements and related earnings press releases prior to issuance. As part of its reviews, the audit committee should review and discuss with management and the outside auditor the corporation's critical accounting policies, the quality of accounting judgments and estimates made by management, any comments received from Securities and Exchange Commission staff, and any material written communications between the outside auditor and management.

The audit committee should oversee the corporation's system of internal controls over financial reporting and its disclosure controls and procedures, including the processes for producing the certifications required of the CEO and principal financial officer. On a periodic basis, the committee should review with both the internal and outside auditors, as well as with management, the corporation's procedures for maintaining and evaluating the effectiveness of these systems. The committee should be promptly notified of any significant deficiencies or material weaknesses in internal controls and should be kept informed about the steps and timetable for correcting them.

Unless the full board or one or more other committees does so, the audit committee should oversee the corporation's program that addresses compliance with ethical and legal standards and important corporate policies, including the corporation's code of conduct and the mechanisms it has in place for employees to report compliance issues. In accordance with applicable legal requirements, the audit committee should establish procedures for receiving and handling complaints and concerns related to accounting, internal accounting controls and auditing issues, and the committee should evaluate these procedures periodically and revise



them as appropriate. The audit committee should be briefed regularly by senior management (including senior management responsible for the legal, compliance and audit functions) on the status of outstanding compliance issues, including concerns submitted through the committee's procedures for handling accounting and related concerns, and it should receive prompt notification of any significant compliance issues. The audit committee should report at least annually to the full board on its oversight of the compliance program.

Unless the full board or another committee does so, the audit committee should oversee the corporation's risk assessment and risk management. Many corporations address risk through the audit committee, in part because securities market listing standards applicable to many corporations require audit committees to discuss policies with respect to risk assessment and risk management. However, the audit committee should not be the sole body responsible for risk oversight, and the board may decide that it is appropriate to allocate responsibility for some types of risk to other committees (for example, compensation risk to the compensation committee) or to the board as a whole. No one risk oversight structure is right for every board, and different structures may be appropriate depending on a corporation's industry and other factors. Committees with risk-related responsibilities should report regularly to the full board on the risks that they oversee and brief the audit committee as appropriate in cases where securities marked listing standards require the audit committee to retain some oversight responsibility for risk.

The audit committee should oversee the corporation's internal audit function, including reviewing the scope of the internal audit plan, reports submitted by the internal audit staff and management's response, and the appointment and replacement of the senior internal auditing executive. The senior internal auditing executive should have a direct communication line to the audit committee, so that the executive has the authority to report any issues or concerns directly to the committee. Final decisions relating to the hiring and termination of the senior internal audit executive should be made following consultation with the audit committee.

The audit committee should implement a policy covering the hiring of personnel who previously worked for the corporation's outside auditor. At a minimum, this policy should incorporate the "cooling off" period and other auditor independence hiring requirements mandated by applicable law and regulations.

Audit committee meetings should be held at least quarterly, with additional meetings held frequently enough to allow the committee to monitor the corporation's financial reporting appropriately. Meetings should be scheduled with enough time to permit and encourage active discussions with management and the internal and outside auditors. The audit committee should meet privately with each of the internal and outside auditors and management on a

regular basis, and in any event at least quarterly, and communicate with them between meetings as necessary. The audit committee also should hold private sessions on a regular basis with senior management responsible for the corporation's legal function to facilitate the communication of concerns regarding legal compliance matters and significant legal contingencies. In addition, the audit committee should consider whether to hold private sessions from time to time with other parties, including senior management responsible for risk assessment and risk management, and those responsible for compliance.

### **Corporate Governance Committee**

Every publicly owned corporation should have a committee composed solely of independent directors that addresses director nominations and corporate governance matters.

The corporate governance committee (often combined with or referred to as a nominating committee) should have at least three members and should be composed solely of independent directors.

The corporate governance committee recommends director nominees to the full board and the corporation's shareholders, oversees the composition, structure, operation and evaluation of the board and its committees, and plays a leadership role in shaping the corporate governance of the corporation. Depending on how the board has allocated responsibilities among its committees, the corporate governance committee also may oversee the compensation of the board if the compensation committee does not do so, or the two committees may share oversight responsibility for this area. The committee should remain informed about legal and regulatory developments in the area of corporate governance.

