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THE NOMINATING COMMITTEE AS A CORPORATE ACCOUNTABILITY MECHANISM

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* THE SECURITIES AND EXCHANGE COMMISSION, AS A MATTER OF POLICY, DISCLAIMS RESPONSIBILITY FOR SPEECHES BY ITS COMMISSIONERS. THE VIEWS EXPRESSED HEREIN ARE THOSE OF THE SPEAKER AND DO NOT NECESSARILY REFLECT THE VIEWS OF THE COMMISSION.

SINCE I BECAME A COMMISSIONER OF THE SECURITIES AND EXCHANGE COMMISSION I HAVE BEEN ASKED TO SPEAK ABOUT CORPORATE GOVERNANCE MORE OFTEN THAN I HAVE BEEN ASKED TO SPEAK ABOUT ANY OTHER TOPIC. A CYNIC MIGHT SAY THAT ONE RESPONSE TO AN INABILITY TO SOLVE A PROBLEM IS TO CALL FOR A REORGANIZATION. SINCE, AS INDIVIDUALS, WE ARE UNABLE TO AFFECT THE CONDUCT OF OUR LARGE PUBLIC CORPORATIONS, AND WE WE BELIEVE THAT THE GOVERNMENT IS EQUALLY INEFFECTIVE, WE CONCLUDE THAT THE GOVERNANCE OF OUR CORPORATIONS IS DEFECTIVE AND SHOULD BE REFORMED.

I BELIEVE THAT IT IS APPROPRIATE FOR US TO EXPLORE MECHANISMS FOR IMPROVING THE STRUCTURE OF BOARDS OF DIRECTORS AND THE RELATIONSHIPS BETWEEN BOARDS, MANAGEMENT, SHAREHOLDERS AND THE PUBLIC. I AM GOING TO TALK TO YOU TODAY ABOUT ONE OF THOSE MECHANISMS -- THE NOMINATING COMMITTEE.

HOWEVER, I WOULD NOT WANT OUR FOCUS ON CORPORATE GOVERNANCE TO OBSCURE THE EXPLORATION OF SOLUTIONS TO SUCH URGENT PROBLEMS AS UNEMPLOYMENT, INFLATION, POLLUTION AND OUR INCREASING DEPENDENCE ON FOREIGN ENERGY SOURCES. I WOULD NOT WANT US TO BECOME SO PREOCCUPIED WITH STRUCTURAL FORMS THAT WE BECOME INDIFFERENT TO THE GREAT NEED OF CORPORATE AMERICA TO RAISE CAPITAL TO FINANCE BUSINESS GROWTH.

DISPARATE CRITICS OF BUSINESS HAVE URGED CORPORATE REFORM TO MEET AN ASSORTMENT OF ANTI-SOCIAL AND UNLAWFUL ACTIVITIES ON THE PART OF CORPORATIONS AND CORPORATE EXECUTIVES. SOME OF THESE ACTIVITIES, SUCH AS THE BRIBERY OF PUBLIC OFFICIALS AT HOME AND ABROAD TO OBTAIN BUSINESS, AND THE USE OF CORPORATE FUNDS FOR PERSONAL EXTRAVAGANCES, ARE SUSCEPTIBLE OF SENSATIONALISM. IT WOULD BE EASY FOR ME TO INFURIATE AND TITILATE THIS AUDIENCE BY CATALOGUING THE MISCONDUCT OF MANAGEMENT IN RECENT CASES BROUGHT BY THE SEC AND CALL FOR RADICAL REFORM IN THE BOARD ROOM.

