

WHITE PAPER

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Board Consents and Section 16 Reports Move Online

A Legal Review of Web-Based Technology Supporting Effective Corporate Governance for Boards of Directors

ABSTRACT:

Straddled by increasing responsibilities in support of corporate boards, general counsels and corporate secretaries are beginning to examine new ways to efficiently process time-sensitive board approvals and Section 16 reports by using technology and the Internet. This paper considers: What are the legal implications of electronic board consents and online approval of Section 16 reports?

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Introduction

Written board consents and Section 16 reports (i.e., Forms 3, 4, and 5) are necessary processes for boards of directors. These processes are also often extremely time-sensitive. For instance, board consents for stock option grants must be approved in writing by directors before a company's stock price substantially changes. Similarly, Section 16(a) of the Securities Exchange Act of 1934 requires that directors file a Form 4 within two business days of a change in beneficial ownership in a company's equity securities. From the perspective of a general counsel or corporate secretary, these processes can be somewhat tedious and repetitious. Moreover, these traditionally paper-based processes are sometimes constrained by the need for fast responses from remote or traveling directors who may be difficult to reach. This white paper provides a legal review of the Web-based technology that solves these issues by moving written board consents and Section 16 reports (especially Form 4 filings) online, improving the way boards communicate to promote better corporate governance.

Legal Perspective

The following section provides a review of Delaware state law establishing the legality and enforceability of electronic board consents and an analysis of the legal procedures that can be implemented to permit electronic review and approval of Forms 3, 4, and 5.

In order to implement electronic board consents, the following two-step process is recommended.

Electronic Board Consents: Recommended Process

STEP 1:

AMEND COMPANY BYLAWS

Companies need to amend their bylaws to permit for electronic approval of consents of the board of directors.

STEP 2:

FILE AN 8-K

Once the company bylaws are amended (per Step 1), companies must file a Form 8-K disclosing the bylaw amendment.

After following these steps, electronic approval of board consents can occur online. This electronic approval process also permits greater efficiency with respect to minute-book documentation. Traditionally, paper-based minute books for executed written board consents are used as evidence of corporate actions. By contrast, electronic board consents allow general counsels and corporate secretaries to track corporate actions in a searchable repository, easily accessible in either electronic or print format.

Similarly, with respect to Section 16 reports (i.e., Forms 3, 4, and 5), online approval by directors can result in greater efficiency, while minimizing inaccuracies. General counsels or corporate secretaries can request a director to validate information on a Form 4 before submission to the SEC, and then document such director's approval online. Once a director reviews and approves the

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Section 16 report online, such director need only click and approve the form, and then authorize the general counsel or corporate secretary to file the report with the SEC. Just as with the traditional paper-based process, when completing SEC forms on behalf of directors, general counsels or corporate secretaries must secure a power of attorney for this purpose in advance.

Electronic Board Consents – Delaware Law

Effective July 1, 2000, Section 141(f) of the Delaware General Corporation Law (the “DGCL”) was amended to provide that unless otherwise restricted by the certificate of incorporation or bylaws, any action required or permitted to be taken at a meeting of the board of directors may be taken without a meeting if all directors consent thereto in writing or *by electronic transmission*, and such writing or electronic transmission is filed with the minutes of the board. Furthermore, Section 232(c) of the DGCL defines an “electronic transmission” to mean “any form of communication, not directly involving the physical transmission of paper, that creates a record that may be retained, retrieved, and reviewed by a recipient thereof, and that may be directly reproduced in paper form by such a recipient through an automated process.”

As a result of this amendment to the DGCL, directors are permitted to approve corporate actions by electronic transmission (i.e., email). No longer are directors required to follow the cumbersome process of receiving a paper-based fax transmission of the

proposed board consent, reviewing and signing such consent, and then returning his or her executed consent by facsimile or overnight delivery.

Electronic Approval of Section 16 Reports

In order to avoid disclosing delinquent Form 4 reports in the annual proxy statement (under a separately captioned section), companies should consider implementing new compliance procedures to ensure that directors (and affected officers) comply with the accelerated two-business-day filing requirement imposed by the Sarbanes-Oxley Act of 2002. Pursuant to this compliance policy, directors (and affected officers) should sign a power of attorney granting the general counsel or corporate secretary authority to file Section 16 reports on behalf of the directors (and affected officers). With this power of attorney, general counsels and corporate secretaries will be empowered to perform any and all acts for, and on behalf of, the director or affected officer that may be necessary to complete and execute any Form 3, 4, or 5. In order to maximize efficiency in this process, companies can use Web-based technology to permit directors to review draft Form 4 filings online, confirm the information contained in the filing, and finally approve the filing for submission to the SEC by the general counsel or corporate secretary using the previously enacted power of attorney. In so doing, directors (and affected officers) can now ensure that all Form 4 filings will be made in a timely and accurate manner as required under the Sarbanes-Oxley Act of 2002.

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Real-World Practices

Organizations are using technology today to speed approvals of written board consents for items ranging from stock option grants to executive compensation packages for new hires – reducing the inefficiencies of re-doing grants that expire when director signatures cannot be returned in a timely manner.

Companies such as Silicon Valley-based BoardVantage, Inc., offer secure Internet portals for board activities, making it easy for directors to review and approve board consents as well as approve their Section 16 reports online using a simple point-and-click workflow. This Web-based technology, moreover, permits an accurate tally of responses for online documentation that avoids missed signatures.

As more boards move these kinds of processes online, directors gain easy, secure point-and-click access from anywhere, and corporate secretaries are able to reach remote directors and notify them for quick response through secure email, PDA, or voice alerts.

Conclusion

Pursuant to Delaware law, written board consents can be approved by electronic transmission. Through secure portals, companies have efficient Web-based technology to implement these electronic consents. Similarly, directors now can review and electronically approve Forms 3, 4, and 5 in a timely manner before they are filed with the SEC.

By moving written board consents and Form 4 reports online, organizations can more effectively address the time sensitivity involved in such necessary processes with the same legal effect as traditional paper-based processing.

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