



THE IMPACT OF THE SARBANES-OXLEY ACT AND DEVELOPMENTS
CONCERNING INTERNATIONAL CONVERGENCE

TESTIMONY OF
GREG BENTLEY
CEO
BENTLEY SYSTEMS, INC.

before the
COMMITTEE ON BANKING, HOUSING, AND URBAN AFFAIRS
UNITED STATES SENATE
SEPTEMBER 9, 2004

Good afternoon, Mr. Chairman and members of the Committee. My name is Greg Bentley and I serve as the Chairman, President, and CEO of Bentley Systems, Inc., which is headquartered in Exton, Pennsylvania, near Philadelphia. I note the presence of Senator Santorum on this Committee and offer our sincere thanks for his service to the citizens of the Commonwealth and our nation.

As a member of the American Business Conference, founded by Arthur Levitt almost twenty-five years ago, I am honored to represent a growing majority of our economy—privately-held companies, and businesses smaller than you hear from most—regarding the Sarbanes-Oxley Act. Significantly, Bentley Systems remains a private company today, despite having filed our preliminary registration statement for an initial public offering in April 2002. We stayed the course in registration despite the seven-figure cost of hiring a second firm to re-audit our financials, replacing Arthur Andersen, our longtime auditors. In retrospect, the delay turned out to be fortuitous, as it coincided with the promulgation of Sarbanes-Oxley, whereupon we withdrew our offering.

I believe our experiences in this regard are relevant to your assessment of policy formulations to stimulate continued entrepreneurship, growth in the private sector, and a robust national economy. To us, this is so critical that in return, I will divulge what I've referred to as the "secret sauce" behind our business success to date. Last week, I heard a compelling articulation of an "ownership society", within which I want to advocate the importance and preservation of our company's "ownership culture".

Our 1,600 colleagues at Bentley Systems last weekend observed the company's twentieth birthday. During this lifetime we've grown from (literally) a "band of brothers" to about \$300 million of annual revenues, profitably and primarily self-financed. We rank among the larger firms within the global applications software industry—and among the very largest of those that have remained private companies. Our software supports the architecture, engineering, construction, and operations of the world's physical infrastructure. Our products are used, by way of example, to design the majority of

roadways, manufacturing plants, and water/utility networks in most major countries in the world.

In growing tenfold over the past decade, we have created over 700 jobs in the U.S., with average annual compensation here of over \$90,000; and our exports contribute over \$150 million per year to the U.S. trade balance.

While I and my four brothers (all of them engineers) who founded and control the company work hard and plan to continue doing so, we have always recognized that our growth and success is entirely to the credit of our colleagues, who comprise all the key assets for producing and vending our software. By 2002, the number of colleagues to whom we had granted stock options was approaching the limit of 500 (made famous recently by Google), above which, under current law, formal disclosures, and consequently now Sarbanes-Oxley adherence, are required. The motivation for our IPO filing was thus less to achieve *public* ownership per se, but rather to make available deserved liquidity for these option holders, to appropriately reward their ongoing efforts and results.

At this same time, it happens that I chaired the audit committee of a large public (S&P-500) IT services firm. As a consequence, my personal experience with the various emerging costs and burdens of Sarbanes-Oxley compliance led us to conclude that such costs and distractions would not be prudent for Bentley Systems at the time.

In summary—because I realize you have other witnesses to present the perspective of existing public companies—those costs and burdens are substantial, and are still increasing, and their ultimate extent is still uncertain, depending on how new audit standards end up getting put into practice. Most of us are prepared to accept that in the aggregate these costs are probably justifiable, to preserve confidence for public investors.

And frankly, many aspects of Sarbanes-Oxley represent sufficiently worthwhile notions (such as executive attestations, whistle-blower hotlines, and some degree of explicit and

audited internal controls documentation) that, though we expect to remain private for the foreseeable future, we've begun a deliberate (hence, relatively frugal) implementation process at Bentley Systems.

But beyond the new compliance costs, what settled Bentley's IPO withdrawal was the mismatch between new corporate governance requirements, and our own ownership culture. In particular, the Act obliged exchanges to promptly propose new listing standards, the drafts of which dictated, for the first time, a majority of independent directors, which we have never contemplated.

