

**DUTY OF DIRECTORS
IN PREVENTING CORPORATE WRONGDOING**

Prepared by

Michael M. Boone

and

Taylor H. Wilson

Haynes and Boone, LLP

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1. INTRODUCTION

1.1. Background. Today, corporate directors are well advised to take a hands-on approach in the development, implementation and maintenance of effective internal systems for detecting and deterring illegal and unethical corporate conduct. After all, boards of directors are increasingly facing private lawsuits whenever their company engages in corporate wrongdoing (e.g., issuing false financial statements, violating the Foreign Corrupt Practices Act or backdating stock options). By the same token, government regulators are very likely now to scrutinize board conduct where there has been illegal corporate activity. Without question, the Enron, WorldCom and other major corporate scandals have led to corporate directors being the focal point of regulatory efforts to improve legal compliance in corporate America. In sum, boards of directors are now expected to play a leading role in achieving legal compliance and ethical conduct within their corporations.

1.2. Summary Overview Of The Duty Of Care.

A. General Oversight Duties Of Directors. Under most state corporate statutes (e.g., Delaware General Corporation Law (“DGCL”) §141; Texas Business Corporation Act Art. 2.41), directors are generally charged with the responsibility of overseeing the affairs of the corporation. *However, state corporate statutes typically provide little, if any, guidance as to what these responsibilities actually require of directors.* So, the scope of director oversight in detecting and deterring wrongdoing under state corporate law has been largely left to judicial interpretation. The evolution of the judicial guidance in Delaware of the oversight responsibilities of directors is basically two-pronged: (1) duty to exercise care in making corporate decisions and (2) the duty to exercise care in preventing corporate wrongdoing.

B. Duty Of Care In Decision Making. Directors have a legal duty to exercise proper care in making decisions. However, directors are insulated against personal liability for their negligent conduct in decision making by reason of the Business Judgment Rule (“BJR”). The BJR requires that directors follow a reasonable decision making process which means that they must (i) devote adequate time to their decision making process, (ii) become fully informed of all material facts before making a decision, (iii) carefully deliberate the issues as a board before making a decision and (iv) then exercise their business judgment believing in good faith that their decision is in the best interests of the corporation. So, under the BJR, directors are culpable only in the case of gross negligence. But even there, director liability can be excused if the shareholders adopt in the corporate charter an exculpatory clause for director gross negligence. If such a charter provision is in place, it means that directors will only be liable for decisions made in “bad faith.” The “bad faith” standard requires a showing of knowing wrongdoing by directors which can be very difficult to prove in most cases.

C. Duty Of Care In Preventing Corporate Wrongdoing (“Duty To Monitor”).

As discussed more fully in Section 2 below, directors have a duty to prevent corporate wrongdoing. Through judicial interpretation, it is generally recognized that this duty requires of directors that:

- (1) They keep themselves informed about the affairs of the corporation.
- (2) They, in good faith, satisfy themselves that the corporation has in place effective internal systems for detecting and preventing corporate wrongdoing; and
- (3) They appropriately monitor the effectiveness of the internal reporting and legal compliance systems.

Special Note: The BJR does not give protection to directors in failure to prevent cases. The business judgment rule only applies to *claims challenging business decisions* of a board (see *Aronson v. Lewis*, 473 A.2d 805, 813 (Del. 1984) and *Pereira v. Cogan*, 52 Fed. Appx. 536 (S.D.N.Y. 2003)). In failure to prevent wrongdoing cases, the challenged conduct is about a failure to act, not about a board decision.

1.3. Scope And Purpose Of Outline. The purpose of this outline is to discuss what is expected of directors under state and federal law in the prevention of corporate wrongdoing. More specifically, the outline focuses on (i) the judicial development of the legal duties of directors in preventing corporate wrongdoing and (ii) the federal regulatory reforms (including reforms implemented under the Sarbanes-Oxley Act of 2002) that, directly or indirectly, call for directors to take responsibility for overseeing the goals of corporate legal compliance and ethical conduct. Finally, this outline discusses key steps that directors should consider in fulfilling these oversight responsibilities.