I WILL RESIST THAT TEMPTATION, HOWEVER, BECAUSE I DO NOT BELIEVE THAT THE CASE FOR CORPORATE REFORM RESTS ON EVIDENCE OF INCREASED CORPORATE MISCONDUCT. IN THE CORPORATE GOVERNANCE HEARINGS WHICH THE SEC HELD LAST FALL, RALPH NADER AND MARK GREEN TESTIFIED THAT "THE SYSTEM OF LAW THAT SUPPOSEDLY GOVERNS THE CORPORATION'S INTERNAL PROCESSES -- THE SYSTEM OF STATE CHARTERING -- HAS BROKEN DOWN." THEY CLAIMED THAT "CORPORATE CRIME HAS BEEN SHOWN TO EXIST AT LEVELS THAT SHOCKED BUSINESS ADHERENTS AND CRITICS ALIKE." I DO NOT AGREE THAT WE ARE WITNESSING A CORPORATE CRIME WAVE AS MUCH AS WE ARE WITNESSING INCREASED AND MORE EFFECTIVE PROSECUTION OF WHITE COLLAR CRIME BY THE SEC AND OTHER LAW ENFORCEMENT AGENCIES.

IN ANY EVENT, I WOULD NOT FAVOR GREATER GOVERNMENT REGULATION OF BUSINESS BY FEDERAL CHARTERING LEGISLATION, OR OTHER LEGISLATIVE INTERFERENCE WITH CORPORATE GOVERNANCE. THIS DOES NOT MEAN, HOWEVER, THAT I AM AGAINST CORPORATE REFORM OR THE IMPROVEMENT OF ETHICAL STANDARDS IN THE BUSINESS WORLD.

DISCUSSIONS ABOUT CORPORATE GOVERNANCE ARE NECESSARILY ADDRESSED TO QUESTIONS OF CORPORATE LEGITIMACY. I AGREE WITH THE BUSINESS ROUNDTABLE WHICH POINTED OUT IN ITS RECENT STATEMENT ON "THE ROLE AND COMPOSITION OF THE BOARD OF DIRECTORS OF THE LARGE PUBLICLY OWNED CORPORATION," --

> CORPORATE LEGITIMACY DERIVES IN THE FIRST INSTANCE FROM THE FACT THAT IN THE CONTEXT OF THE DEMOCRATIC SYSTEM, THE CORPORATION HAS PROVED THE MOST EFFECTIVE INSTRUMENT FOR CREATING THE PRODUCTS, SERVICES, JOBS AND EARNINGS BY WHICH THE MEMBERS OF SOCIETY CAN IMPROVE THEIR LIVES. (PP. 1-2)

YET, AS PAINE WEBBER INCORPORATED POINTED OUT IN ITS 1977 ANNUAL REPORT --

> MORE AND MORE AMERICANS SEEM TO BE LOSING CONFIDENCE IN FREE ENTERPRISE. ... THE QUESTION IS WHY. THERE IS, OF COURSE, NO SINGLE ANSWER. ... BUT ATTITUDES TOWARD FREE ENTERPRISE SEEM TO BE INFLUENCED PRIMARILY BY THE OVERALL PERFORMANCE OF THE ECONOMY. AND ONE MEASURE SEEMS TO BE MORE IMPORTANT THAN ALL THE REST: <u>DOES THE SYSTEM PROVIDE ENOUGH JOBS</u>? (P. II)

THE REPORT GOES ON TO EXPLAIN THAT JOB FORMATION DEPENDS ON CAPITAL FORMATION. IT IS CALCUALTED THAT ON THE AVERAGE ABOUT $37,000 OF CAPITAL HAS BEEN SAVED AND INVESTED TO SUPPORT EACH EXISTING JOB IN OUR ECONOMY. HOWEVER, THE SCARCITY OF CAPITAL IS BLUNTING OUR GROWTH AND PARTICULARLY OUR JOB-FORMING CAPACITY.

ONE DISTRESSING INDICATION OF THIS ECONOMIC MALAISE IS THE DECREASE IN THE DOLLAR VALUE OF SECURITIES REGISTERED BY CORPORATIONS UNDER THE SECURITIES ACT OF 1933 FOR SALE TO THE GENERAL PUBLIC. THIS AMOUNT HAS DECREASED FROM $42 BILLION IN THE COMMISSION'S FISCAL YEAR ENDED JUNE 30,1975 TO $36 BILLION IN THE YEAR ENDED JUNE 30, 1976 AND $31.8 BILLION DURING THE TWELVE MONTHS ENDING SEPTEMBER 30, 1977.