It remains especially implausible to me, candidly, that our founders would relinquish control to such potential new independent directors as would be willing to expose themselves to the "perfect storm" of liability risks unleashed by Sarbanes-Oxley, especially for new public companies.

To start with, I am afraid that an appropriately long-term management horizon to best serve long-term shareholders is inherently incompatible with infallible short-term earnings visibility. But even if consistent and predictable fundamental performance could be a given, I believe that current U.S. GAAP accounting standards make financial restatements more likely than not. This is because these Byzantine rules and picayune bureaucratic interpretations change frequently—and often with retroactive effect—superseding what should be constant and overriding principles for measuring financial performance with consistency.

From my lay standpoint, to the extent that convergence with international accounting standards would reinstate principles-based accounting rather than "rules-based" accounting, every CEO should favor such a change.

In the meantime, occasional downside earnings surprises are inevitable, with impact on stock prices. I believe that rational equity investors can and must (as they once did) take this in stride. Unfortunately, Sarbanes-Oxley has increased the very real apprehension

that hair-trigger plaintiffs' lawyers will misuse the Act's standards to exploit these "gotcha's" as windfall opportunities, sapping (and, deterring) competent and well-meaning management and boards, with their deadweight of expensive distraction.

From a public policy standpoint, in fact, I believe that relatively simple litigation reform could more immediately and effectively redress the excessive risk aversion that Sarbanes-Oxley has engendered, than complicated rework of its complexities.

Otherwise, growing and prospering companies like Bentley Systems will assuredly remain private indefinitely. Not only will IPO's (other than perhaps spin-outs) be less prevalent, but so will acquisitions of private companies by public companies, who would effectively incur unaddressed Sarbanes-Oxley liabilities.

Are there national interests that may be at risk when a larger segment of our economy consists of larger private companies? One could be concerned that investors in public equities will have fewer choices among smaller growth companies where more investment capital, on the margin, could provide higher overall returns. On the other hand, there is presently an abundance of equity funds seeking private-company investments. Presumably such investors prefer the long-term orientation of private managements, to the enforced relative fixation of public companies on short-term earnings.

It is also clear to me that this providential abundance of long-term equity capital has been fostered by the recent structural tax reforms. Rolling these back to any degree will reduce growth funding for our privately-led economy, while making them permanent will even more substantially increase the ability of firms like Bentley Systems to invest in faster growth of our exports and employment.

But financial capital, while essential, is far from sufficient for the U.S. to maintain and extend its world leadership in technology—such as the software which is key to growth in *all* of our industries, including those we serve at Bentley. In fact, financing would be

useless without the key ingredient in our Bentley recipe—the ownership culture by which we attract, incent, and reward the colleagues whose intellectual property creation we are all dependent upon.

Post-Sarbanes-Oxley, our recipe’s potency has been somewhat watered down, in a respect which I’m afraid is representative of American companies at large. But the good news is that I also think there can be some simple public-policy changes, within the purview of your Committee, which could in fact serve even to improve upon the original recipe.

My first modest proposal would be to exclude equity grants to employees from the applicable count of “securities holders,” so that larger private companies could extend their ownership culture to more than 500 colleagues without becoming subject to public-company regulatory burdens, since such grants aren’t the result of any securities purchase decisions.

I would also suggest a policy direction to update the *form* of ownership culture, which gets beyond the tedious controversy over option expensing. As a major shareholder myself, I am well aware of the costs of option grants, no matter where they are measured in financial statements.

But of course I am equally aware of their benefits, in our American success recipe. I support the pending legislation which would delay and circumscribe option expensing, but only because otherwise most companies are significantly reducing the breadth and scope of their option programs, without substitute ingredients to sustain their ownership cultures.

In fact, of greater concern to me, than their expensing, is that the negative attention to stock options has unfortunately associated with them the stigma of greed and corruption. On the other hand, this could open the door to fresh thinking.

