

## Corporate Leaders Bristle at Oversight

### *New regulations called a waste of time, money*

When a swirl of business scandals brought down the likes of Enron and WorldCom, Congress clamped down hard on corporate America.

Two years later, company executives are punching back.

Complaining loudly about the time and costs already associated with the new corporate governance rules, business leaders are scrambling to head off additional measures to force companies to deduct the cost of stock options and allow shareholders to nominate directors.

"Sometimes ... it's important to recognize when we have gone far enough," John Thain, chief executive officer of the New York Stock Exchange, said in a recent speech.

The new regulations, business leaders say, are forcing top-level managers and board members to waste precious time wading through financial data of dubious strategic value.

But shareholder rights groups view this backlash as a massive case of corporate amnesia about the problems that triggered these changes, even as a Houston grand jury has brought charges against one-time Enron Chairman Ken Lay.

"I think it's a bunch of whining," said Elliot Schwartz, director of research at the Washington-based Council of Institutional Investors.

The new regulations are an outgrowth of the Sarbanes-Oxley Act, the sweeping corporate regulation overhaul passed at the height of the uproar over Enron and the ensuing run of corporate accounting scandals.

That string of corporate implosions, earnings restatements and subsequent criminal probes put thousands of workers out on the street, cost investors billions of dollars and, according to the Justice Department, has led to more than 300 convictions and guilty pleas so far.

### **Section 404**

Sarbanes-Oxley imposed new criminal penalties for corporate wrongdoing, transformed the way the accounting sector is regulated and made corporate executives more accountable for the veracity of their financial reports.

Corporate executives have complained most vehemently about Section 404 of the law, which requires management to establish internal controls and warn shareholders of any weaknesses in those safeguards.

Critics complain that provision has prompted an avalanche of paperwork.

Sending board members financial reports 3 inches thick "is not necessarily effective," noted Beverly Behan, a partner with New York-based Mercer Delta Consulting.

Mercer Delta officials point to an unidentified board member of a major energy firm who complained that, as a member of the audit committee, he now has to attend 11 meetings a year, rather than two. Those gatherings cover "details that add little value but lots of work."

### **Compliance costs**

AMR Research, a Boston-based business research firm, has estimated American companies will spend a whopping \$5.5 billion this year complying with Sarbanes-Oxley, although shareholder rights groups are skeptical about such figures.

Initially, companies were supposed to comply with the Section 404 rules by June 15, but regulators granted them a five-month extension. According to a survey of senior auditors conducted by ACL Services Ltd. of Vancouver, British Columbia, and the Center for Continuous Auditing, based at Texas A&M University's Mays Business School, half of large corporations still hadn't finished even 60 percent of the work involved in meeting the filing requirements.

### **Corporate counterattack**

The corporate counterattack began as behind-the-scenes lobbying but has since broken out into a highly public debate.

The New York Stock Exchange's Thain, in a speech in May before the Economic Club of New York, called for a "sense of balance and perspective" in the effort to rebuild and maintain investor confidence.

Stock exchange officials declined to comment.

"Just as patients can be overmedicated to the detriment of their health, we need to use care in setting the proper dosage of reporting and governance requirements for business and markets," Thain said.

Thain said he keeps hearing the same refrain from corporate executives: "The pendulum has swung too far. The costs of compliance are too high. ... We'll avoid the risks. ... We'll delay our investments."

Thain blamed the new rules, in part, for a decline in foreign companies listing their stocks on the U.S. financial markets.

Fed, SEC response

Thain's remarks spurred former Federal Reserve Chairman Paul Volcker and one-time Securities and Exchange Commission Chairman Arthur Levitt Jr. to defend the changes.

In a piece for the Wall Street Journal, Volcker and Levitt argued the costs of compliance cannot be "too much to pay for a multibillion-dollar international company when compared to how much investors have lost — and stand to lose — if internal controls are not improved."

## Expensing issue

The outcry against Sarbanes-Oxley come as industry and government regulators are considering more regulations.

The Financial Accounting Standards Board, the private-sector group that writes the accounting rules, is considering a proposal that would require firms to calculate the value of an employee's stock option and treat that option as an expense.

The accounting board hopes to have the new rule in place for fiscal years after Dec. 15, 2005.

Groups like the Business Roundtable have called on the board to delay a new standard for some years. The group of corporate CEOs wants the board to first conduct a "market test" to determine how expensing might affect stock performance.

Stock options are especially popular with high-tech firms because their stock values can skyrocket quickly. "This is going to have a dramatic effect on the marketplace," said Tom Lehner, the Business Roundtable's director of public policy. The Securities and Exchange Commission, meanwhile, is mulling a proposal that could change the makeup of boardrooms.

The idea is to allow frustrated shareholders the chance to bypass the usually costly, time-consuming avenues for getting new blood on a corporate board.

The suggested rule change would allow shareholders controlling at least 1 percent of a company's stock to put a proposal in the proxy calling for new director candidates to be added to the ballot the following year. That trigger to add candidates would kick in automatically if at least 35 percent of shareholders withheld their votes for one or more directors.

Then, the dissident shareholders would have to garner support from at least 5 percent of the stockholders to actually nominate a candidate.

'Give me a break'

Last year, SEC Chairman William Donaldson threw his support behind the change.

Earlier this year, the Business Roundtable ran newspaper ads signed by 40 former CEOs — including Archie Dunham of ConocoPhillips, and Phil Carroll of Shell Oil Co. — warning the proposed rule could enable "large institutional investors with narrow short-term interests to infiltrate corporate boards."

Shareholder advocates have little patience with all the complaints about Sarbanes-Oxley.

"Give me a break," said Schwartz of the Council of Institutional Investors.

"These guys are very short-sighted. They have very short memories. They forgot what things were like when Sarbanes-Oxley was approved."

And he added, if company leaders are being more cautious, that's "just fine with me."