Analysis of the Boards in U.S. Firms

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Contents

Ⅰ. Introduction
Ⅱ. Boards of Directors in U.S. Firms
Ⅲ. Conclusion

I. Introduction

The structure of boards in U.S. was led by autonomous endeavors rather than law enforcement. Principle of corporate governance in each firm takes the most important role to control the agency cost. However, after the Enron scandal, Securities and Exchange Commission(hereafter, SEC) has strengthened the regulations regarding the boards. In Korea, since the market pressure and autonomous efforts for better corporate governance are perceived to be low, controlling through law or guidelines is preferred.

This paper proposes desirable direction to the boards in Korean firms by analyzing regulations, principles, and trends regarding the duties, structures, and operations of the boards in U.S. We focus on recent corporate boards issues about bank regulations and guidelines for financial institutions in Korea. We provide several implications in this paper. First, the majority of boards are management experts in U.S. 66% of the boards are former or current executives. The ratio of professors or government officials on the boards is very low. In the case of Korean firms, the ratio

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of professors and officials is very high. Considering the case of U.S, we should understand that the harmony of independency and expertise is needed. The reason that the boards in U.S. can maintain high proportion of outside directors is that there is the wide managers' market. Former or current managers have expertise while meeting the standard of independency. Since there are not enough former or current managers who can be assigned as outside director in Korea, professors or officials to meet the independency standard tend to be assigned as outside director. This is likely to cause problems in a productive advisory function of the boards.

Second, the ratio of outside directors on the boards depends on the characteristics of the firms. When CEO holds substantial amount of shares, the ratio of outside directors becomes lower in U.S. firms. This means that, when there is a mechanism which inline CEO and shareholder interests, necessity of monitoring by the boards relatively gets lower.

Third, whether CEO actually exercises influence over selection of outside directors is a still debatable issue in U.S. Hermalin and Weisbach(1998) show that firms select new outside directors when their performance is bad. They argue that, when performance is bad, CEO loses bargaining power on selection of outside director. Therefore, in that situation, outside director who can monitor CEO is likely to be selected, not someone who are friendly to CEO. Cohen *et al.*,(2008) suggest that outside directors who are friendly to the management is preferred. When firms select an analyst as outside director, they choose an analyst who had given positive forecast for the performance of the firms.

Fourth, a term period of outside director is listed on company bylaws or left to the discretion of the company in U.S. There is no statement about total tenure or the ratio of newly selected outside director in bylaws or principles of corporate governance. It is autonomy of the firm. Regulations

proposed by Korea financial institutions guideline about term period of outside directors, and the ratio of newly selected outside directors are less likely to improve corporate governance. Considering situation in Korea market where the pool of candidates for outside director is small, these guidelines are likely to lower the quality of outside directors. Enforcing the outside director replacement will be likely to create a situation where firms have to choose candidates who are not qualified as an outside director.

Fifth, what the directors do on management is about between developing and rubber-stamping in U.S. Until 1980s, the role of the boards was just to agree on the proposal of executives on the management. Through 1990s, the boards performed an active debate on shaping the final business strategy.

Ⅱ. Boards of Directors in U.S. Firm

1. Obligation of the Boards

Corporate law of each state in U.S. abstractly describes the rights and obligation of the boards. Specific authorities, duties, and structures of the boards generally follow company bylaws, corporate governance principle and practice, committee charter, and etc. In U.S., corporate governance is made by market autonomy rather than by the law(See Table 1). Though it is more autonomous than government regulation, regulations of SEC and NYSE have been strengthened after the Enron scandal. Regulation reinforcement was focused on enhancing the monitoring role for accounting aspect and compensation level setting role. For the boards, in general, principle of corporate governance(1992) has the most detailed information.

Principle of corporate governance which was made in 1992 strongly influenced the companies setting their principles for governance structure.

Table 1: Principles for Governance Structure in U.S. and Korea

	U.S.	Korea bank law	Korea insurance law
Principles for governance structure	No reference in the law about the principles.	23th amendment Need deliberation and vote of the boards 1. Regarding business goal and assessment 2. Changing the bylaws 3. Funding and settlement including pay for the executives 4. Break ups, transfer of business, merger and other things that are significant change in the organization.	No reference in the law about the principles.

