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Spotlight on Boards

The ever-evolving challenges facing corporate boards prompt periodic updates to a snapshot of what is expected from the board of directors of a major public company—not just the legal rules, or the principles published by institutional investors and various corporate and investor associations, but also the aspirational “best practices” that have come to have equivalent influence on board and company behavior. So too, legislation like the Accountable Capitalism Act introduced by Senator Elizabeth Warren in 2018, and the position paper on the problems of shareholder capitalism and the merits of industrial policy by Senator Marco Rubio in 2019.

A very significant June decision by the Delaware Supreme Court interpreting the *Caremark* doctrine that limits director liability for an oversight failure to “utter failure to attempt to assure a reasonable information and reporting system exists” prompts this update. Our memo discussing the decision is available [here](#). The Court said to “satisfy their duty of loyalty,” “directors must make a good faith effort to implement an oversight system and then monitor it” themselves. Without more, the existence of management-level compliance programs is not enough for the directors to avoid *Caremark* exposure.

Today, boards are expected to:

- Recognize the heightened focus of investors on “purpose” and “culture” and an expanded notion of stakeholder interests that includes employees, customers, communities, the economy and society as a whole and work with management to develop metrics to enable the corporation to demonstrate their value;
- Be aware that ESG and sustainability have become major, mainstream governance topics that encompass a wide range of issues, such as climate change and other environmental risks; systemic financial stability; worker wages, training, retraining, healthcare and retirement; supply chain labor standards and consumer and product safety;
- Oversee corporate strategy (including purpose and culture) and the communication of that strategy to investors, keeping in mind that investors want to be assured not just about current risks and problems, but threats to long-term strategy from global, political, social, and technological developments;
- Work with management to review the corporation’s strategy, and related disclosures, in light of the annual letters to CEOs and directors, or other communications, from BlackRock, State Street, Vanguard, and other investors, describing the investors’

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expectations with respect to corporate strategy and how it is communicated;

- Set the “tone at the top” to create a corporate culture that gives priority to ethical standards, professionalism, integrity and compliance in setting and implementing both operating and strategic goals;
- Oversee and understand the corporation’s risk management, and compliance plans and efforts and how risk is taken into account in the corporation’s business decision-making; monitor risk management; respond to red flags if and when they arise;
- Choose the CEO, monitor the CEO’s and management’s performance and develop and keep current a succession plan;
- Have a lead independent director or a non-executive chair of the board who can facilitate the functioning of the board and assist management in engaging with investors;
- Together with the lead independent director or the non-executive chair, determine the agendas for board and committee meetings and work with management to ensure that appropriate information and sufficient time are available for full consideration of all matters;
- Determine the appropriate level of executive compensation and incentive structures, with awareness of the potential impact of compensation structures on business priorities and risk-taking, as well as investor and proxy advisor views on compensation;
- Develop a working partnership with the CEO and management and serve as a resource for management in charting the appropriate course for the corporation;
- Monitor and participate, as appropriate, in shareholder engagement efforts, evaluate corporate governance proposals, and work with management to anticipate possible takeover attempts and activist attacks in order to be able to address them more effectively, if they should occur;
- Meet at least annually with the team of company executives and outside advisors that will advise the corporation in the event of a takeover proposal or an activist attack;
- Be open to management inviting a major shareholder or even an activist to meet with the board to present the shareholder’s or activist’s opinion of the strategy and management of the corporation;

- Evaluate the individual director's, board's and committees' performance on a regular basis and consider the optimal board and committee composition and structure, including board refreshment, expertise and skill sets, independence and diversity, as well as the best way to communicate with investors regarding these issues;
- Review corporate governance guidelines and committee charters and workloads and tailor them to promote effective board and committee functioning;
- Be prepared to deal with crises; and
- Be prepared to take an active role in matters where the CEO may have a real or perceived conflict, including takeovers and attacks by activist hedge funds focused on the CEO.

To meet these expectations, major public companies should seek to:

- Have a sufficient number of directors to staff the requisite standing and special committees and to meet investor expectations for experience, expertise, diversity, and periodic refreshment;
- Compensate the directors commensurate with the time and effort that they are required to devote and the responsibility that they assume;
- Have directors who have knowledge of, and experience with, the corporation's businesses and with the geopolitical developments that affect it, even if this results in the board having more than one director who is not "independent";
- Have directors who are able to devote sufficient time to preparing for and attending board and committee meetings and engaging with investors;
- Provide the directors with the data that is critical to making sound decisions on performance, strategy, compensation and capital allocation;
- Provide the directors with regular tutorials by internal and external experts as part of expanded director education and to assure that the directors have the information and expertise they need to respond to disruption, evaluate current strategy and strategize beyond the horizon; and
- Maintain a truly collegial relationship among and between the company's senior executives and the members of the board that facilitates frank and vigorous discussion and enhances the board's role as strategic partner, evaluator, and monitor.

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