OUR NATIONAL ECONOMY HAS BEEN ADVERSELY AFFECTED BY WORLD WIDE SHIFTS IN ECONOMIC POWER AT A TIME WHEN GROUPS WHICH ARE AT THE BOTTOM AND ON THE SIDES OF OUR SOCIO-ECONOMIC HIERARCHY ARE DEMANDING ENTRY INTO OUR ESTABLISHMENT INSTITUTIONS. THE STRAIN WHICH HAS BEEN PLACED ON OUR GENERAL POLITICAL FABRIC IS FELT BY, AND TO SOME EXTENT DIVERTED TO, THE CORPORATE SECTOR. CORPORATE EXISTENCE IS DEPENDENT UPON THE GOVERNMENT. ACCORDINGLY, IN OUR DEMOCRATIC SOCIETY, CORPORATIONS ARE EXPECTED TO FUNCTION FOR THE PUBLIC GOOD AS WELL AS FOR THE PRIVATE BENEFIT OF MANAGEMENT AND SHAREHOLDERS.

BECAUSE OUR LARGE PUBLIC CORPORATIONS AFFECT SOCIETY IN MANY WAYS, THEY CAN NO LONGER MERELY BE CONCERNED WITH MAXIMIZING PROFITS. AS A RESULT OF SOCIAL CHANGES, CORPORATIONS ARE UNDER PRESSURE TO BE MORE RESPONSIVE TO POLITICAL AND ENVIRONMENTAL ISSUES WHICH AFFECT SOCIETY AS A WHOLE. FURTHER, RESPONSIBLE OPINION IN THE BUSINESS COMMUNITY HAS COME TO RECOGNIZE THAT SHAREHOLDERS HAVE AN INTEREST IN BALANCING THE SHORT-RANGE AND LONG-TERM PROFITABILITY OF A CORPORATION BY CONSIDERING THE POLITICAL AND SOCIAL VIABILITY OF AN ENTERPRISE OVER TIME INCLUDING ITS ABILITY TO ADJUST TO THE GLOBAL ENVIRONMENT IN WHICH IT OPERATES.

AS POINTED OUT IN A RECENT ARTICLE BY PROFESSOR WALTER WERNER, "MANAGEMENT, STOCK MARKET AND CORPORATE REFORM: BERLE AND MEANS RECONSIDERED," 77 COL. L. REV. 388 (1977), SOCIETY'S GOALS AND SHAREHOLDERS' GOALS MAY, AND IN THE PAST HAVE TENDED TO, COINCIDE, BUT THEY ALSO MAY CONFLICT. ALTHOUGH THE CORPORATION IS BOTH A BUSINESS ENTERPRISE OPERATED FOR PRIVATE GAINS AND A SOCIAL INSTITUTION, MANAGEMENTS TEND TO SUBORDINATE COMMUNITY TO SHAREHOLDER INTEREST IF THE SATISFACTION OF COMMUNITY DEMANDS IS LIKELY TO AFFECT SHAREHOLDERS ADVERSELY.

BY REASON OF OUR STATUTORY MANDATES AND BECAUSE OF OUR TRADITIONAL PREOCCUPATION WITH INVESTOR PROTECTION, THE SEC ALSO HAS FOCUSED PRIMARILY UPON SHAREHOLDERS' CONCERNS, RATHER THAN GENERAL ISSUES OF SOCIAL SIGNIFICANCE. TO THE EXTENT THAT THE CURRENT IMPETUS FOR CORPORATE REFORM ARISES FROM AN EFFORT TO SUBORDINATE SHAREHOLDER TO COMMUNITY GOALS, THE COMMISSION MAY BE FORCED TO BROADEN ITS TRADITIONAL SIGHTS.

