

write a regular column for DIRECTORS & BOARDS, and he has been our lead columnist since 1997.

THE VICE CHANCELLOR PRINCIPLE: Avoid doing or approving anything that could even remotely result in your winding up as a named defendant in the Delaware Chancery Court.

There is no way you can insulate yourself from being sued as a director. For example, directors are often sued upon approval of a buyout (even if the price is very generous by any objective financial measure), with boilerplate language in the complaint virtually identical to the hundreds of prior similar lawsuits. Complaints alleging violation by directors of the federal securities laws often exude a similar fragrance.



Hoffer Kaback

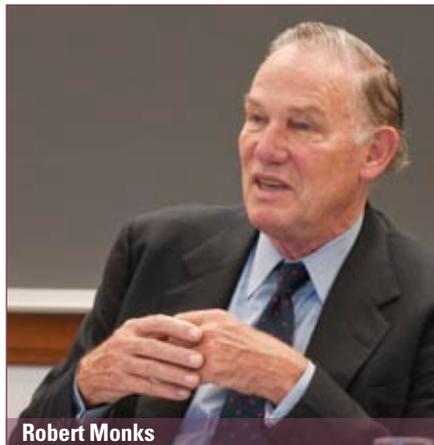
The tautology here is that if you have, in fact and in law, acted properly, then you have acted properly. You cannot act effectively as a director if you fear your own shadow;

the shareholders and the corporation are disserved by directors possessing such banana-spines. But if you have a sound appreciation of the niceties of the governing state and federal law (important), you abide by them (very important), you act with integrity (critical), and you act conscientiously as a prudent director should (critical), there is nothing to fear so long as the courts act rationally.

Separating the top jobs is a must

From *"The Great Divide: To Separate the Chairman and CEO Roles, or Not?"* [First Quarter 2010]. Robert Monks participated in this roundup of divergent views on a topic addressed numerous times over the years in the journal, and which began heating up again in the last several years as more companies moved to separate the roles. Monks founded Institutional Shareholder Services Inc. in 1985, and we have drawn upon his thoughtful approach to governance a number of times. In this passage from the article he reflected upon his experience as a director of Tyco International.

IT REQUIRES GREAT TALENT to be a CEO of a company. It is a lonely job that is best done by individuals with a good sense of their worth, but this personality trait usually comes with a need for power and control. The individuals compris-



Robert Monks

Boards: Heed these warning signs

From *"How to Avoid Firing Your CEO"* by Dee Soder and Richard M. Clarke [Fall 1999]. Soder and Clarke co-founded *The CEO Perspective Group*, a firm providing executive assessments and coaching for senior executives. Both have written several subsequent articles for the journal on the human dynamics of leadership.

Dee Soder

Early warning signs of trouble with a CEO®:

- Personality changes
- Change in personal appearance
- Not communicating to/knowledgeable about customers
- Unexpected resignation of board member or senior executives
- Reluctance to specifically discuss financial, sales, or other areas
- Poor communication and unavailability
- Missed targets
- Failure to take actions on timely basis
- Shift in time allocation
- Increase in lawsuits
- Excessive "trappings" of success
- Conflict among senior staff

Noticing signs of trouble early on can help a board — usually composed of strong-willed, opinionated people — save time, expense, and, hopefully, the incumbent CEO.

ing Tyco's board while I was there were probably typical of most boards. The members had no particular sense of governance, no sense of the dangers of absolute authority, and they took great pleasure in the company's seemingly limitless expansion potential and rising stock price. They were not bad people. [Former Tyco Chairman and CEO]

Dennis Kozlowski isn't a bad person. He could have functioned well under a suitable chairman. The money he was convicted of stealing would not have been denied him by a properly functioning board and compensation committee. The board was fully aware of the value that Dennis brought to the com-

pany, and that level of compensation was part of the culture of the times. In the words of President Nixon, “Mistakes were made,” and a tragic result for all ensued.

Not all independent chairpersons are helpful, but institutionalizing accountability creates a constructive energy in the governance of corporations. The tragedy for both Dennis Kozlowski and Tyco was huge, and it was unnecessary. In order to protect against problems resulting from the abuse of power, separation of roles of authority at the top of the corporation is essential.

Just say, ‘Whoops, I made a mistake’

From “*The Chairman and the Board: Charles Wohlstetter*” [Spring 1991]. Wohlstetter pulled no punches on a range of governance matters in this interview with editor James Kristie, unloading on institutional investors in particular, as in this passage from the article. He co-founded Contel Corp. in 1961, then a \$1.5 million telephone business, and merged it with GTE Corp. in 1991 in a \$6 billion transaction. He died in 1995.

INSTITUTIONAL INVESTORS keep saying, “I own the stock.” They don’t own a damn thing. What they do is pretend to manage funds that don’t belong to them — over which they have no ownership — so that if things go well, they can’t profit by it, and if they go badly, they’ll just blame it on the



Charles Wohlstetter

marketplace. They frequently can’t even be fired because they have civil service tenure. What they are is the same thing as a trustee would be in a will. They have a fiduciary responsibility. But there is no God-given information to them. They are not at birth injected with some kind of smart fluid that suggests that they even know how to run anything.

If an institutional investor is unhappy with management, he should sell out. That’s all he has to

do. Say “Whoops,” admit you made a mistake, and get out. It is not to say, “I made a mistake, therefore I’m going to punish you, and the way I’m going to do that is I’ll scratch my head and look in the phone book and get somebody who is going to tell you how to run your business.” What foolishness.

Out with the ‘confirm and conform’ model

From “*The Power and the Process*” by Paul G. Stern [Spring 1993]. At the time Stern was nonexecutive chairman of Northern Telecom Ltd. and serving on a number of major boards, including Dow Chemical Co. (which he continues to serve on to this

Sutton’s Laws

From “*Rules for Rock-Solid Governance*” by Gary Sutton [Spring 2004]. Sutton has served as a chief executive and board member of a number of public and private companies in his career as a specialist in business startups and turn-arounds. We liked this article and his strong operational and governance c.v. so much (and his strong opinions!) that we then invited him to become a regular columnist. His “Sutton’s Laws” column ran from 2004 to 2010. Three of his ‘Laws’ from his original article follow.



Gary Sutton

‘Sutton’s Laws’ won’t solve all the problems that boards face, but they can filter the bad boards from the good and help directors sleep better.

- The minutes should show split votes sometimes. If every vote is unanimous, there’s no governance or discussion going on. It’s okay and healthy if a director resigns every couple of years. When several quit, that’s nervous time. If nobody ever leaves, the job’s too cushy and there’s not enough jousting.

- Perhaps the silliest Sarbanes-Oxymoron rule is that the audit committee needs a finance or accounting expert. That’s way insufficient. Everybody on the board must be fluent in the

language of business, which is accounting. Absent that, they’re as effective as the Portuguese-speaking directors of a Lithuanian business. (I remember a director

in one board meeting wailing over the loss of all that goodwill from our balance sheet. If that joke requires explanation, stay far away from any board.)

- Directors should average 10 years older than the officers. Running a business requires energy. Spotting problems requires pattern recognition. Over-the-hill CEOs like me have lost the energy to manage effectively but have some “been there” advice that’s occasionally worth hearing. If they fire the CEO, it won’t be because they want the job themselves.

I’ve not always followed Sutton’s Laws. These are goals. When I was a CEO during the ‘80s and ‘90s, my board duties were simple. All I did was to keep those directors who thought me stupid from talking much with those who hadn’t decided yet. Those days are gone. Good thing.