As part of its responsibility to oversee the composition of the board, the corporate governance committee should engage in succession planning for the board. This process should include looking at the skills and experience currently represented on the board, identifying qualifications and attributes that the board may find valuable in the near-term and the future based on the corporation's strategic direction, and planning ahead for the departure of directors and the designation of new board members. The corporate governance committee should regularly conduct an assessment of the mix of skills represented on the board to evaluate whether the board, as a whole, contains the right balance of professional and personal backgrounds, and includes individuals that bring industry and other relevant knowledge, financial expertise, diversity and other desired characteristics to the board.

In performing the core function of identifying and recommending director candidates to the board, the corporate governance committee should establish criteria for board membership

and recommend these criteria to the board for approval. There are certain criteria that every director should have, such as sound judgment, integrity and an objective mind. The committee should periodically review the board's membership criteria and recommend changes to the board as appropriate. Based on the board's membership criteria and the qualifications and attributes identified through the assessment of the board's composition, the committee should identify director candidates, review their qualifications and any potential conflicts with the corporation's interests, and recommend new director candidates to the board.

In identifying director candidates, the corporate governance committee should take a proactive approach by soliciting ideas for potential candidates from a variety of sources. The committee should have the authority to retain search firms as appropriate to assist it in identifying candidates and should provide search firms with the criteria articulated by the committee. The committee also should develop a process for considering shareholder recommendations for board nominees. Although it is appropriate for the CEO to meet with board candidates, the final responsibility for selecting director nominees should rest with the corporate governance committee and the board.

In connection with the renomination of current directors, the corporate governance committee should review their skills and experience, assess their contributions to the board, and consider their continued value to the corporation in light of current and future needs. Some boards may undertake these steps, in part, through individual director evaluations, which may occur through a more formalized process or in connection with renominating directors.

The corporate governance committee should monitor and safeguard the independence of the board. An important function of a corporate governance committee, related to its core function of recommending nominees to the board, is to see that a substantial majority of the directors on the board meet appropriate standards of independence that are consistent with securities market listing standards and to see that these directors are independent both in fact and in appearance. It is also important that directors have the ability to question management, exercise constructive skepticism and express their views even when those views may differ from those of management or other directors.

The corporate governance committee should consider all relevant facts and circumstances in assessing independence and make recommendations to the board regarding determinations of director independence. If the board has developed a set of standards for assessing independence, the committee should evaluate directors' relationships in light of these standards. In addition, the committee should receive prompt notification from directors of any change in a director's circumstances that may affect the director's independence (such as a family member's job change).

The corporate governance committee should conduct a periodic evaluation of the board's leadership structure to assess whether the current leadership structure remains appropriate. In addition, the committee should oversee the process of planning for succession to the position of chairman of the board, which should involve consideration of whether to combine or separate the positions of CEO and chairman of the board when the current chairman's tenure ends and consideration of whether a new CEO might necessitate a change to the board leadership structure.

The corporate governance committee also recommends directors for appointment to committees of the board. The committee should periodically review the board's committee structure and annually recommend candidates for membership on the board's committees. The committee should see that the key board committees, including the audit, compensation and corporate governance committees, are composed of directors who meet applicable independence and qualification standards. In addition, the committee should consider whether periodic rotation of committee memberships and chairs would provide fresh perspectives and enhance directors' understanding of various aspects of the corporation's business.

The corporate governance committee should oversee the effective functioning of the board. The committee should review the board's policies relating to meeting agendas and schedules and the corporation's processes for providing information to the board, with input from the lead director or independent chairman. The corporate governance committee should assess the reporting channels through which the board receives information and see that the board obtains appropriately detailed information in a timely fashion. This includes receiving information from a variety of sources, from inside and outside of the corporation, including both positive and negative materials such as analyst reports, industry publications and press articles. It also includes seeing that relevant information that the corporation receives from key stakeholders, such as long-term shareholders, is appropriately shared with the board.

The corporate governance committee should develop and recommend to the board a set of corporate governance principles, review them annually and recommend changes to the board as appropriate. The corporation's corporate governance principles should be available on the corporation's website and should address, at a minimum, board leadership, qualifications for directors, director independence, director responsibilities, the structure and functioning of board committees, board access to management and advisers, director compensation, director orientation and continuing education, board evaluations and management succession.