2. WHAT STATE CORPORATE LAW EXPECTS DIRECTORS TO DO IN PREVENTING CORPORATE WRONGDOING

2.1. Judicial Development Of The Standard Of Conduct Required Of Directors In Preventing Corporate Wrongdoing. While there are only a handful of leading Delaware decisions that speak to what is legally required of directors in carrying out their oversight duties in preventing corporate wrongdoing, the Delaware judiciary has now established a standard for directors to follow that is pragmatic and workable.

A. Graham Case (1963) – “Red Flag” Warning Standard. The first noteworthy Delaware case on the responsibility of directors in detecting and preventing corporate wrongdoing was *Graham v. Allis Chalmers Mfg. Co.*, 188 A2d 125 (Del. 1963). The defendant directors were alleged to have breached their oversight duties by having failed to prevent antitrust violations perpetrated by the company. The directors had no knowledge that company employees were engaged in such wrongdoings. In finding the directors not liable, the Delaware Supreme Court essentially held that in the normal course of things, directors do not have an affirmative duty to search out wrongful conduct by the corporation.

The court explained that “*Absent a cause for suspicion*, there is no duty upon directors to install and operate a corporate system of espionage to ferret out wrongdoing which they have no reason to suspect exists.” In sum, the *Graham* case stands for the proposition that in the absence of an obvious “red flag” warning of a problem, directors have no obligation to be out searching for wrongful corporate conduct. Thus, if directors receive notice of possible corporate wrongdoing (e.g., an employee whistle-blower complaint), the board will be expected to diligently investigate the matter in order to determine the validity of the complaint and whether any remedial action needs to be taken.

- B. Caremark Case (1996) – Affirmative Duty To Monitor.** In the *Caremark* case, the directors were alleged to have breached their duty to monitor the affairs of the corporation because they had failed to detect and deter wrongful conduct of employees who had been illegally making payments for referrals of Medicare and Medicaid patients. The directors had no knowledge or reason to know of this wrongful conduct so there was no evidence that the directors were guilty of violating the “red flag” warning standard announced in the *Graham* case. However, the Delaware Chancery Court pointed out that director oversight duties also require that directors have reasonable grounds for believing that the company has in place effective internal systems for detecting and preventing company wrongdoing. The *Caremark* court explained that:

“[I]t would . . . be a mistake to conclude that our Supreme Court’s statement in Graham concerning “espionage” means that corporate boards may satisfy their obligation to be reasonably informed concerning the corporation, without assuring themselves that information and reporting systems exist in the organization that are reasonably designed to provide to senior management and to the board itself timely, accurate information sufficient to allow management and the board, each within its scope, to reach informed judgments concerning both the corporation’s compliance with law and its business performance.”

Since the decision, the *Caremark* case has been cited many times for the proposition that in fulfilling their oversight duties, directors are expected to have in place reasonable systems for detecting and preventing wrongful conduct by the company. However, the *Caremark* case adopted a high standard for proving that directors have breached this responsibility. The court held that liability attaches only when there is “*a sustained or systematic failure to exercise oversight*” or there has been “*an utter legal failure to attempt to ensure a reporting and information system.*”

- C. Stone Case (2006) – Delaware Supreme Court Upholds Caremark.** In *Stone v. Ritter*, 911 A2d 362 (Del. 2006), the Delaware Supreme Court for the first time directly addressed the conclusions expressed in *Caremark* on director legal responsibilities for corporate legal compliance. There a Tennessee bank branch of AmSouth Corporation was used by some customers in carrying out their unlawful Ponzi scheme to defraud investors. In its aftermath, government investigators

found that AmSouth had violated certain federal anti-money-laundering laws by failing to file Suspicious Activity Reports with the regulators. Moreover, they concluded that AmSouth's systems for detecting and preventing violations of anti-money-laundering statutes were "materially deficient" and lacked "adequate board and management oversight." In settling resulting civil and criminal charges, AmSouth paid \$50 million in fines and penalties. Subsequently, a stockholder derivative lawsuit was brought against AmSouth's directors for damages resulting from their failure to prevent such wrongdoing.