IN A SOCIETY AS PLURALISTIC AS OURS, WHERE THE RELATIONSHIP BETWEEN GOVERNMENT AND BUSINESS IS BOTH ADVERSARIAL AND COOPERATIVE, SIGNIFICANT CHANGE IN OUR PUBLIC CORPORATIONS EVOLVES THROUGH AN INTERACTION OF GOVERNMENT AND PRIVATE SECTOR INITIATIVES. ALTHOUGH THE SEC HAS NO DIRECT OR SPECIFIC MANDATE TO STRUCTURE, OR ALTER THE STRUCTURE OF CORPORATE BOARDS, THE FORM OF ANY RESTRUCTURED BOARD MODEL CAN OBVIOUSLY BE INFLUENCED BY COMMISSION ACTION.

IN RECENT YEARS THE COMMISSION HAS OBTAINED VARIOUS TYPES OF ANCILLARY RELIEF IN NUMEROUS ADMINISTRATIVE AND COURT CASES WHICH REQUIRED SUBSTANTIAL ALTERATIONS IN THE STRUCTURE OF BOARDS OF DIRECTORS AND BOARD COMMITTEES.

SUCH ANCILLARY RELIEF HAS REQUIRED THAT CERTAIN NUMBERS OF INDEPENDENT DIRECTORS BE APPOINTED TO THE BOARDS OF DIRECTORS, OR THAT A NEW INDEPENDENT AUDIT COMMITTEE BE ESTABLISHED. MOREOVER, OFTEN THE ANCILLARY RELIEF HAS REQUIRED THAT A FULLY INDEPENDENT COMPLIANCE COMMITTEE AND AN EXECUTIVE COMMITTEE BE FORMED. USUALLY, APPOINTMENTS TO THE BOARD AND AUDIT COMMITTEE (AS WELL AS OTHER COMMITTEES) MUST BE APPROVED BY THE COMMISSION AND THE COURTS; AND BOARD COMMITTEES REQUIRED TO BE ESTABLISHED MUST MAINTAIN AN INDEPENDENT MAJORITY ACCEPTABLE TO THE COMMISSION.

THE COMMISSION'S POWERS UNDER THE SECURITIES EXCHANGE ACT OF 1934 CAN BE UTILIZED TO IMPACT CORPORATE GOVERNANCE. SINCE THE ADOPTION OF THE EXCHANGE ACT, THE COMMISSION HAS HAD BROAD AUTHORITY OVER RULES AND REGULATIONS OF THE VARIOUS REGISTERED EXCHANGES AND THE NASD INCLUDING CERTAIN OVERSIGHT POWERS CONCERNING LISTING REQUIREMENTS OF THE VARIOUS EXCHANGES. IN 1975, THE COMMISSION WAS GIVEN THE AUTHORITY TO DETERMINE WHICH SECURITIES SHOULD BE QUALIFIED FOR TRADING IN THE NATIONAL MARKET SYSTEM AND ITS JURISDICTION OVER SELF-REGULATORY ORGANIZATIONS WAS EXPANDED SIGNIFICANTLY. THE COMMISSION NOW IS REQUIRED TO APPROVE ALL PROPOSED RULE CHANGES OF THE SELF-REGULATORY ORGANIZATIONS AND IT HAS BROAD AUTHORITY TO AMEND SELF-REGULATORY RULES IN ANY RESPECT CONSISTENT WITH THE ACT.

It was in this regulatory framework that the Commission suggested and the New York Stock Exchange submitted its rule proposal requiring that by June of 1978 all listed domestic companies have an independent audit committee as part of their board structure.