The corporate governance committee should oversee the corporation's efforts in the area of shareholder engagement and coordinate with management any appropriate board-level involvement in that process.

The corporate governance committee should oversee the evaluation of the board and its committees. Specifics concerning the evaluation process are discussed under “Board and Committee Evaluation.”

### **Compensation Committee**

Every publicly owned corporation should have a committee composed solely of independent directors that addresses compensation issues.

The compensation committee should have at least three members and should be composed solely of independent directors. All committee members should have and maintain sufficient knowledge of executive compensation and related issues to perform their duties effectively.

The compensation committee’s responsibilities include overseeing the corporation’s overall compensation structure, policies and programs, establishing or recommending to the board performance goals and objectives for the CEO and other members of senior management (or, in some companies, in conjunction with the corporate governance committee), and establishing or recommending to the independent directors compensation for the CEO and senior management. The compensation committee should see that the corporation’s compensation policies reflect the core principle of pay for performance and should establish meaningful goals for performance-based compensation paid to senior management.

The committee should see that the corporation’s compensation policies and performance goals are closely linked to its strategic plan and that they create incentives to produce long-term value for shareholders without encouraging excessive risk-taking.

The compensation committee should have the authority to retain compensation consultants, counsel and other advisers to provide the committee with independent advice.

The compensation committee should understand all aspects of an executive’s compensation package, and should review and understand the maximum payout due under multiple scenarios (such as retirement, termination with or without cause, and severance in connection with business combinations or the sale of a business).

The compensation committee should require senior management to build and maintain significant continuing equity investment in the corporation. To align senior management interests with the interests of shareholders, the committee should establish requirements that senior management acquire and hold a meaningful amount of the corporation’s stock for at least the duration of their tenure with the corporation.

In addition to reviewing and setting compensation for senior management, the compensation committee should look more broadly at the overall compensation structure of the enterprise to determine that it establishes appropriate incentives for management and employees at all levels and that these incentives do not encourage inappropriate risk-taking. The committee should consider carefully and understand the incentives created by different forms of compensation. Incentives should further the corporation's long-term strategic plans by looking beyond short-term market value changes to the overall goal of creating and enhancing enduring shareholder value, and they should be consistent with the corporation's culture. The committee should see that the corporation has in place appropriate practices to mitigate risks created by compensation programs.

Executive compensation should directly link the interests of senior management, both individually and as a team, to the long-term interests of shareholders. It should include significant performance-based criteria related to long-term shareholder value and should reflect upside potential and downside risk.

The compensation committee should carefully examine the benefits and perquisites provided to senior management and determine whether they appropriately balance the interests of long-term shareholders and the ability of the corporation to recruit and retain top talent. The corporation should generally bear the cost of these items only if they are directly related to management's job performance; the corporation should not bear the cost of personal expenses.

The compensation committee should oversee the corporation's disclosures with respect to executive compensation. Disclosure about executive compensation should be transparent and written in plain English so that it is understandable to shareholders. In particular, the committee should use the compensation discussion & analysis (CD&A) disclosure to provide shareholders with meaningful and understandable information about the corporation's executive compensation philosophy, policies and practices, the factors that the committee and the board consider in making compensation decisions, and the relationship between executive compensation and corporate performance.

### **Board Operations**

Serving on a board requires significant time and attention on the part of directors. Directors must participate in board meetings, review relevant materials, serve on board committees, and prepare for meetings and discussions with senior management. Certain roles, such as committee chair, chairman of the board and lead director, carry an additional time

commitment beyond that attendant to board and committee service. Directors must spend the time needed and meet as frequently as necessary to discharge their responsibilities properly.

The board of directors, with the assistance of the corporate governance committee, should consider the appropriate frequency and length of board meetings. Longer meetings may permit directors to explore key issues in depth, whereas shorter but more frequent meetings may help directors stay up-to-date on emerging corporate trends, and business and regulatory developments. When arranging a meeting schedule for the board, each corporation should consider the nature and complexity of its operations and transactions, as well as its business and regulatory environment.

