



**IMPLEMENTATION OF THE SARBANES-OXLEY ACT AND  
RESTORING INVESTOR CONFIDENCE**

**Testimony of John J. Castellani  
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**before the**

**Senate Committee on Banking, Housing and Urban Affairs**

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Good morning. My name is John Castellani, and I am President of The Business Roundtable, an association of CEOs of leading corporations with a combined workforce of more than 10 million employees in the United States and \$3.7 trillion in annual revenues. I appreciate this opportunity to share the Roundtable's views on implementation of the Sarbanes-Oxley Act and restoring investor confidence.

I would like to begin by commending this Committee for your efforts to strengthen corporate governance and restore investor confidence over the past two years. The Business Roundtable has been a leader in advocating corporate governance reforms for over three decades, beginning in the 1970s with our first statement on corporate governance and continuing through the 1980s and 1990s with numerous publications addressing corporate governance best practices. In May of 2002, we published our *Principles of Corporate Governance*, a set of best practices designed to guide corporate governance practices and further U.S. companies' ability to compete, create jobs and generate economic growth. The Roundtable strongly supported the Sarbanes-Oxley Act, and we have supported the SEC's efforts to implement it.

And a word of thanks to the SEC. Despite a tight rulemaking schedule, it took the time to consider every rule, weigh its consequences, and solicit – and listen to – input from investors, companies and others.

The Sarbanes-Oxley Act put a necessary spotlight on corporate governance and financial reporting. Our members have viewed the Act as an opportunity to enhance their corporate governance practices and financial reporting procedures. In addition, Roundtable companies have implemented – voluntarily at this point – many of the proposed New York Stock Exchange and NASDAQ corporate governance reforms, with independent boards of directors, entirely independent audit, nominating and compensation committees and written committee charters.

A recent survey of Roundtable companies shows that our members are committed to living up to the spirit, not just the letter, of all of these reforms.

For example, 88 percent of Roundtable companies report increased involvement in board and committee meetings by members of the audit, nominating and compensation committees, and over 90 percent report increased involvement by the board as a whole. In keeping with the spirit of the reforms, audit committees today have taken "ownership" of the relationship with independent auditors, making it clear that auditors report to the committee, not to management.

Roundtable companies also report a dramatic increase in director evaluations, with 70 percent of companies performing director evaluations this year compared to 44 percent in 2002. As we stated in our *Principles of Corporate Governance*, directors should serve only so long as they

add value to the board, and the recent rise in director evaluations reflects companies' renewed commitment to board quality and accountability.

The Business Roundtable supports enhanced communications with shareholders, and, to that end, we supported recent SEC efforts to increase disclosure about nominating committee processes and to require disclosure concerning shareholder communications with the board. In fact, two-thirds of Roundtable companies have discussed with their nominating committees a process to communicate and respond to shareholder proposals and inquiries. An equal number have a process in place to communicate and respond to shareholder nominations of board candidates.

Moreover, the Roundtable has strongly supported the New York Stock Exchange and NASDAQ proposals to require regularly scheduled executive sessions of independent directors. In fact, the independent directors of 55 percent of Roundtable companies expect to meet in executive session five or more times this year. In many cases, directors today are convening in executive session before or after each meeting of the full board.

The New York Stock Exchange also has proposed to require that a director be designated to preside at executive sessions of the independent directors. Our members agree that it is important to provide leadership for a company's independent directors. In our recent survey, 55 percent of Roundtable companies reported that they have named an independent lead director as either an independent chairman, lead director or presiding outside director. This indicates the diversity of approaches to board leadership that companies take, depending on their unique circumstances.

Finally, 8 in 10 Roundtable companies report that their boards of directors are at least 75 percent independent, and 9 in 10 report that at least two-thirds of their directors are independent, exceeding the proposed New York Stock Exchange and NASDAQ listing standard requirements. As we stated in our *Principles of Corporate Governance*, providing objective, independent judgment is at the core of the board's oversight function – a key to good corporate governance.

Although much progress has been made, implementation of the Sarbanes-Oxley Act is not complete. For example, the SEC provided an extended effective date for its rules relating to internal controls over financial reporting to give companies and their accounting firms time to comply on a better and more cost-effective basis. Nevertheless, these rules may prove to be the most costly of the Sarbanes-Oxley Act reforms.

I mention these costs not to begrudge them. Rather, many of the costs associated with Sarbanes-Oxley are necessary and appropriate. At the same time, we need to remember that business must satisfy the needs of a large set of stakeholders— our shareholders, our employees, our customers and the communities in which we operate. To do that, we must run our companies in an effective and ethical manner. In this regard, good corporate governance should be equated with high value for all of our shareholders and other stakeholders. We should not so overly focus on regulating the mechanics of corporate governance that we lose sight of creating that value.

We need to be mindful of the potential for over regulation of corporate governance becoming another overhang on the economy. The economy currently faces several overhangs: the war on

terrorism and the war in Iraq, the bursting of the bubble of the 1990s and the collapse of stock valuations, and the corporate scandals of the past 18 months. We must be careful that we do not go so far in creating obligations and restrictions in the name of corporate governance that we create another overhang. We do not want directors and managers to become so afraid to take risks that we stifle the entrepreneurial spirit that is an essential characteristic of American business.

All of us – Congress, the SEC, the securities markets and the corporate community – have worked hard to restore investor confidence over the past two years, and we are proud of those efforts. Nevertheless, as I said before, there is still work to be done. The SEC should move expeditiously to approve the proposed New York Stock Exchange and NASDAQ corporate governance listing standards, and companies should continue – as they have been doing – to set standards for transparency, honesty and fairness that go beyond the law and reflect a culture of integrity.

At the Business Roundtable, our companies will continue our work to improve corporate governance practices. We have a number of initiatives underway. First, we are examining how we can better train both current and future business leaders to enhance the role of ethics in their decision-making process. Second, we are working to bring more sense and transparency to executive compensation. Finally, we are continuing to develop and share best practices in corporate governance so that companies and their boards and management can learn what works most effectively.

Congress did its job in enacting the Sarbanes-Oxley Act, and the SEC is doing its job in implementing the Act. We recognize that the rest is up to us.