Like the directors in *Caremark*, the AmSouth directors also had no "red flag" warnings of the corporate wrongdoings so the *Graham* duty to pursue obvious signs of wrongdoing was not applicable. The derivative suit alleged a so-called *Caremark* claim that the AmSouth directors had breached their fiduciary duties by failing to properly satisfy themselves that the company had in place effective systems for detecting and preventing illegal activity. In affirming the dismissal of the lawsuit against the directors, the Delaware Supreme Court said:

"We hold that Caremark articulates the necessary conditions predicate for director oversight liability: (a) the directors utterly failed to implement any reporting or information system or controls, or (b) having implemented such a system or controls, consciously failed to monitor or oversee its operations thus disabling themselves from being informed of risks or problems requiring their attention."

The court then explained that director "oversight liability" draws directly from the concept of director bad faith as discussed in its *In re Walt Disney Derivative Litigation*, 906 A2d 27 (Del. 2006), decision. In that connection, the court announced that the duty to act in good faith to prevent corporate wrongdoing is not a stand alone fiduciary duty, but instead is a "subsidiary element" of the directors' duty of loyalty. While the *Caremark* decision had previously been viewed as holding that an alleged violation of the duty to monitor falls under the duty of care, the Delaware Supreme Court made it clear that a *Caremark* claim is in fact a duty of loyalty claim. That being the case, it is important to recognize that a *Caremark* claim asserted against directors *does not fall within the protection of an exculpation clause in a corporate charter nor are directors afforded protection from liability under the business judgment rule against such a claim*. In sum, a *Caremark/Stone* claim goes to intent (state of mind) of the defendant-directors as opposed to whether they exercised proper care in gathering information about their company's activities. So, to prove a breach of the duty to prevent corporate wrongdoing "*requires a showing that the directors knew that they were not discharging their fiduciary duties.*"

In concluding that the plaintiffs had failed to adequately plead bad faith conduct on the part of the AmSouth directors, the court pointed to a report of KPMG that evaluated AmSouth's compliance programs. The KPMG report found that AmSouth's board of directors had "dedicated considerable resources" to the compliance programs and had put in place "numerous procedures and systems to

attempt to ensure compliance.” Moreover, the court took special notice of the fact that the board had “at various times enacted written policies and procedures designed to ensure compliance.” The fact that the AmSouth directors had made a conscious “good faith” effort to meet their oversight duties in striving to deter illegal conduct was determinative of the case being dismissed.

D. Lessons Learned. In order for directors to meet the *Caremark/Stone* oversight standard in preventing corporate wrongdoing, directors must consciously satisfy themselves that the company has implemented effective internal monitoring and reporting systems specifically designed to detect and prevent illegal conduct by the company. While corporate directors are not expected to guarantee that no corporate wrongdoing will ever occur, they will be held personally accountable if they have not made a good faith effort to see that the company has in place sound programs that promote legal compliance. To be sure, director oversight responsibilities for corporate legal and ethical conduct cannot be taken lightly in the post-Enron era. Directors have to be educated about the company’s compliance systems and their effectiveness.

2.2. Potential Intersection Of Caremark/Stone Duties And The Federal Regulatory Expectations Of Directors In Preventing Corporate Wrongdoing. Inasmuch as independent directors are assigned direct oversight responsibilities (e.g. the oversight of employee whistle-blower complaints) as well as certain indirect oversight responsibilities under the post-Enron regulatory reforms (as discussed in Section 3 below), it is predictable that the courts may in the future find that a failure to perform these responsibilities constitutes a breach of the duty to monitor even though private individuals have no standing to sue under the Sarbanes-Oxley Act to enforce such mandates. In sum, the fiduciary oversight responsibilities of directors under state law may give teeth to the post-Enron regulatory requirements from a private litigant’s standpoint.