Note: Korea bank law specifically regulates what should be deliberated by the boards.

2. Structure of the Boards

A. Qualification and Selection of Directors

General procedure for selecting director can be found in company law, SEC and NYSE regulation, but the most specific procedure is written in company bylaws. General procedure is, "Recommendation of the boards, and then election at the general meeting". Qualification for outside director also has its general content stated in SEC and NYSE regulation, but the specific clause can be found in bylaws. SEC Rule states reasons for disqualification to be outside director considering employee relationship, family relationship, and business relationship. If one is a worker at the company or family to a worker at the company, one is not qualified. If one is in close business relationship with the company, one is not qualified. If

one is a worker at an independent auditing company or related to, one is not qualified(See Table 2).

Table 2: Qualifications and Selections of Outside Directors in U.S. and Korea

	U.S.	Korea bank law	Korea insurance law
Assigning outside director	Organize recommendation committee for outside director consists of only outside directors	Organize recommendation committee for outside director that has outsider directors more than ½ (2010.05.17. amendment)	Same as Korea bank law
	Outside director is elected from whoever recommended by the recommendation committee: NYSE regulation	Same as U.S. (2010.05.17. amendment)	Same as U.S.
Reasons for disqualification	SEC regulation	Regulated in 22th amendment	Regulated in 15th amendment
Remarks regarding disqualification reasons		Controlling shareholder and its connected parties are not qualified for outside directors. (2010.05.17. amendment)	Controlling shareholders are not qualified for outside directors.

Note: In guidelines of outside directors for Korea insurance company, connected parties to controlling shareholder are also disqualified as outside directors

In U.S., the outside director (or independent director) means someone who is independent from the management's interest. However, in case of Korean companies, it means someone who is independent from the management's and controlling shareholder's interest. In U.S., Controlling shareholder is thought to have enough qualification and incentives to monitor the management. In the case of Korean companies, there is an

opinion that, since controlling shareholder is exercising too much power through pyramid structure, mutual investing, and circular investing, the boards should actively monitor controlling shareholder. Specific cases of advanced firms in U.S. are in Table 3.

Table 3: Cases for Advanced Firms in U.S.

Firms	Characteristics
Prudential	1. Financial holding company 2.Dispersed ownership
Berkshire Hathaway	1. Conglomerate 2. Managed by controlling shareholder
GE	1. Conglomerate 2. Dispersed ownership

Assigning procedure and qualification (based on bylaws) for directors in U.S. firms is as following.

Case Ⅰ: Assigning procedure and qualification of Prudential

Corporate governance and business ethics committee finds and recommends candidates, and then the director is elected at the general meeting. It gains assistance of an independent search company while finding candidates. A search company provides constant feedback information for the candidates. Corporate Governance and Business Ethics Committee considers variety of things like independency, financial knowledge, expertise, and experience in assigning director. As a financial complex group, they offer life insurance, pension plans, retirement plan, funds, real estate, and other various products. Therefore, they consider industry experience that is related to insurance, finance, real estate, and corporate tasks. Knowledge about risk management, finance, investment, corporate governance, business, and marketing is also needed. In assessing existing directors, past performance as director and dedication to each committee is also considered. Generally, most directors are re-elected

based on past performance.

Case II: Assigning procedure and qualification of Berkshire Hathaway

Governance, compensation, and nominating committee finds and recommends candidates, and then the director is elected at the general meeting. The diversity of director is not a main concern. They care more about integrity/business experience/how interested one is to the firm.

There is no regulation about tenure of the outside director exist in U.S. Tenure of outside directors is either mentioned in the bylaw of the company or left to the discretion of the company. In most cases, upper limit for tenure of outside director is stated in the bylaws. There is no clear statement about total tenure or the ratio of newly selected outside director in bylaws or principles of corporate governance. It is autonomy of the firm(See Table 4).

