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Psst! How Secret Should Executive Sessions Be?

By Sasha Issenberg

The New York Stock Exchange's new listing standards – approved by the Securities & Exchange commission in 2003 and implemented last year – state that "to empower non-management directors to serve as a more effective check on management, the non-management directors of each listed company must meet at regularly-scheduled executive sessions without management." The goal was clear – to establish a recurring occasion for outside directors to gab behind management's back about touchy issues such as honesty, performance, and compensation that are best avoided in mixed company. But the NYSE offered little guidance on the particulars.

More directors are participating in executive sessions. The 2005 Corporate Board Member/PricewaterhouseCoopers survey found that 22% do so at every board meeting, up from 15% two years ago. And 59% of those surveyed say they meet privately every quarter, up from 50% in 2002.

Most elements of the undefined executive-session-planning protocol will presumably be learned naturally through experience. Are refreshments served? Who sits at the head of the table? If it's a summer Friday, may attendees dress down? As with most matters, different companies will choose to do things differently. But one major question applies to everyone, and with urgency: Just how secret should these get-togethers be? And how can you, as a participant, respect confidentiality and still protect yourself from legal consequences later on?

According to Nell Minow, co-founder and editor of the Corporate Library, "Executive sessions should be extremely private. The purpose is to provide what we in Washington call a free and frank exchange of information. It should be our number one priority that people feel comfortable talking about their most serious concerns. You don't want to have them worried that that will be discoverable." Adds Charles Elson, director of the Center for Corporate Governance at the University of Delaware: "The idea is that it should be a free forum where directors can discuss matters freely. Afterward, if a concern has been raised, it's only fair that it be shared with management. But I don't think it's proper to betray the confidences of the room. That's just good common sense."

Directors agree. Galen D. Powers, an attorney and a director of HMS Holdings Corp. and MedCath Corp., says the boards of both companies, "candidly discuss management's performance. We then designate one or two directors to discuss the issues with the CEO." John C. Miles, who is a retired chairman and CEO of the dental-supply company Dentsply International and sits on the boards of Dentsply, Inamed Corp., and Respironics Inc. says, "There is an executive session during each board meeting, and if issues need to be fed back to the CEO, it's done by the lead director." And Walter M.

Higgins, chairman, president, and CEO of Sierra Pacific Resources says that his directors "spend hours in executive session mulling over my performance. They then communicate their conclusions to me, and if there's something they don't like, they have no bones at all telling me exactly what they think. Sometimes it's not much fun."

While they are willing to share certain conclusions, directors regard the privacy of the discussions leading there as essential. Those conversations can be fiery as well as candid. At times we've had direct confrontation between directors," says Joseph T. Casey, former vice chairman and CFO of Litton Industries and a director of Advanced BioPhotonics Inc. If discussions are kept confidential, "it's easier to discuss personalities or individual people," says Jack Curcio, former president and CEO of Mack Trucks Inc. and a member of the Minerals Technologies Inc. board.

Nevertheless, while directors and governance experts advocate strict confidentiality, lawyers see it differently. "My feeling is that you'd better have proof of what you did when it comes to litigation," says Roscoe C. Howard, a partner who specializes in white-collar defense at the Washington DC office of Sheppard Mullin Richter & Hampton LLP. "Especially when you have a company that's publicly traded, you want evidence of the executive session – what was said, what was decided." He advises directors to take notes on the details of the process that leads to a decision: "Just write it down."

Howard's views are grounded in experience as a federal prosecutor. "We have come into an age," he says, "where you need to be able to demonstrate before prosecutors, 'That's what we did. Look, we're doing our job. And here are our notes.' When I was a US attorney and somebody said, 'We've always done these things,' I'd say, 'How am I supposed to know that?'"

An executive session "isn't a litigation vehicle," Elson counters. "It's a tool for directors to exchange ideas in a free environment."

Those who recommend a closed-door strategy hew to a hard line: Attendees should not take notes. "And minutes," Minow advises, "don't need to include anything more detailed than 'The board met in executive session,' and perhaps a brief accounting of what subjects were discussed."

Maybe so. But talk to your lawyer first.