3. WHAT FEDERAL LAW EXPECTS DIRECTORS TO DO IN PREVENTING CORPORATE WRONGDOING.

3.1. Overview. Today, the U.S. Congress and federal regulators expect directors to play a pivotal role in bringing about corporate legal compliance and ethical conduct. Perhaps the earliest federal statute aimed at curtailing corporate wrongdoing was the Foreign Corrupt Practices Act of 1977 (“*FCPA*”) which prohibits the bribing of foreign officials. The FCPA requires U.S. public companies to put in place certain record keeping and internal financial controls to detect and prevent such payments. While the FCPA does not directly impose duties on directors in seeing that the act is complied with, it is fair to say that over the past 30 years, the FCPA has made boards of directors much more aware of the need to develop programs aimed at preventing corporate bribery domestically as well as internationally. Since the adoption of the FCPA, other federal regulatory reforms have promoted the implementation of legal compliance programs. For instance, federal statutes and regulations have materially impacted legal compliance programs of companies in the banking, securities, health care, pharmaceutical and other specialized industries. In a similar vein, federal regulators (e.g., U.S. Department of Justice and the Securities and Exchange

Commission) have impacted company compliance programs by giving written guidance on what is expected in effective compliance systems if a company is to mitigate possible regulatory action. Finally, in settling government investigations, federal regulators have imposed on companies changes in their programs and policies with the objective of improving legal compliance. This overall federal regulatory framework must be considered carefully by boards in establishing policies and procedures aimed at achieving corporate compliance.

- 3.2. Expectations Of Directors Under The Federal Sentencing Guidelines In Preventing Corporate Wrongdoing.** The United States Sentencing Guidelines for Organizations (“Sentencing Guidelines”) were originally promulgated in 1991 in an attempt to influence corporate behavior – both before and after wrongdoing occurs – by providing for lesser sentencing sanctions against companies which implement legal compliance programs that are adequately designed to detect and deter corporate criminal conduct. *The Sentencing Guidelines have probably been the greatest catalyst for the development of legal compliance programs across corporate America.* The Sentencing Guidelines have been very instructive to companies in fashioning effective compliance programs.

In 2004, the Sentencing Guidelines were amended in the aftermath of the corporate scandals that spawned the post-Enron regulatory reforms. These amendments were aimed at strengthening the requirements of legal compliance programs. Most importantly, they have imposed greater duties on directors in implementing and monitoring compliance programs. *The amendments require that (i) directors be “knowledgeable about the content and operations of the compliance and ethics programs,” (ii) the person in charge of the compliance program have direct access to the board (or an appropriate board committee), (iii) directors take the compliance training programs and (iv) the effectiveness of the company’s compliance programs be evaluated annually.*

Importantly, the 2004 amendments made it abundantly clear that effective compliance programs were those that promoted an internal culture of ethical conduct and of striving to be legally compliant. Printing a code of conduct and distributing it to employees and providing training on compliance policies and procedures does not alone lead to proper conduct. There must also be an internal culture that strives to act right.

It should also be noted that the U.S. Department of Justice, the Securities Exchange Commission and other governmental agencies have from time to time given guidance to corporate America as to what they expect to see in an effective compliance program. For instance, the U.S. Department of Justice’s so-called Thompson Memo identified nine factors that federal prosecutors will consider in making charging decisions with respect to a business organization. Likewise, the SEC issued what is known as the Seaboard Release (Securities Exchange Act Release No. 34-44969 (2001)) which sets forth factors (including the presence and effectiveness of compliance procedures and policies) that the SEC will take into account in deciding whether or not to charge a company with securities law violations. These kinds of regulatory pronouncements can also be instructive in crafting compliance programs.