Table 4: Tenure and Ratio of the Outside Director in U.S. and Korea

	U.S.	Korea bank	Korea insurance
Term limitation on outside directors	Differ from 1 to 3 years: Bylaws Total tenure: Autonomy	2 years: Guideline Total tenure up to 5 years: Guideline	3 years: Guideline Total tenure up to 5 years: Guideline
Ratio of new outside directors	Autonomy	Replace 1/5 every year: Guideline	Replace 1/5 every year: Guideline

Regulations proposed by Korea financial institutions guideline about term period of outside director, and the ratio of newly selected outside directors aim to replace current outside directors. However, those have little to do with long-term enhancement of corporate governance. As you can see in Table 5, outside directors in U.S. serves a long time. This means that

gaining knowledge about the firm takes time. When we consider the Korea market where the pool of candidates for outside director is small, guidelines above are likely to lower the quality of outside directors. Enforcing the outside director replacement will likely to create a situation where firms have to choose candidates who are not qualified as an outside director.

Table 5: Cases for Tenure of the Outside Directors

	Prudential	Berkshire Hathaway
Average term of outside directors	7 years(2009)	7.4 years(2009)

Source: Proxy Statement

There is no regulation about CEO serves as chairman of the boards (See Table 6.), but it is a trend not to do so. Institutional investors and academic scholars criticize it because, when CEO serves as chairman of the boards, independency of the boards is damaged and the boards are likely to work as trench for the management. For example, Wal-Mart assigns former CEO as chairman of the boards. These things often happen, and this is kind of a succession planning to efficiently transfer the control rights.

Table 6: Leadership Structure of the Boards in U.S. and Korea

	U.S.	Korea bank	Korea insurance
Serving as both CEO and chairman	Autonomy	When chairman is an outside director, public announcement is needed: Guideline When CEO serves as chairman, public announcement and senior outside director is needed: Guideline	Same as Korea bank

Note: In case of U.S., autonomy means that, for some firms, they have it on principle of corporate governance, and for some firms, they do not.

U.S. cases for leadership structure of the boards (CEO serves as chairman, assigning senior outside director) are shown in Table 7.

Table 7: Cases for Leadership Structure of the Boards

	Prudential	Berkshire Hathaway	GE
Chairman	CEO serves as chairman	CEO serves as chairman	CEO serves as chairman
Senior outside director	Exist	Do not exist	Do not exist

Source: Proxy Statement

Case Ⅰ: Leadership structure of the boards in Prudential

Leadership structure of the boards consists of chairman and Lead Independent Directors. According to the Principle of Corporate Governance, when CEO serves as chairman, outside directors elect senior outside director through vote. Rights of senior outside director are as following;

1) When chairman is absent, lead the board meeting
2) Rights to call outside director meeting
3) Bridge between chairman and outside directors
4) Overall judgment on information submitted to the boards and rights to agree on meeting agenda of the boards.

Case Ⅱ: Leadership structure of the boards in Berkshire Hathaway

Warren Buffett is the CEO and, at the same time, chairman of the boards. He thinks that controlling shareholder should be in charge of the position. The board agrees on his opinion, and has not assigned a senior outside director.

U.S. cases for organization of the boards are shown in Table 8.

Case Ⅰ: Organization of the boards in Prudential

9 directors of all outside directors are former/current manager. There are 1 former government official (Constance J. Horner), and 1 politician (William H. Gray III)(See Table 8).

Table 8: Profile of the Boards in Prudential

	Year	Career	Committee
Thomas Baltimore(46)	2008	Current president at RLJ Development(Real estate Investment Firm)	Finance, Investment
Gordon M. Bethune(68)	2005	Current Managing Director of g-b1 Partners (Travel Advisory Firm), Former CEO at Continental Airline	Compensation, Governance
Gaston Caperton(70)	2004	Current President of the College Board (Non-Profit Membership Association of 5,600 Schools, Colleges, and Universities) Former CEO at Privately Owned Insurance Brokerage Firm	Finance, Investment
Gilbert F. Casellas(57)	2001	Current Vice President at Corporate Responsibility of Dell, Inc Current director at Prudential Insurance(1998)	Audit
James G. Cullen(67)	2001	Former COO at Bell Atlantic Corporation Current director at Prudential Insurance(1998)	Audit, Compensation, Executive
William H. Gray III (68)	2001	Former CEO at The College Fund Former Member of the U.S. House of Representative	Governance and Business ethics(chairman), Executive
Mark B. Grier(57, inside director)	2008	Current Vice Chairman of Prudential (Executive of Prudential Financial)	
Jon F. Hanson(73)	2001	Current Chairman at The Hampshire Companies(Real Estate Investment Fund Management Firm) Current director at Prudential Insurance(2001)	Executive(chairman), Finance(chairman), Investment(chairman)

