



## CORP. GOV. - STANLEY KELLER

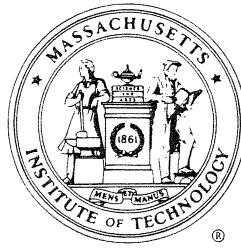
ENRON BACKGROUND: REALLY REINVENTED HOW TO DO BUSINESS IN THE 90'S: SELL OFF HARD ASSETS AND JUST TRADE. IT WAS THE 1000 LB. GORILLA; NUMBER 5 ON FORTUNE 100. A TRADING COMPANY REQUIRES THE TRUST OF ITS COUNTER-PARTIES. THEIR OFF BALANCE SHEET ARRANGEMENTS HOUSED ALL THE TROUBLE. THEY HAD A BLUE CHIP BOARD THAT STILL FAILED TO CATCH THE IRREGULARITIES.

SARBANES-OXLEY → DRIVEN THRU BY ENRON, THEN WORLD.COM. WAS RUSHED, AND HAS MANY FLAWS. PUT LOTS OF PRESSURE ON SEC TO WRITE IMPLEMENTING RULES.

CORP. REGULATION GENERALLY: STATE STATUTORY LAW → IS PERMISSIVE; TELLS YOU WHAT YOU CAN DO. CASE LAW SETS OUT THE DUTIES: DUTY OF CARE AND LOYALTY. YOU THEN HAVE AN OVERLAY OF FEDERAL LAW, WHICH HAS HISTORICALLY BEEN DISCLOSURE BASED AND FOCUSED ON PUBLIC COMPANIES. THEN, YOU HAVE THE LISTING STANDARDS PROMULGATED BY THE EXCHANGES. EXCHANGES ARE NOW DRIVING CHANGES IN CORPORATE GOVERNANCE.

S-O, THE ASSOCIATED REGULATIONS, AND UPDATED LISTING STANDARDS. FOCUS AREAS: (1) IMPROVE CORP. GOVERNANCE; (2) IMPROVE DISCLOSURE; (3) PERSONAL RESPONSIBILITY AND ACCOUNTABILITY; AND (4) REGULATION OF ASSOCIATED PROFESSIONALS.

(1) CORP. GOVERNANCE: NEED A MAJORITY OF INDEPENDENT DIRECTORS. MANAGEMENT HAS A BIG INCENTIVE TO MANIPULATE, AND BETTER OVERSIGHT IS REQUIRED. BUT, NO COMPANY HAS EVER BEEN GREAT BECAUSE OF THEIR INDEPENDENT DIRECTORS. CREATES A TENSION BETWEEN MANAGEMENT AND BOARDS. NO LONGER IS THERE REALLY A SINGLE BOARD; THERE ARE COMMITTEES, SUCH AS THE AUDIT COMMITTEE, WHICH HAS HIGHTENED STANDARDS INCLUDING A STIFF DEFINITION OF "INDEPENDENCE." AUDIT COMMITTEE IS RESPONSIBLE FOR OUTSIDE AUDITORS. A NOMINATING AND GOVERNANCE COMMITTEE HANDLES APPOINTMENT OF NEW BOARD MEMBERS AND PERFORMANCE EVALUATIONS. COMPENSATION COMMITTEE IS RESPONSIBLE FOR SETTING CEO SALARY.



BIG ISSUE: DO AUDIT COMMITTEE MEMBERS HAVE INCREASED LIABILITY EXPOSURE?  
YET TO BE ANSWERED. NOTE: SARBANES-OXLEY DOES NOT ADDRESS EXECUTIVE  
COMPENSATION IN A DIRECT WAY; THIS HAS BEEN CHALLENGED AS A MAJOR FLAW.  
OPTIONS ACCOUNTING IS THE PRIMARY PROBLEM. LEGAL COMPLIANCE FUNCTION →  
SEC REGS CREATE AN INCENTIVE FOR A SPECIAL COMMITTEE TO HANDLE LEGAL  
COMPLIANCE. SARBANES DOES PROHIBIT PERSONAL LOANS, DRIVEN BY TYCO.

(2) REGULATION OF PROFESSIONALS → SARBANES CREATED A QUASI-GOVERNMENT  
ENTITY TO REGULATE AUDITORS OF PUBLIC COMPANIES. SEVERED CONSULTING  
TO A LARGE EXTENT. GOVERNS AUDITING STANDARDS OR CAN DELEGATE,  
BUT HAS CHOSEN TO GOVERN. IT IS STILL RELYING ON FASB FOR GAAP.  
THIS IS A BIG CHANGE. WE ARE GETTING CLOSE TO GOVERNMENTAL  
AUDITING. LAWYERS: SEC WAS DIRECTED BY SARBANES TO ESTABLISH  
MINIMUM GUIDELINES FOR LAWYERS APPEARING BEFORE THE SEC, INCLUDING  
A RULE TO REPORT UP TO THE BOARD OF FINANCIAL IRREGULARITIES.  
SEC PROPOSED A NOISY WITHDRAWAL RULE → THIS IS A HUGE PROBLEM  
BECAUSE IT UNDERMINES THE PRINCIPLE OF CONFIDENTIALITY OF  
CLIENT COMMUNICATIONS. NO FINAL DECISION HAS BEEN MADE.  
PROPOSED RULE: IF YOU HAVE AN INDEPENDENT LEGAL COMPLIANCE  
COMMITTEE, LAWYER WOULD NOT HAVE TO REPORT OUT.

SOME IMPACTS: INCREASES IN SHAREHOLDER RESOLUTIONS, AND MORE  
ASSERTIVE SHAREHOLDER ACTIVISM FROM INSTITUTIONAL INVESTORS. FOCUS  
IS ON EXECUTIVE COMPENSATION, AND IS BEING PUSHED THRU THE  
EXCHANGE LISTING STANDARDS. SEC DETERMINES WHAT ISSUES ARE  
SUFFICIENT TO WARRANT SHAREHOLDER RESOLUTION. THIS AREA NEEDS  
TO BE REVIEWED. SOME FOREIGN COMPANIES ARE CHOOSING NOT TO LIST  
ON OUR EXCHANGES SO THEY DON'T HAVE TO DEAL WITH NEW REGS.

(3) PERSONAL ACCOUNTABILITY → CEO AND CFO MUST CERTIFY ACCURACY  
OF FINANCIAL STATEMENTS, INCLUDING CRIMINAL AND CIVIL PENALTIES,  
AND FORFEITURE OF OPTION PROFITS.



(4) DISCLOSURE. GOAL: IMPROVE QUALITY AND TIMELINESS OF DISCLOSURE. CURRENT REPORTING IS BEING OVERLAPED ON EXISTING PERIODIC REPORTING REQUIREMENTS. PROCESSES HAVE BEEN FORMALIZED, AND CERTIFICATION IS PART OF THE PROCESS. THE PRIMACY OF THE FINANCIAL STATEMENTS IS BEING REDUCED WHEN COMPARED TO THE MANAGEMENT'S DISCUSSION SECTION. ARE THEY ADEQUATELY DESCRIBING ONE TIME EVENTS, MAJOR RISKS, ETC? A RENEWED FOCUS ON THE BALANCE SHEET, UNEXPECTED LIABILITIES, AND LIQUIDITY, ALL MAINLY DRIVEN BY ENRON. RECOGNITION OF ASSUMPTIONS GOING INTO ACCOUNTING FIGURES, AND NEW EMPHASIS ON EXPLANATION.