Corporate Directors' Group Gives Repair Plan to Boards

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By Joann S. Lublin
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The leading U.S. organization of directors says its members must do a better job governing corporate America, or risk further alienation of wary shareholders.

In a report to be released Tuesday, the National Association of Corporate Directors urges boards to bolster their handling of risk oversight, corporate strategy, executive compensation and investor communications. Among other things, the report suggests directors consider creating so-called bonus banks for executives, which would pay out over time if executives reach key goals.

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The governance drive comes amid intensified scrutiny of corporate boards for poor oversight of management leading up to the credit crisis and recession. A new federal law requires 400 companies receiving bailout money to give stockholders an advisory vote on executive-compensation practices. Congress likely will extend the requirement to all listed companies. At many companies, individual directors are now subject to possible dismissal if they don't win a majority of votes cast during annual meetings.

No report alone, regardless of its source, will restore investor confidence, some governance specialists say. "The public wants to see good results, not just good principles," said Lucian Bebchuk, a Harvard Law School professor and head of its corporate-governance program.

The report suggests boards might avoid the "exorbitant" compensation often paid chief executives by evaluating incumbents partly on their grooming of possible successors. Studies show CEOs hired from the outside are paid more than those promoted from within. But only 36% of public companies have a plan for developing internal CEO candidates, an NACD survey last year of 703 directors concluded.

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Bonnie Hill, who sits on four corporate boards, says one of her prior boards several years ago slashed the annual bonus of a CEO she declines to identify because he resisted identifying potential successors. That "got his attention," she recalled. "The following year, we had someone in the pipeline" -- along with two external recruits.

Several boards already embrace certain steps proposed by the Washington, D.C.-based NACD. For example, the report recommends that boards relieve overworked audit committees by
assigning some risk oversight to other committees and tapping outside experts for risk advice. Every board committee at Aetna Inc. handles risk oversight to some extent and the audit panel coordinates those efforts, according to Barbara H. Franklin, an Aetna director who also is on Dow Chemical Co.’s board.

At Home Depot Inc., where Ms. Hill is the lead director, the board recently enlarged its involvement in corporate strategy -- another approach endorsed by the NACD.

At the request of CEO Frank Blake, Home Depot directors spent a Saturday in October discussing possible strategic shifts with top management. Ms. Hill said it was the first all-day strategy-planning session involving directors since she joined the board a decade ago. The discussion contributed to Home Depot's January decision to close its 34 Home Expo Design Centers, Ms. Hill said.

The NACD report also urges boards to constantly review their size and makeup "to ensure a close fit" with the company's strategic direction. Aetna and Dow Chemical directors go a step further. They recruit new members with "the expertise and experience to oversee [future] strategic thrusts," Ms. Franklin said. Their recruitment efforts sometimes begin years before an expected vacancy, she added.

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