Constance J. Homer(68, Female)	2001	Former The Brookings Institution, Deputy Secretary, U.S. Department of Health and Human Service	Compensation, Governance and Business ethics
Karl J. Krapek(61)	2004	Former COO at United Technologies Corporation	Finance, Investment
Christine A. Poon(57, Female)	2006	Current Dean of Fisher College of Business, Ohio State University Former Executive at Johnson&Johnson, Bristol-Myers Squibb	Finance, Investment
John R. Strangfeld(56, inside director)	2008	Current Chairman and CEO	
James A. Unruh(68)	2001	Founding member, Alerion Capital Group(Private Equity Investment Group) Current director at Prudential Insurance(1996)	Audit

Source: Proxy Statement

Case Ⅱ: Organization of the boards in Berkshire Hathaway

Whole outside director consists of former/current managers and financial experts(See Table 9).

Table 9: Profile of the boards in Berkshire Hathaway

	Year	Career	Committee
Warren E. Buffett(79) Inside director	1965	Current CEO, Chairman of the boards, and Controlling shareholder	
Howard E. Buffett(55) Inside director	1993	Family(Son)	
Stephen B. Burke(51)	2009	Current COO at Comcast	
Susan L. Decker(47, Female)	2007	Former President at Yahoo	Governance
William H. Gates III(54)	2005	Current Co-chairman at Bill&Melinda Gates Foundation Former CEO at Microsoft	
David S. Gottesman(83)	2003	Current Principle at First Manhattan Co.,	Governance

		Investment Advisory Firm	
Charlotte Guyman(53, female)	2003	Current chairman of the board at UW Medicine Former General Manager at Microsoft	Audit
Donald R. Keough(83)	2003	Current chairman at Allen&Company, IB	Audit
Charles T. Munger(86) Inside director	1978	Former chairman of the boards and CEO at Wesco Financial Corporation(80% Owned by Corporation)	Vice chairman of the board
Thomas S. Murphy(84)	2003	Former chairman of the boards and CEO at Capital Cities/ABC	Audit
Ronald L. Olson(68)	1997	Current Partner at Munger,Tolles&Olson LLP	
Walter Scott, JR(78)	1988	Current chairman of the boards at Level 3 Communication	Governance

Source: Proxy Statement

U.S. firms tend to consider former/current managers to have capability as an outside director. Capability of outside director means both the monitoring over the management's operation and advising over strategic direction. Expertise in monitoring and advising means experience as manager. Lee (2008) shows that 47% of outside directors in U.S larger firms are retired/ongoing CEO. As in Table 10, 66% of directors in U.S. are former/current managers. The ratio of professors or government officials is very low (Linck *et al*, 2009). Considering the case of U.S., we should extend our recognition and understand that the harmony of independency and expertise is needed on organizing the boards. The reason that the boards in U.S. can maintain high level of independency (high level of outside director) is that they have wide pool of former/current managers who have expertise while meeting the standard of independency. Since Korea market has narrow pool of former/current managers who can be assigned as outside director, Korean companies assign professors/officials to meet the independency standard. This is likely to cause problems in a

productive advisory aspect.

Table 10: Composition of the Directors in U.S. and in Korea

Profession	U.S.	Korea conglomerate (Mutual investing restriction)	Korea listed company
Former/current manager	66%	20.6%	30.8%
Financial expert	12.8%	9.0%	N/A
Professor	4.9%	29.3%	24.3%
Government official	N/A	20.1%	8.1%
Legal profession	9.7%	13.2%	11.6%
etc	6.6%	7.7%	25.2%

Note: 1000 listed companies in U.S. were analyzed(Linck *et al.*, 2009).
Note: The professions of outside director in 247 listed companies, among 79 Korean conglomerates under restriction of mutual investing(April, 2008).
Note: In the case of U.S., officials are included in “etc” section.
Note: In the case of Korea conglomerate, 8.8% of outside director is executives from affiliates and it is included in former/current manager section.
Note: In the case of Korea listed companies, financial experts are included in “etc” section.

B. Size of the Boards and Ratio of Outside Director

There is no regulation about the total size of the boards. However, firms sometimes have a certain range stated on their bylaws. For instance, Bylaw of Prudential states that the board size should be between 10~24 people. Cases of US firms regarding the total size of the boards are in Table 11.