A further Commission influence for change has been the hearings on corporate governance which the Commission held last fall and in which the Commission specifically asked questions concerning corporate accountability and how to achieve it. Corporate governance issues transcend the proxy rules. But the Commission can affect the internal affairs of corporations through its broad regulatory power under Section 14(a) of the Exchange Act to maintain, promote and improve fair corporate suffrage for shareholders. The Commission's focus on issues of corporate accountability reflects its concern about corporate structure. Our request for comment on whether or not structural change is warranted, and the national discussion which thus ensued, will hopefully have some influence on the process of reform.

Finally, the Commission's various disclosure requirements will in all likelihood bring about some change in corporate structure.

FOR EXAMPLE, AFTER ENDORSING THE CONCEPT OF INDEPENDENT AUDIT COMMITTEES FOR PUBLIC CORPORATIONS IN 1972, THE COMMISSION AMENDED ITS RULES IN 1974 TO REQUIRE DISCLOSURE IN PROXY STATEMENTS OF WHETHER OR NOT A CORPORATION HAS AN INDEPENDENT AUDIT COMMITTEE. THE REQUIREMENT TO DISCLOSE WHETHER OR NOT AN AUDIT COMMITTEE EXISTS HAS PRESUMABLY TENDED TO ENCOURAGE THE FORMATION OF SUCH COMMITTEES.

THE COMMISSION HAS TRADITIONALLY RELIED UPON THE PROPHYLACTIC EFFECT OF DISCLOSURE IN THE PROCESS OF REFORM. THE COMMISSION'S INTERPRETATIVE RELEASE CONCERNING DISCLOSURE OF EXECUTIVE REMUNERATION CLASSIFIED AS PERQUISITES IS A RECENT EXAMPLE. ALTHOUGH REMUNERATION OF CORPORATE MANAGEMENT IS ALREADY REQUIRED TO BE DISCLOSED, THE SCRUTINY OF PERQUISITES MAY WELL INFLUENCE THE ESTABLISHMENT OF BOARD COMPENSATION COMMITTEES.

ALTHOUGH MANY PEOPLE HAVE EXPRESSED SUPPORT FOR THE PROPOSAL TO INCREASE THE NUMBER OF INDEPENDENT DIRECTORS ON THE BOARD, SOME HAVE QUESTIONED WHETHER A SUFFICIENT NUMBER OF POTENTIAL COMPETENT INDEPENDENT DIRECTORS EXISTS TO AVOID THE PROBLEMS OF INTERLOCKING DIRECTORSHIPS. THIS WEEK THE SENATE COMMITTEE ON GOVERNMENTAL AFFAIRS ANNOUNCED ITS CONCLUSIONS THAT MOST OF THE NATION'S LARGEST CORPORATIONS WHICH REPRESENT 25 PERCENT OF THE ASSETS OF ALL U.S. CORPORATIONS ARE LINKED TOGETHER THROUGH INTERLOCKING DIRECTORSHIPS.

DESPITE THE COMMITTEE'S FINDINGS OF DIRECT OR INDIRECT INTERLOCKS, I BELIEVE THERE IS AMPLE TALENT AVAILABLE FOR DIRECTORSHIPS, PARTICULARLY IF BUSINESSES SEARCH FOR TALENT OUTSIDE OF THE CLOSED AND COZY SOCIAL NETWORKS OF EXISTING TOP MANAGEMENT. ONE WAY TO CONDUCT SUCH A SEARCH IS THROUGH THE MECHANISM OF A NOMINATING COMMITTEE. VESTING THE BOARD MEMBER SELECTION POWERS IN AN INDEPENDENT NOMINATING COMMITTEE SHOULD MINIMIZE THE PERCEIVED INDEBTEDNESS OF DIRECTORS, AND ESPECIALLY INDEPENDENT DIRECTORS, TO THE CHIEF EXECUTIVE TO WHOM THEY WOULD NO LONGER OWE THEIR APPOINTMENT.