- 3.3. **Expectations Of Directors Under The Sarbanes-Oxley Reforms In Preventing Corporate Wrongdoing.** The Sarbanes-Oxley regulatory reforms have expanded, directly and indirectly, the oversight functions of independent directors with respect to legal compliance by corporation. Many of these reforms have mandated changes in corporate compliance programs.

A. Direct Oversight Responsibilities Of Independent Directors .

- (1) **Independent Directors Must Oversee Employee Whistle-Blower Complaints.** Under Section 301 of the Sarbanes-Oxley Act (“SOA”), a company’s audit committee (which consists solely of independent directors) is required to establish procedures for receiving, retaining and responding to anonymous and confidential complaints from employees regarding accounting, internal controls and auditing matters. *In view of how Enron’s management handled the infamous Sherron Watkins complaint about Enron’s accounting practices, Congress saw a need for independent directors rather than management to have sole control over the receipt and handling of whistle-blower complaints.* The audit committee should be given total discretion in setting its policies and procedures.
- (2) **Independent Directors Must Oversee Lawyer Whistle-Blower Complaints.** Under Section 307 of Sarbanes-Oxley Act (“SOA”), Congress attempted to correct what it perceived to be weaknesses in the way lawyers handled matters involving wrongful conduct by a client. Lawyers who provide legal advice to a public company with respect to SEC matters and who become aware of evidence of an actual violation of (i) securities laws, (ii) fiduciary duty laws or (iii) other federal or state law, have a duty to report the information “up the ladder.” The lawyer must report first to the chief legal officer of the company and if this does not result in an appropriate response, then up to the CEO. If both of these give unsatisfactory responses, the lawyer must then report the matter to the audit committee (or if one is in place, a Qualified Legal Compliance Committee consisting solely of independent directors) or to the board of directors. *In sum, the independent directors, as opposed to management, have been made the final arbiter of how a company will handle a lawyer’s discovery of unlawful conduct.*
- (3) **Independent Directors Must Oversee Waivers Of Corporate Code Of Conduct.** NYSE Rule 303A.10 and NASDAQ Rule 4350(n) require that listed companies adopt a code of conduct for directors, officers and employees. A code is to cover such things as conflicts of interest, compliance with law and the reporting of unethical behavior and illegal conduct. *Any waiver of the code for a director or an executive officer must be approved by the board (of which the independent directors are the majority) and then promptly disclosed to the public through a Form 8-K filing.* Except for SOA and related SEC requirements that public companies disclose in their annual reports whether or not they have adopted a code of ethics applicable to the CEO, CFO and controller (and, if not, why not), the

post-Enron regulatory scheme does not require the independent directors to oversee a company's code of conduct. However, in view of the new expectations of independent directors, it would be wise for independent directors to satisfy themselves as to the adequacy and effectiveness of their code of conduct. The SEC regulations require that (i) a code be reasonably designed to deter wrongdoing and to promote ethical conduct including making proper public disclosures and (ii) all amendments to a code be promptly disclosed to the public.

- (4) **Independent Directors Must Oversee Public Comments** The NYSE commentary to its Rule 303A.03 requires that a director ("*Presiding Director*") preside over executive sessions of the non-management directors (see Section 2.3 above) and that the name of the Presiding Director be identified in the Company's annual proxy statement. *Most importantly, the company is also required to disclose in its annual meeting proxy statement how a stockholder or other interested party can contact the Presiding Director or the non-management directors as a group. What this means is that interested parties are provided a way by which they can communicate their concerns to the independent directors.* There is no comparable provision in the NASDAQ Rules.