Table 11: The Size of the Boards in U.S.

	US Major firms	Prudential	Berkshire Hathaway
Bylaws regarding the board size	Case by Case	10~24	Not mentioned
Actual size	10.4(2004)	13(2009)	12(2009)

Source: Linck *et al.*,(2008), Proxy Statement

Linck *et al.*,(2008) show that the size of the boards in US firms was decreasing throughout 1990s, but is increasing after the Enron scandal and SOX (2002). In 1990s, there was arguments that when the board size is big, efficiency in decision making decreases. After the Enron scandal, the size started to increase, because of increased tasks and responsibilities of the boards. Average board size in 2004 is about 10.4 people in US firms. Linck *et al* (2008) also show that the more shares CEO has, the smaller the boards get. This implies that when controlling shareholder directly manages the firm, role of the boards gets smaller and authority of CEO and executives gets bigger.

SEC regulation says that majority of the boards should be outside director(See Table 12).

Table 12: Regulations for the Size of Boards in U.S. and Korea

	U.S.	Korea bank law	Korea insurance law
Constitution	(Following SEC standards) Majority is outside director	More than 3 outside director, majority (2010.05.17 amendment)	More than 3 outside director, over half.

Linck *et al.*, (2008) show that the portion of outside directors is about 75% in 2004. For Korean firms (with mutual investing restriction, April 2008), the ratio of outside directors is about 44%(See Table 13). The

ratio of outside directors is also increasing after the Enron scandal and SOX. At the time of Enron scandal, the boards were blamed for not monitoring the management effectively. This became a basis of an argument that says to increase the ratio of outside director.

Table 13: The Number and Ratio of Outside Directors on Boards in U.S.

outside director	Average US firms	Prudential	Berkshire Hathaway	GE
Number	8.0	11	8	13
Ratio	75%	85%	67%	81%

Source: Linck *et al* (2008), Proxy Statement

However, Linck *et al.*,(2008) argue that the ratio of outside directors is different across different ownership structure. When CEO holds substantial amount of shares, the ratio of outside directors is shown to be low. This means that, when there is a mechanism which inline CEO and shareholder interests, necessity of monitoring by the boards relatively gets lower. As in Table 13, Berkshire Hathaway which is managed by controlling shareholder has 67% ratio of outside directors.

3. Operation of the boards

(Generally) Meeting procedure and setting procedure for agenda is stated in the bylaw. Meetings are classified to Regular meeting and Special meeting, and Regular meeting is held at once a quarter. Generally, set the agenda together when CEO and chairman are different person, and CEO consults with senior outside director or major director when CEO and chairman are the same. Number of meetings varies across companies, but meeting is held 6~7 times a year on average and, at least 5 times a

year(See Table 14). After the Enron scandal, number of meetings in the board and each committee is increasing. It is an increase from the aspect of accounting-monitoring (audit committee) or compensation (compensation committee), not from the aspect of business strategy(Linck *et al.*, 2009).

Table 14: Number of Board and Committee Meeting in U.S.

	Year	Board meeting	Audit committee meeting	Compensation committee meeting	Recommendation committee meeting
Small firms	1998	5.8	1.7	2.1	0.5
	2001	5.8	2.6	2.2	1.0
	2004	6.9	5.1	2.3	1.6
Middle firms	1998	5.7	2.3	2.1	0.2
	2001	6.4	4.0	2.4	0.9
	2004	7.3	6.2	3.3	1.9
Major firms	1998	6.5	3.2	3.5	1.2
	2001	6.4	4.5	4.0	1.3
	2004	6.4	8.2	4.7	4.2

Source: Linck *et al.*,(2009)

Board meetings have two kinds. One that finishes on the day and one that takes 2-3 days. Meetings of each committee have two kinds. One that is held on the day before the board meeting or at morning of the board meeting day, and one that is held separately. General agendas are as shown in Table 15. Get an agreement on and debate about annual plan or business strategy at the top of the year meeting, and get an assessment and modification (if needed) after the first half of the year.

Table 15: General Agendas on Boards in U.S.