THE ESTABLISHMENT OF NOMINATING COMMITTEES IS IN LINE WITH THE BALANCING OF ECONOMIC AND SOCIAL GOALS THAT I BELIEVE IS IMPORTANT. THE EXISTENCE OF A NOMINATING COMMITTEE COMPOSED ENTIRELY OR IN LARGE PART OF INDEPENDENT DIRECTORS MAY HELP ASSURE OR INCREASE THE ACCOUNTABILITY OF A BOARD OF DIRECTORS TO ITS SHAREHOLDERS AND POTENTIALLY TO THE PUBLIC. THIS COMMITTEE CAN BE THE SINGLE MOST EFFECTIVE FORCE IN IMPROVING CORPORATE GOVERNANCE BECAUSE OF ITS IMPACT OVER TIME ON THE COMPOSTION OF THE BOARD AND, ACCORDINGLY, THE SUCCESSION OF MANAGEMENT.

THE NOMINATING COMMITTEE SHOULD PROVIDE A BROAD RANGE OF VIEWPOINTS TO THE BOARD AND MAKE THE COMPANY MORE RESPONSIVE TO CHANGES IN POLITICAL AND SOCIAL, AS WELL AS ECONOMIC, TRENDS. AT THE SAME TIME, THE NOMINATING COMMITTEE IS NOT A MECHANISM WHICH ENTAILS RADICAL CHANGES IN EXISTING CORPORATE GOVERNANCE MECHANISMS. FURTHER, THE ESTABLISHMENT OF A NOMINATING COMMITTEE IS NOT COSTLY.

DESPITE MY ENTHUSIASM FOR THE NOMINATING COMMITTEE, I AM NOT PERSUADED THAT THE COMMISSION SHOULD REQUIRE OR URGE ALL PUBLIC COMPANIES, OR REQUEST THE EXCHANGES TO REQUIRE THEIR LISTED ISSUERS TO ESTABLISH NOMINATING COMMITTEES. CONGRESS WAS VERY MUCH CONCERNED THAT SHAREHOLDERS BE ASSURED "FAIR CORPORATE SUFFRAGE" WHEN THE SECURITIES EXCHANGE ACT OF 1934 WAS ENACTED. IT WAS ITS VIEW THAT

> MANAGEMENTS OF PROPERTIES OWNED BY THE INVESTING PUBLIC SHOULD NOT BE PERMITTED TO PERPETUATE THEMSELVES BY THE MISUSE OF CORPORATE PROXIES.

HOWEVER, CONGRESSIONAL INTENT WAS NOT TO REGIMENT BUSINESS. RATHER, CONGRESS INTENDED TO ENTRUST THE EXCHANGES, SUBJECT TO SOMEWHAT LIMITED COMMISSION REVIEW, WITH THE TASK OF ACCORDING TO SHAREHOLDERS FAIR SUFFRAGE ON THE THEORY THAT EXCHANGES ARE PUBLIC INSTITUTIONS WHICH MAKE POSSIBLE WIDE DISTRIBUTION OF SECURITIES.

THE LEGISLATIVE HISTORY OF THE EXCHANGE ACT INDICATES THAT CONGRESS HAD TWO GOALS IN ADOPTING SECTION 14 OF THAT ACT: TO PROMOTE FAIR CORPORATE SUFFRAGE AND TO CURTAIL MANAGEMENT'S DOMINANCE OF THE PROXY PROCESS. NOTWITHSTANDING ITS POTENTIAL BREADTH, SECTION 14(A) GENERALLY HAS BEEN REGARDED PRIMARILY AS A DISCLOSURE RATHER THAN A REGULATORY PROVISION.

The stock exchanges would have the authority to require listed companies to establish nominating committees and the SEC would have the right to review or propose such a rule under the 1975 Amendments. Nevertheless, some persons such as Professor William Cary, have urged the Commission to be prudent in attempting to require the Exchanges and self-regulatory agencies to effect corporate governance related reforms in this manner, and I am mindful of the general value of governmental self restraint in such matters.