The board of directors, with the assistance of the committee responsible for overseeing director compensation, should periodically review the compensation of the board in light of developments in the marketplace and the board's needs. This review should include consideration of differential compensation for specific roles that carry more responsibility, such as chairing committees, acting as lead director or acting as independent chairman. The board should approve changes in compensation based on the recommendation of the committee. In determining director compensation, the board should focus on creating total director compensation that is reasonable relative to directors' responsibilities and compensation at comparable companies. The board also should be comfortable that compensation adequately rewards directors for the risks associated with board service, as well as their time and efforts.

Director compensation should consist of a mix of cash and equity. The board should consider paying the cash portion of director compensation in the form of an annual retainer, rather than through meeting fees, to encourage directors to view board service as an ongoing commitment and to foster a long-term focus. Equity helps align the interests of directors with those of the corporation's shareholders, but equity compensation should be carefully designed to avoid unintended incentives such as an emphasis on short-term market value changes. Corporations increasingly are providing the long-term equity component of director compensation in the form of restricted stock, rather than stock options, to better align directors' interests with those of shareholders. The board should establish a requirement that directors hold a meaningful amount of the corporation's stock for as long as they remain on the board.

Business Roundtable does not endorse a specific limitation on the number of directorships an individual may hold. However, service on too many boards can interfere with an individual's ability to satisfy his or her responsibilities, either as a member of senior management or as a director. Before accepting an additional board position, a director should consider whether the acceptance of a new directorship will compromise the ability to devote adequate time and focus to present responsibilities. Directors should notify the chair of the corporate governance

committee before accepting a seat on the board of another corporation or assuming a significant new role on an existing board (such as a committee chair or lead director position). Some boards require the prior approval of the corporate governance committee before a director accepts a seat on the board of another corporation. Similarly, the corporation should establish a process to review senior management service on other boards prior to acceptance in order to consider the time commitment and review any potential conflicts of interest and interlocks.

The board's independent or non-management directors should have the opportunity to meet regularly in executive session, outside the presence of the CEO and any other management directors.

- ▶ Time for an executive session should be placed on the agenda for every regularly scheduled board meeting. The independent chairman or lead director, as applicable, should see that adequate time is reserved for these sessions, and should set the agenda for and chair these sessions.
- ▶ To maximize the effectiveness of executive sessions, the independent chairman or lead director, as applicable, should follow up with the CEO and other appropriate members of senior management on matters addressed in the executive sessions.

Many board responsibilities may be delegated to committees to permit directors to address key areas in more depth as discussed above. Regardless of whether the board grants plenary power to its committees with respect to particular issues or prefers to take recommendations from its committees, committees should keep the full board informed of their activities. Corporations benefit greatly from the collective wisdom of the entire board acting as a deliberative body, and the interaction between committees and the full board should reflect this principle.

The board's agenda must be carefully planned yet flexible enough to accommodate emergencies and unexpected developments. The chairman of the board should work with the lead director (when the corporation has one) in setting the agenda, and should be responsive to individual directors' requests to add items to the agenda and open to suggestions for improving the agenda. It is important that the agenda and meeting schedule permit adequate time for discussion and a healthy give-and-take between board members and management.

The board should work to foster open, ongoing dialogue between management and members of the board. Board members should have full access to senior management outside of board meetings.



Board agendas should be structured to maximize the use of meeting time for open discussion and deliberation. Highlighting changes relevant to recurring agenda items and distributing copies of presentations sufficiently in advance of meetings can facilitate review of materials prior to meetings and increase the time that is available for discussion and constructive dialogue.

The board must have accurate, complete information to do its job; the quality of information that the board receives directly affects its ability to perform its oversight function effectively. Directors should receive and review information from a variety of sources, including senior management, board committees, outside experts and the outside auditor, as well as industry journals, and analyst and media reports. The board should receive information before board and committee meetings with sufficient time to review and reflect on key issues and to request supplemental information as necessary. Corporations should consider ways in which they can use technology, such as board portals, to provide directors access to relevant information on a timely basis. Technology can provide a mechanism for providing meeting materials, delivering real-time information about developments that occur between meetings and creating resources with background information and educational tools for directors to access at their convenience.

Corporations should have a robust orientation process for new directors that is designed to familiarize them with the various aspects of the corporation, including its business, strategy, industry, management, compliance programs and corporate governance practices. Common components of board orientation programs include briefings from senior management, on-site visits to the corporation's facilities, informal meetings with other directors and written materials.