Items	Content	Form
Check for a quorum		
Set the board agenda	1. Modifiable on the spot of the board meeting	Agreement
Process agreement clauses	1. Process routine clauses which do not need debate: Agreement on stenographic records, announcement for shareholder meeting, etc 2. Reference data must be sent priori 3. Directors can call for debate.	Agreement
The board reporting	1. Each committee reports results of committee meeting: Major issues debated, Decisions made, Recommendations for the board decision, etc	Agreement
Current operation reporting	1. CEO: Result of recent events and prospects for near future.	Debate
Briefing or Proposal	1. Executives deliver briefing or proposal about major point in management Ex) Capital investment Ex) Proposals about M&A could take up all the meeting schedule	Agreement
Executive session	1. Outside directors alone have debate after the board meeting 2. Chairman or senior outside director can give a message to CEO or ask CEO to participate in the debate.	Debate

The level of intervention that the directors do on business strategy is about between developing and rubber-stamping. Until 1980s, the role of the boards was just to agree on the proposal of the management. Through 1990s, the boards performed a certain role through active debate on shaping the final business strategy. The proposal of the management sometime got declined by the boards. Nonetheless, the boards hardly proposed or led the discussion on strategy planning.

In preparing the board meeting, (1)efficient task performance of the Meeting manager (person in charge of the meeting) and (2)smooth operation of the committees under the boards in crucial. Meeting manager

should provide enough information about the board agenda. Data of the board agenda should be distributed prior to the meeting so that the directors have enough time to consider. Most of the board agenda (or item) is discussed at each committee meeting before the board meeting. Experts from each committee gather to enhance the efficiency of the debate and decision making. Directors from each committee should have discussion with major executives and (if necessary) outside experts. When executives and each committee propose an idea for the board decision about major issues of business, it is important to submit pros and cons of the proposal and the data that forms basis of the proposal.

The regulation for organizing a committee under the boards and giving rights to each committee is stated in the company bylaw, Principle of Corporate Governance, and Charter of the boards. Each committee can be classified into both advising committee and monitoring committee. Advising committee (advising the business direction) includes finance committee, investment committee, strategy committee, etc. Monitoring (monitoring execution function) includes corporate governance committee, compensation committee, audit committee, etc. When assigning people to each committee, consider committees function to enhance efficiency. To the committees which propose business directions and give advice on management, person who is experienced in management field is preferred. Professors, officials and non-management experts are tend to be placed in Monitoring committee, especially in corporate governance committee. In case of US, new committees are created to reflect the trend or main issue of business management at the time. After financial crisis, there were opinions that a risk-management committee should be organized under the boards. In 2000s, social responsibility of corporation was addressed in and around academic field, and creating corporate social responsibility committee became a trend. Regarding the main issues, corporations think

that assuring balance and harmony by creating an independent committee under the boards in addition to the executive who is in charge of the issue is important. U.S. cases for operation of the boards are as following

Case Ⅰ: Operation of the boards in Prudential

The boards consist of audit, compensation, governance and business ethics, executive, finance, and investment committee.

1) Audit committee: corporate accounting, finance reporting and monitoring of information disclosure, audit of the company's financial statement, and overall management of the risks.
  a) Assign independent auditor and assess their performance.
  b) Review result from both independent auditor and inside auditor.
  c) Members of Audit committee satisfies SEC Rule 10A-3 and NYSE Manual of listed companies Section 303A.

2) Governance and business ethics committee: monitor overall corporate governance structure.
  a) Recommendation of the director candidates, recommendation about director compensation, etc

3) Compensation committee: monitor developing and executing of compensation and benefits mechanism.

4) Finance committee: monitor over capital structure, agreement and action.
  a) Debt structure, major capital expenditures, etc

5) Investment committee

a) Actions and monitoring about take over and selling off the investment assets
b) Review on invest performance of the pension fund
c) Review on risk and performance of investment on real assets organization of the committee under the boards is as shown in Table 16. Major feature is that government official (Constance J. Horner), and politician (William H. Gray III) who are non-experts in business are assigned at corporate governance committee, and compensation committee.