Granting outright (or correspondingly restricted) shares instead of options would even more completely align employee incentives (to the downside as well as upside) with that of the stockholders at large. While under option expensing there would not be a relative accounting bias against this, unfortunately the employee would be subject to income tax upon vesting, without a source of liquidity other than prematurely selling the shares (if there's a public market), now that Sarbanes-Oxley precludes loans from the employer.

An evident solution would be to grant the stock into the employee's qualified retirement account, where its value could presumably accumulate indefinitely, tax-advantaged. The company could then even elect to pay a dividend on such shares, likewise tax-deferred. That would further leverage the secret sauce of ownership culture to focus companies on long-term cash-flow generation, while at the same time focusing employees on long-term, stable career development and retirement funds.

It happens that company contributions, in stock, to our U.S. colleagues' profit-sharing accounts are already made annually at Bentley Systems. These contributions are over and above the company's cash 401-K matches of colleagues' own cash contributions, so that this incentive is always incremental to baseline retirement financing, rather than a substitute. Also, many other companies take advantage of ESOP plans, authorized by Congress in acknowledgement that our national economic interests are served by encouraging broad employee ownership.

The problem with either means, as a candidate to replace broad employee stock options programs post-Sarbanes-Oxley, is that all such ERISA-permitted equity contributions must in effect be "non-discriminatory"—that is, in essentially the same proportions of cash compensation to all employees. However, in the U.S. (and at Bentley Systems) we have always recognized that our colleagues' efforts and results are NOT correspondingly distributed equally. The ownership culture can't generate its intended incentive leverage, when it's made into an entitlement.

So I would ask that you consider creating an exception under ERISA for discretionary outright grants of stock to employees, for the purposes traditionally served by option grants. While many of the Enron abuses have been appropriately curtailed through Sarbanes-Oxley and related policy developments, our company, our colleagues, and our country can least afford to curtail the potent economic force of long-term equity incentives. This ownership culture secret sauce should be restored and reinforced as a key ingredient in our corporate and national economic strategies.

Thank you very much for this opportunity, and I look forward to questions.

Greg Bentley

Gregory S. (Greg) Bentley has been CEO of Bentley Systems since 2000, President since 1995, and Chairman of the Board since 1994. When he joined his four founding brothers at Bentley Systems in 1991, the company had 35 employees and only R&D activities. Today Bentley Systems, Inc., with 1500 employees and 2003 revenues of \$260 million, provides software for the lifecycle of the world's infrastructure. The company's comprehensive portfolio for the building, plant, civil, and geospatial vertical markets spans architecture, engineering, construction (AEC) and operations. Bentley is the leading provider of AEC software to the Engineering News-Record Design 500 and major owner-operators.

Prior to 1991, Mr. Bentley founded and served as CEO of Devon Systems International, Inc., a provider of financial trading software.

Mr. Bentley earned a bachelor's degree in Decision Sciences in 1976 and a M.B.A. in Finance in 1977 (Summa Cum Laude with General Honors) from the Wharton School, University of Pennsylvania. He was a Presidential Scholar in 1973.

In 2003, Mr. Bentley was recognized as CEO of the Year by the Chester County Chamber of Commerce. He was the Chairman of Campaign 2000 for the United Way of Chester County, which surpassed its goal. He is a member of the Board of Overseers for the School of Design, University of Pennsylvania. Mr. Bentley was an Enterprise Awards finalist for the Eastern Technology Council's CEO of the Year in November 2002.

In July 2002, Mr. Bentley was selected to participate in the President's Crawford Economic Forum in Waco, Texas. He represented the technology industries in October 2002 in the "Productivity in the 21st Century" conference co-sponsored by the U.S. Department of Labor and the American Enterprise Institute. He frequently endeavors to contribute to governmental policy determinations by representing the Business Software Alliance and the American Business Conference.

Greg lives with his wife Caroline and four teen-aged children at Snowhill Farm in Unionville, Pennsylvania. He has served on the boards of the ARC of Chester County, and Camphill Soltane, a community for young adults with developmental disabilities. He is a member of the Church of the Advent in Kennett Square, and regularly enjoys tennis, karate, and equestrian events.