Corporations should encourage directors to take advantage of educational opportunities on an ongoing basis. Continuing education can assist directors in keeping abreast of issues and developments relevant to the corporation and enable them to address specific subjects in greater depth. Continuing education can take the form of participation in outside programs or "in board" educational sessions, led by members of senior management or outside experts and customized for the corporation. Many boards rely on a combination of the two methods by informing their directors of outside programs and holding educational sessions for the full board or particular committees on a regular basis.

Where appropriate, boards and board committees should seek advice from outside advisers independent of management with respect to matters within their responsibility. For example, there may be technical aspects of the corporation's business—such as risk assessment and risk management—for which the board or a committee determines that additional expert advice

would be useful. Similarly, many compensation committees engage their own compensation consultants. Situations where the board or a committee may decide it is appropriate to seek independent legal advice include circumstances involving conflicts of interest, external or internal investigations, and mergers and acquisition activity. The board and its committees should have the authority to select and retain advisers and approve the terms of their retention and fees.

### **Senior Management Development and Succession**

Long-term planning for CEO and senior management development and succession is one of the board's most important functions. The board, its corporate governance committee or another committee of independent directors should identify and regularly update the qualities and characteristics necessary for an effective CEO. With these principles in mind, the board or committee should periodically monitor and review the development and progression of potential internal candidates against these standards, and see that internal candidates receive the necessary preparation. The board should review the corporation's succession plan at least annually and periodically review the effectiveness of the succession planning process.

Emergency succession planning also is critical. Working with the CEO, the board or committee should see that plans are in place for contingencies such as the departure, death or disability of the CEO or other members of senior management to facilitate the transition to both interim and longer-term leadership in the event of an untimely vacancy.

The corporation should disclose information about the board's succession planning process, either in the corporate governance principles or proxy statement or both. This disclosure can help facilitate shareholder understanding of the process that the board follows in planning for succession to the position of CEO.

Under the oversight of an independent committee or the lead director, the board should annually review the performance of the CEO and participate with the CEO in the evaluation of members of senior management. All non-management members of the board should participate with the CEO in senior management evaluations. The results of the CEO's evaluation should be promptly communicated to the CEO in executive session by representatives of the independent directors and used by the compensation committee or independent directors in determining the CEO's compensation.

## Board and Committee Evaluation

The board should have an effective mechanism for evaluating performance on a continuing basis. Meaningful board evaluation requires an assessment of the effectiveness of the full board, the operations of board committees and the contributions of individual directors.

There are a variety of ways to conduct board and committee evaluations. These include written questionnaires, group discussions led by a designated director, employee or outside facilitator (often with the aid of written questions) and individual interviews. Each board, with the assistance of the corporate governance committee, should determine what method or combination of methods will result in a meaningful assessment of the functioning of the board and its committees. Boards and committees should consider periodically varying the methods they use to keep the evaluation process fresh.

- ▶ For some companies, securities market listing standards require that the board and its audit, compensation and corporate governance committees conduct annual evaluations. Regardless of whether an evaluation is required, the performance of the full board should be evaluated annually, as should the performance of its committees. The board should use the annual evaluation to assess whether it is following the procedures necessary to function effectively. Each committee should conduct an annual evaluation to assess its effectiveness, and to review the committee's charter to determine whether any changes are appropriate. The results of this evaluation should be reported to the full board.
- ▶ Boards take a variety of approaches to assessing the contributions of individual directors. In this regard, board positions should not be regarded as permanent, and directors should serve only so long as they add value to the board. The corporate governance committee should examine a director's ability to continue to contribute to the board each time it considers the director for renomination. In addition, the corporate governance committee also should consider the continued value that directors will bring to the corporation as part of the committee's regular assessment of the skills and experience represented on the board as a whole and the board's current and future needs. Some boards also conduct individual director evaluations through a more formalized process that involves self or peer evaluations.

## **IV. Relationships with Shareholders and Other Constituencies**

Corporations are often said to have obligations to shareholders and other constituencies, including employees, the communities in which they do business and government, but these obligations are best viewed as part of the paramount duty to optimize long-term shareholder value. Business Roundtable believes that shareholder value is enhanced when a corporation engages effectively with its long-term shareholders, treats its employees well, serves its customers well, fosters good relationships with suppliers, maintains an effective compliance program and strong corporate governance practices, and has a reputation for civic responsibility.