Table 16: Organization of the Committee under the Boards-Prudential

	Audit	Compensation	Governance	Executive	Finance	Investment
Thomas J. Baltimore(46)			○		○	○
Gordon M. Bethune(68)	CHAIR			○		
Gaston Caperton(70)					○	○
Gilbert F. Casellas(57)	○					
James G. Cullen(67)	○	CHAIR		○		
William H. Gray III(68)			CHAIR	○		
Mark B. Grier(57, inside director)						
Jon F. Hanson(73)				CHAIR	CHAIR	CHAIR
Constance J. Homer(68, Female)		○	○			
Karl J. Krapek(61)					○	○
Christine A. Poon(57, Female)					○	○
John R. Strangfeld(56, inside director)						
James A. Unruh(68)	○					
Number of meetings held in 2009	14	6	7	0	10	8

Source: Proxy Statement

Case Ⅱ: Operation of the boards in Berkshire Hathaway

The boards consist of audit and governance, compensation, and nominating committee. Full authority of the management is given to the executives, and the boards' role is limited to ex-post monitoring. No committee related to advising business strategy exists. Organization of the committee under the boards is as shown in Table 17.

Table 17: Organization of the Committee under the Boards-Berkshire Hathaway

	Audit	Governance, Compensation, and Nominating
Warren E. Buffett(79) Inside director	As an insider director, attached to no committee	
Howard E. Buffett(55) Inside director	As an insider director, attached to no committee	
Stephen B. Burke(51)		
Susan L. Decker(47, Female)		○
William H. Gates III(54)		
David S. Gottesman(83)		○
Charlotte Guyman(53, female)	○	
Donald R. Keough(83)	○	
Charles T. Munger(86) Inside director	As an insider director, attached to no committee	
Thomas S. Murphy(84)	○	
Ronald L. Olson(68)		
Walter Scott, JR(78)		○
Number of meeting held in 2009	7	2

Source: Proxy Statement

4. Election and Dismissal of Executive Officer

Election method of executive officers is specified in the company regulation. However, except the election and dismissal of the CEO, there is no evidence of general pattern. In the case of CEO, election and dismissal is made by the boards of directors. Election and dismissal of executive officers under the CEO is made either by the boards, by the CEO, or by both. By looking at company regulation only, it is hard to determine who has the actual authority over election and dismissal of executive officers under the CEO. Actual case regarding election and dismissal of executive officer is shown in Table 18.

Table 18: Cases for Election and Dismissal of Executive Officer

	Election and dismissal of executive officer
Morgan Stanley	Boards of directors has the rights to elect and dismiss the executive officer
Prudential	Higher than senior vice president: boards of directors has the rights Lower than senior vice president: nominated by proper officer
GE	CEO has the rights to elect and dismiss the executive officer

Source: Bylaw

The most powerful monitoring mechanism of the boards over CEO is turn-over decision. Recently, the tenure of CEO tends to shorten from average of 8 years in 1990s to average of 6 years in 2000s(Kaplan and Minton, 2006).

5. Compensation of Executive Officer

Generally, according to the company regulation, Compensation

Committee under the boards of directors is responsible for compensation of executive officer. They develop the compensation system, set the level of compensation, and monitor the execution of compensation, with the help of Human Resource department and outside consultant. Compensation Committee submits suggestion about overall executive compensation as an agenda for the meeting of the boards. By the regulation of SEC and NYSE, Compensation Committee must be composed of outside directors only. However, there are cases where CEOs intervene in a discussion about compensation for executive officers other than the CEO. Actual case regarding the setting of compensation plan for executive officers is shown in Table 19.

Table 19: Cases for Compensation Plan for Executive Officers

	Setting compensation level for executive officer.
Prudential	Compensation Committee (consists of outside director only) will review the CEO compensation compared to the market level. Compensation Committee will approve the appropriate level of CEO compensation and report it to the boards for further approval. Compensation Committee intervenes actively in deciding compensation level for major executives.
GE	Compensation Committee(consists of outside director only) decides the level of CEO compensation Compensation Committee and CEO together assess the performance and decide the level of compensation for the executives: It is based on the Initial Recommendation made by the CEO.

Source: Bylaw

6. Audit Committee and Full Time Audit

SEC (Security Exchange Act Rule 10A-3) regulates installation of Audit Committee within the boards and, according to the NYSE rule (NYSE manual Section 303A), Audit committee should consist of at least three

members and all members should be outside directors. SEC regulates that the Committee must have at least one financial expert. This is the strengthened result after the Enron scandal(See Table 20).