The adoption of a disclosure requirement is certainly within our jurisdictional authority, however. I would therefore endorse a requirement that registrants state in their proxy material or their annual report to shareholders whether there is a nominating committee on the board and, if so, who the members are. In the view of the Advisory Committee on Corporate Disclosure it would be reasonable to require this type of disclosure because registrants are required already to identify the members of the Executive and the Audit Committees. Some of the persons who submitted letters of comment or testified at the Commission's hearings on the issue of corporate governance also endorsed disclosure regarding the nominating committee.

Two commentators, Professor Neil Jacoby and former SEC Commissioner Al Sommer, noted that disclosure would induce corporations to appoint outside directors to the committee. This would produce a wider range of candidates and greater consideration of their competence and would avoid the dangers of cronyism. Others argued, however, that such disclosure would result in meaningless boilerplate or that it would be unnecessary as to smaller companies which have no nominating committees.

Some commentators urged the Commission to require registrants to state other information about the nomination procedure, such as whether shareholder nominations were solicited or whether the committee's nominations were unanimous and the bases for the committee's selections. Professors Elliott Weiss and Donald Schwartz recently discussed their proposals for disclosure requirements that would govern the solicitation of proxies for election of directors. While they intended their disclosure approach to be evaluated as an integral unit, some of their recommendations are particularly interesting to me. They urge that SEC reporting provisions require registrants to describe the authority, responsibilities and operations of each standing committee of the board of directors.

DISCLOSURE ABOUT THE NOMINATING COMMITTEE, IN PARTICULAR, WOULD INCLUDE INFORMATION ABOUT THE NOMINEE SELECTION PROCEDURE AND CRITERIA. COMPANIES WOULD BE REQUIRED TO DISCUSS THE PROCESSES BY WHICH THE COMMITTEE SELECTS NEW NOMINEES FOR ELECTION AS DIRECTORS AND DETERMINES WHETHER TO RENOMINATE SITTING DIRECTORS. THEY WOULD BE REQUIRED TO STATE WHETHER THE COMMITTEE SOLICITS OR REVIEWS SHAREHOLDERS' RECOMMENDATIONS FOR NOMINEES TO FILL BOARD VACANCIES OR FOR REMOVAL OF BOARD MEMBERS AND TO DESCRIBE THE COMMITTEE'S SCREENING CRITERIA AND PROCEDURESTO ENABLE MORE INFORMED AND APPROPRIATE SHAREHOLDER PARTICIPATION.

I THINK THAT THIS DISCLOSURE APPROACH WOULD ENHANCE CORPORATE ACCOUNTABILITY AND INCREASE INVESTOR CONFIDENCE IN A COMPANY'S DECISION-MAKING PROCESS. THE DISCLOSURE REQUIREMENT MIGHT EVEN PROVIDE AN INCENTIVE TO THE BOARDS OF DIRECTORS OF COMPANIES TO ESTABLISH NOMINATING COMMITTEES COMPOSED OF INDEPENDENT DIRECTORS. FURTHERMORE, AS PROFESSORS WEISS AND SCHWARTZ SAID:

> FOR CORPORATIONS, THE PROPOSED SYSTEM COULD ASSIST IN ADDRESSING THE PROBLEM OF CORPORATE LETIGIMACY. LEGITIMACY, LIKE HAPPINESS, CANNOT BE OBTAINED DIRECTLY; RATHER IT IS A BY-PRODUCT OF OTHER ACTIVITIES. IN THE CASE OF LARGE CORPORATIONS, LEGITIMACY COULD DEVELOP AS A BY-PRODUCT OF PUBLIC CONFIDENCE IN THE SYSTEM OF GOVERNANCE AND ACCOUNTABILITY.

THOSE OF YOU WHO HAVE BEEN LISTENING ATTENTIVELY TO THIS SPEECH MAY BE WONDERING ABOUT AN APPARENT INCONSISTENCY IN MY REMARKS. ON THE ONE HAND I HAVE SAID THAT I DO NOT BELIEVE WE ARE BEING ENGULFED BY A CORPORATE CRIME WAVE WHICH REQUIRES THE ENACTMENT OF FEDERAL CHARTERING LEGISLATION, OR OTHER RADICAL REFORM IN CORPORATE GOVERNANCE. ON THE OTHER HAND I AM PROPOSING THAT CORPORATIONS INSTALL NOMINATING COMMITTEES.