### **Shareholders and Investors**

Over the past several years, some shareholders have expressed interest in having more input on matters affecting the corporations in which they invest. Corporations should productively engage with their long-term shareholders in a manner consistent with the respective roles of the board, management and shareholders. Corporations should be responsive to issues and concerns that are of widespread interest to their long-term shareholders. Corporations also should take steps to educate shareholders and other stakeholders about the board's role and its oversight responsibilities.

Corporations should encourage shareholders to make voting decisions based on consideration of what is in the best interests of the individual corporation and its shareholders. Meaningful involvement of shareholders requires that shareholders make company-specific judgments and consider the interests of the specific corporation. In this regard, a corporation should consider additional outreach efforts as appropriate to explain the bases for the corporation's recommendations on the matters it is asking shareholders to vote on.

Communication with shareholders is an important component of effective engagement. Corporations communicate with investors and other constituencies in proxy statements, annual and other reports, and shareholder meetings. Corporations also communicate through informal avenues of communication, such as earnings releases, conference calls and investor meetings.

- ▶ Corporations should consider whether, from time to time, it may be appropriate to use other mechanisms in order to solicit shareholder views. These may include periodic meetings with the corporation's largest shareholders or surveys to obtain feedback from long-term shareholders about particular issues, such as executive compensation.

Corporations should take advantage of technology to enhance the dissemination of information. A corporation's website should include copies of the corporation's governance principles, the charters of its board committees and codes of conduct. Corporations also should consider posting biographies of directors and members of senior management, information about current committee memberships, copies of their articles of incorporation and bylaws, information about communicating with the board and information about the corporation's annual meeting.

Corporations should have effective procedures for long-term shareholders to communicate with members of the board and for directors to respond in a timely manner to the concerns of long-term shareholders. Technology can facilitate these procedures. The board, or the corporate governance committee, should oversee and update these procedures as appropriate.

Corporations should use the annual shareholder meeting as an opportunity to engage with shareholders. Directors should attend the corporation's annual meeting of shareholders, and the corporation should have a policy that directors attend the annual meeting each year, absent unusual circumstances. Time at the annual meeting should be set aside for shareholders to submit questions and for senior management or directors to respond to those questions.

The board or its corporate governance committee should oversee the corporation's response to shareholder proposals. The board should seriously consider issues raised by shareholder proposals that receive substantial support and should communicate its response to proposals to the shareholder-proponents and to all shareholders.

## **Employees**

It is in a corporation's best interest to treat employees fairly and equitably.

Corporations should have in place policies and practices that provide employees with compensation, including benefits that are appropriate given the nature of the corporation's business, the employees' job responsibilities and geographic locations.

When corporations offer retirement, health care, insurance and other benefit plans, employees should be fully informed of the terms of those plans.

Corporations should have in place and publicize mechanisms for employees to seek guidance and to alert management and the board about potential or actual misconduct without fear of retribution.

Corporations should communicate honestly with their employees about corporate operations and financial performance.

### **Communities**

Corporations have obligations to be good citizens of the local, national and international communities in which they do business. Failure to meet these obligations can result in damage to the corporation, both in immediate economic terms and in longer-term reputational value.

A corporation should be a good citizen and contribute to the communities in which it operates by making charitable contributions and encouraging its directors, managers and employees to form relationships with those communities. A corporation also should be active in promoting awareness of health, safety and environmental issues, including any issues that relate to the specific types of business in which the corporation is engaged.

### **Government**

Corporations, like all citizens, must act within the law. The penalties for serious violations of law can be extremely severe, even life-threatening, for corporations. Compliance is not only appropriate—it is essential. Management should take reasonable steps to develop, implement and maintain an effective legal compliance program, and the board should be knowledgeable about and oversee the program, including periodically reviewing the program to gain reasonable assurance that it is effective in deterring and preventing misconduct.

Corporations have an important perspective to contribute to the public policy dialogue and should be actively involved in discussions about the development, enactment and revision of the laws and regulations that affect their businesses and the communities in which they operate and their employees reside.



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