B. Indirect Oversight Responsibilities Of Independent Directors

- (1) **Overview.** The Sarbanes-Oxley regulatory scheme is aimed at holding corporate management and directors accountable for the accuracy of corporate disclosures. In particular, the SOA has focused on the CEO and CFO because they are directly responsible for the way a company operates, including compliance with applicable laws and regulations. In that regard, these reforms have imposed on the principal executive officer ("*CEO*") and the principal financial officer ("*CFO*") certain certification and assessment duties that are aimed at assuring public disclosures and financial reporting. *Interestingly, these requirements of corporate executives have a spill-over effect on an independent director's fiduciary duty to monitor.* These federally mandated duties of corporate executives clearly fall within the oversight responsibilities of directors. Accordingly, boards are expected to be proactive in periodically satisfying themselves that the duties imposed on the CEO and CFO are being reasonably performed with the help of information reporting systems that are reliable and effective. Below is a review of the oversight responsibilities of independent directors and of the CEO and CFO with respect to a public company's legal compliance and financial reporting that arise under the new federal regulatory scheme.
- (2) **Required CEO/CFO Certification Of The Accuracy Of 10-Qs And 10-Ks.** Section 302(1) through (3) of the SOA requires the CEO and CFO of public companies to certify the accuracy of annual reports on Form 10-K and quarterly reports on Form 10-Q. Securities Exchange Act of 1934 ("*Exchange Act*") Rules 13a-14 and 15d-14 that implement Section 302 require that the CEO and CFO certify in such reports that: (i) the signing

officers have reviewed the report; (ii) based on the officer's knowledge, the report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made not misleading and (iii) based on such officer's knowledge, the financial statements and other information included in the report fairly present in all material respects the financial condition, results of operations and cash flows of the company as of, and for, the periods presented in the report.

- (3) **Required CEO/CFO Certification Of The Quality Of Internal Controls.** Section 302(4) requires the CEO and CFO to certify in such 10-Q and 10-K reports that they (i) are responsible for establishing and maintaining internal controls over financial reporting, and (ii) have designed such internal controls over financial reporting to ensure that material information relating to the company and its subsidiaries is made known to the CEO and CFO by others within those entities. SEC Rules 13a-15 and 15d-15 implement Section 302(4).
- (4) **Required CEO/CFO Certification Of The Quality Of Disclosure Controls And Procedures.** Rules 13a-14 and 15d-14 require the CEO and CFO to certify in such 10-Q and 10-K reports that they (i) have designed such disclosure controls and procedures to ensure that material information is made known to them on a timely basis, (ii) evaluated the effectiveness of the disclosure controls and procedures within 90 days prior to the filing date, and (iii) presented in the filing their conclusions about effectiveness of the disclosure controls. These duties are intertwined with their duties described in Section 3.3.
- (5) **Required CEO Certification Of NYSE Compliance.** NYSE Rule 303A.12 requires the CEO of each listed company to annually certify to the NYSE that such person is not aware of any violation by the company of the NYSE corporate governance listing requirements. This certification must be disclosed by the company in its annual report to stockholders. There is no similar certification required by NASDAQ Rules.
- (6) **Required Management Assessment Of Internal Controls.** Section 404(a) of the SOA mandates that each company's Form 10-K shall contain an internal control report that (i) states the responsibility of management for establishing and maintaining adequate internal control systems and (ii) contains management's assessment, at year-end, of the effectiveness of such internal controls. Section 404(b) also requires the external auditor to attest to and report on management's assessment of such internal control systems.

- (7) **Required Maintenance And Assessment Of Disclosure Controls And Procedures.** Rules 13a-15 and 15d-15 require all companies that file reports under the Exchange Act to (i) maintain disclosure controls and procedures and (ii) within the 90-day period prior to the filing date of each report certified (as described in Section 3.3 and 3.4 *supra*) conduct an evaluation of the effectiveness of those controls with the participation of the company's management, including the CEO and CFO.