MY ADVOCACY OF THE NOMINATING COMMITTEE IS AN EXPRESSION OF MY CONCERN THAT CORPORATIONS ARE NOT SUFFICIENTLY SENSITIVE TO THE CRITICISMS LEVELED AT THEM, AND ARE NOT ADAPTING TO TODAY'S CHALLENGES. I WOULD NOT WANT THE GOVERNMENT TO MANDATE PARTICULAR REFORMS IN CORPORATE GOVERNANCE BECAUSE I HAVE CONFIDENCE IN THE INNOVATIVE CAPABILITY OF THE PRIVATE SECTOR. BUT I BELIEVE THAT CORPORATIONS WHICH IGNORE THE VOICES CLAMORING FOR CORPORATE GOVERNANCE REFORMS DO SO AT THEIR PERIL.

THE DRAFTERS OF THE SECURITIES EXCHANGE ACT NOTED THAT THE ENACTMENT OF THAT ACT WAS NECESSARY BECAUSE:

> /T/HE LEADERS OF PRIVATE BUSINESS, WHETHER BECAUSE OF INERTIA, PRESSURE OF VESTED INTERESTS, LACK OF ORGANIZATION, OR OTHERWISE, HAVE NOT ... BEEN ABLE TO PROTECT THEMSELVES BY COMPELLING A CONTINUOUS AND ORDERLY PROGRAM OF CHANGE IN METHODS AND STANDARDS OF DOING BUSINESS TO MATCH THE DEGREE TO WHICH THE ECONOMIC SYSTEM HAS ITSELF BEEN CONSTANTLY CHANGING ...

I THINK CONGRESS STILL BELIEVES THAT LEGISLATION WILL BE NECESSARY TO EFFECT CORPORATE REFORM UNLESS CORPORATIONS ARE RESPONSIVE TO ECONOMIC AND SOCIAL CHANGES. ONE MINOR BUT POSSIBLY MEANINGFUL WAY IN WHICH CORPORATIONS CAN INCREASE THEIR RESPONSE TO THE EXPECTATIONS OF A SOCIETY UNDERGOING RAPID SOCIAL AND ECONOMIC CHANGE, IN MY VIEW, IS THROUGH THEIR ESTABLISHMENT OF NOMINATING COMMITTEES.

THE 54TH AMERICAN ASSEMBLY WHICH MET AND ISSUED A REPORT EARLIER THIS MONTH DECIDED THAT BOARDS OF DIRECTORS HAVE A PRIMARY ROLE IN INTERPRETING SOCIETY'S EXPECTATIONS AND STANDARDS FOR MANAGEMENT. THE ASSEMBLY EXPRESSED THE VIEW THAT NEW AND DIVERSE OUTSIDE VOICES, DEEPLY CONCERNED ABOUT GENERAL SOCIAL ISSUES SHOULD BE RECRUITED TO BOARDS OF DIRECTORS, THOUGH THEY SHOULD NOT BE CHOSEN TO REPRESENT SPECIFIC CONSTITUENCY INTERESTS. IN A SIMILAR VEIN, THE BUSINESS ROUNDTABLE RECENTLY STATED THAT "DIRECTORS SHOULD BE CHOSEN WITH A VIEW TO BRINGING TO THE WORK OF THE BOARD A VARIETY OF EXPERIENCE AND BACKGROUND. THE BROADER THE RANGE OF VIEWPOINTS PROVIDING INPUTS TO BOARD DELIBERATIONS, THE MORE LIKELY IT IS THAT THE ULTIMATE DECISION WILL BE IN THE LONG-RANGE CORPORATE INTEREST."