How we can restore confidence in our public companies

The first step: stop talking about maximizing shareholder value as the be all and end all.

By Simon M. Lorne and Patricia F. Russo

American economic success has long depended on corporations, which drove a 20th century expansion of the middle class and unprecedented opportunities for increasing standards of living. But in the last decade that economic engine has been called into question, and we have seen an intense debate over our system of corporate governance. Restoring public confidence in our capitalist system and in its governance is critical to sustaining the economic resurgence we have recently experienced. The question is how to accomplish that goal.

Over the past year, we chaired a task force of The Conference Board Governance Center that was formed to examine this question. The task force brought together directors of leading institutional investors and board members of major public companies to determine if we could agree on actions each group could take to help restore and enhance trust in business.

Our first recommendation is critical. We need to stop talking about maximizing shareholder value as if it were an isolated consideration in leading a corporation. While the ultimate goal of a public company *is* to maximize shareholder value, most well run companies know that creating shareholder value can only be done on a sustainable basis by serving the constituents who create that value — the employees, customers, suppliers, communities and the environments in which the company operates.

We also discovered that both investors and companies agree that the directors should be central to governing public companies. Contrary to what is sometimes suggested, investors are not interested in managing corporations. Our legal system supports this division of labor: directors owe fiduciary duties to the company and all of its investors, while investors are free to act in their own interests and do not generally owe fiduciary duties to the corporation or to other investors. That being said, investors play an increasingly important role in the governance of public companies and corporate directors and managements are paying attention to what their investors are saying.

It follows that investors believe the single most important corporate governance factor is the quality of board oversight. But, research indicates that there are no bright-line tests for the quality of board oversight. There has been no demonstrated correlation between corporate performance and most of the standard categories (such as skills and experience) used to judge the quality of the board. Board quality is complex and nuanced and depends as much on interpersonal dynamics as individual skills and experience. We believe that there is now an opportunity for directors to come out from behind closed doors and let investors and the public get a feeling for board quality by knowing more about who is governing our public companies.

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Restoring confidence

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When investors vote

Investors, on their part, have a responsibility not only to have thoughtful voting policies but also to disclose those voting policies and how companies can contact the investors to discuss those policies. When investors decide to vote — and we are clear that there are situations in which investors may appropriately decide not to vote — they should devote sufficient time and resources to make informed voting decisions. If investors take advice from proxy advisors, they should use the proxy advisors' recommendations only as one data point to supplement their own analysis.

> BOARD QUALITY IS COMPLEX AND NUANCED AND DEPENDS AS MUCH ON INTERPERSONAL DYNAMICS AS INDIVIDUAL SKILLS AND EXPERIENCE.

Because proxy advisors play an important role in advising investors on voting on all matters, it is critical that the proxy advisors adhere to the highest standard of conduct in terms not only of avoidance of conflicts or appearances of conflict of interest, but also of transparency in their decision-making process.

Finally, the interaction of companies with their investors on matters of corporate governance depends on the facts and circumstances of each company and each investor. For many companies and investors, engagement will enhance trust and confidence. But not all companies or all investors need to engage directly with each other or engage all of the time. Investors are clear that over-engagement can lead to systemic overload and inefficient use of limited resources.

Similarly, direct engagement between directors of public companies and institutional investors can be beneficial in special circumstances. We endorse the principle that direct engagement involving directors should not be a routine method of engagement for most U.S. companies and for most investors. Many, perhaps most, topics of engagement do not require the participation of company directors any more than they require the participation of senior management or of the investor.

We are confident that if U.S. companies and their investors follow the recommendations of our task force and the recommendations of its advisory board's "Guidelines for Engagement," corporate governance will be improved and necessary public confidence and trust in our capitalist model will be enhanced. ■

The report generated by The Conference Board Task Force on Corporate/Investor Engagement can be accessed at http://www.conferenceboard.org/governance

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