Table 20: Regulations for Audit Committee in U.S and Korea

	U.S.	Korea bank law	Korea insurance law
Setting the audit committee	Audit committee is needed according to the SEC regulation	Banks should have audit committee following the 415 amendment of commercial law.	Insurance company should have audit committee following the 415-2 amendment of commercial law(or should assign senior audit)
Organizing the audit committee	According to the NYSE Rule, audit committee should be at least 3 and must consist only of outside director. Following the SEC regulation, audit committee should have at least 1 financial experts	2/3 of total members should be outside directors. Audit committee must have at least 1 accounting or financial expert designated by a presidential decree.	2/3 of total members should be outside directors. Audit committee must have at least 1 accounting or financial expert designated by a Presidential decree.

"Principle of corporate governance" from American Law Institute suggests installing audit committee which regularly monitors the process of making accounting data, internal control, and independency of outside auditor. In case of U.S., there is no concept of full-time auditor. Korea commercial law says that, in case of listed company with total assets between 100 billion and 2 trillion, the company should assign full-time auditor (who works in the firm full-time and do the audit) in addition to outside director, and in case of listed company with total assets over 2 trillion, the company should create audit committee. Full-time auditor is assigned at a general meeting, but voting rights of controlling shareholder is limited on electing full-time audit(See Table 21).

Table 21: Regulations for Full-Time Audit in U.S and Korea

	U.S.	Korea commercial law	Korea bank law	Korea insurance law
Full-time audit	No reference	Listed company with total assets between 100 billion and 2 trillion should assign full-time auditor (who works in the firm full-time and do the audit) in addition to outside director, and in case total assets are over 2 trillion, the company should create Audit committee.	No reference	Same as Korea commercial law

7. Risk Management Organization

In case of U.S. firms, audit committee usually performs risk management task. There were opinions about creating a new risk-management committee under the board after the financial crisis. The Basel Committee on Banking Supervision (BCBS) argued that the major banks or banks which have global business area should have Risk management committee or auditing organization corresponds to the committee. As in Table 22, risk management committee is not a requirement in the Korea market, but most of the banks, financial holding companies, insurance, and security companies operate risk management committee.

Table 22: Regulations for Risk Management Committee in U.S and Korea

	U.S.	Korea banks	Korea insurance and securities
Risk management committee	No reference	Korea banks and financial holding companies can have risk management committee if needed.	No reference

U.S. Cases of installing independent risk management committee is as shown in Table 23. As in Table 23, cases where major banks newly adopt independent risk management committee appear. OECD suggested that all financial institutions have CRO (Chief Risk Officer) and let it independent from CEO. Regular reporting to the board is stressed.

Table 23: Cases for Risk Management Committee

	Prudential	Berkshire Hathaway	BOA	HSBC
Risk management committee	None	None	Installed	Installed

Ⅲ. Conclusions

This paper studies regulations, principles, and trends of the boards in U.S. The majority of the boards are retired or ongoing executives. Secondly, the ratio of outside directors varies across different ownership structure. When CEO holds substantial amount of shares (or when controlling shareholder is the CEO), the ratio of outside directors is shown to be low. This means that monitoring by the boards relatively matters less when there is a mechanism which inline CEO and shareholder interests. Thirdly, regulations proposed by Korea financial institutions guideline about the tenure of outside director, and the proportion of newly selected outside directors have little to do with long term enhancement of corporate governance. Finally, guidelines above are likely to lower the quality of outside directors in Korea. Enforcing the outside director replacement will be likely to create a situation where firms have to choose a low qualified candidate as an outside director.

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Abstract

Analysis of the Boards in U.S. Firms

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This paper studies regulations, principles, and trends regarding the duties, structures, and operations of the boards in U.S. to provide implications to Korean firms. Firstly, the boards should have majority of its members as management experts to be the last decision maker. In case of U.S., 66% are retired or ongoing executives. Secondly, the ratio of outside directors is different across different ownership structure in U.S. When CEO holds substantial amount of shares, the proportion of outside directors is shown to be low. Thirdly, regulations proposed by Korea financial institutions guideline about term period of outside director, and the ratio of newly selected outside directors have nothing to do with good corporate governance. The tenure of outside directors in U.S. is not regulated, but determined in the market.

Key words: Corporate Governance, Boards, Regulation, Bank, Financial Institution
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