4. **STEPS DIRECTORS SHOULD CONSIDER TAKING IN FULFILLING THEIR OVERSIGHT DUTIES IN PREVENTING CORPORATE WRONGDOING.**

- 4.1. **Be Hands On.** Suffice it to say, directors must be directly involved in the development, implementation and monitoring of compliance programs and systems. While a Compliance Committee consisting of independent directors or some other appropriate board committee (e.g., the Audit Committee) may be charged with the first-line oversight responsibilities due to the significant nature of the company's compliance tasks, it is still imperative that the whole board understand and periodically review and evaluate the effectiveness of the compliance programs.
- 4.2. **Craft A Program That Fits The Company.** As has been said many times, "one size does not fit all" when it comes to corporate compliance programs. That means a company cannot afford to simply markup and adopt another company's compliance programs and policies and procedures. A company's legal compliance program needs to be tailor-made to fit the company's operations, organizational structure, industry issues, compliance risks and other factors particular to the company. Of course, a board of directors can learn from the programs of industry competitors, trade association compliance guidelines, U.S. Sentencing Guidelines and the like in formulating an effective compliance program.
- 4.3. **Diligently Conduct A Risk Assessment.** The starting point in the development of a sound compliance program is for the board of directors to oversee a risk analysis of legal compliance within the company. Such factors as the likelihood that a specific violation might occur, the seriousness of such a violation and the company's track record in preventing such a violation must be carefully weighed in making a risk assessment. In that regard, an effective compliance program should include a continuous risk assessment process.
- 4.4. **Properly Align The Compliance Systems With The Compliance Risks.** A board needs to satisfy itself that its compliance policies and procedures are properly aligned with the risks identified by the company's risk assessment. In a similar vein, a board should also be pro-active in seeing that the company's code of ethics ties back to what the company does day-to-day in conducting its business.
- 4.5. **Develop Reliable Monitoring Systems.** Directors also need to be satisfied that the company has in place adequate monitoring and evaluation systems to ensure that the compliance programs are doing what they are supposed to do. Moreover, these monitoring systems need to provide for appropriate and timely remedial actions when and if a legal violation occurs.

- 4.6. **Put Responsible People In Charge.** Without doubt, as contemplated by the Sentencing Guidelines, it is incumbent on directors to appoint a high-level person to be directly in charge of the day-to-day administration and enforcement of the company's legal compliance programs. Many large companies have even seen a need to create the position of Chief Compliance Officer. Whatever the case, the person put in charge must be at such a level within the company that he or she has the requisite authority to effectively oversee and enforce the compliance programs.
- 4.7. **Implement Sound Training Programs.** A compliance program is of no value unless the programs are communicated to employees and the employees are adequately trained in the company's policies and procedures. Directors need to take appropriate training as well. Companies also should take appropriate steps to document this training program for evidentiary purposes.
- 4.8. **Periodically Measure the Effectiveness Of The Compliance Program.** A board of directors (or appropriate board committee) should periodically receive from people in charge of the day-to-day operations of the compliance programs information about the effectiveness of such programs.
- 4.9. **Enforce The Compliance Program In A Consistent Manner.** If compliance policies and procedures are to be effective and believed, it is incumbent on a board to see that they are administered and enforced in a consistent manner. Unequal enforcement will undermine a compliance program.
- 4.10. **Stay Abreast Of Industry And Public Company Compliance Issues.** Directors need to be alert to legal compliance problems that surface in other companies (e.g., the recent problem of backdating stock options) so they can consider the risks of such problems within their own company.
- 4.11. **Maintain A Culture Of Compliance.** A board of directors must by its own actions send a clear message to everyone in the company that legal compliance and ethical conduct are highly valued. By taking ownership in the development, implementation and monitoring of the company's compliance programs, a board makes a powerful statement. The people in charge of the compliance program will be empowered by such action. Legal compliance and ethical conduct will be seen as a major priority by the rank and file employee.
- 4.12. **Properly Document The Board's Efforts.** If ever challenged in a lawsuit or regulatory investigation, it will be important that the minutes of board meetings and relevant board committee meetings adequately reflect the oversight steps taken by the board to satisfy itself that the company had in place an effective compliance program. Bottomline, directors should make their board minutes count so they are in the best evidentiary position to prove they had reasonable grounds for believing that they had fulfilled their oversight duties.

5. CONCLUSION.