

2007 SPECIAL SUPPLEMENT



# WHAT DIRECTORS THINK 2007

The *Corporate Board Member*/  
PricewaterhouseCoopers Survey

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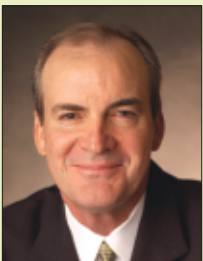
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Over the course of a year, we get many opportunities to speak with directors, both formally and informally, about the issues confronting their boards. Our annual What Directors Think study allows us to take this one step further, to scrutinize these general conversations and measure what is really on directors' minds. For instance, this year our interviews led us to believe that boards are embracing the idea of director and board evaluations as a tool for enhancing board functions and directors' abilities to fulfill their fiduciary duties. Our study results lend credence to this belief: twice as many boards now conduct regular evaluations compared to the numbers we saw in 2002, the first year of the study. This year we also sensed that boards were confronting a new round of challenges, especially those related to executive compensation and increasing shareholder scrutiny. And while all these items are demanding more board attention, directors told us serving on the audit committee is still their most challenging job.

The 2007 What Directors Think study, conducted by *Corporate Board Member* and PricewaterhouseCoopers LLP, is the sixth annual survey of directors of publicly traded companies. This year, we collected responses from more than 1,000 corporate directors who answered questions about how they meet the many demands of their role and stay afloat in a corporate environment where every move is scrutinized and risk is an ongoing concern. We would like to thank you, the directors, for taking the time to provide us with your invaluable insight on topics that often aren't discussed outside the boardroom walls.

We hope you find this special supplement, a companion to the November/December 2007 edition of *Corporate Board Member* magazine, useful in benchmarking how your peers are handling their challenges—and in many cases, rising above them—to promote a stable corporate environment with increased value for shareholders.



A handwritten signature in black ink, appearing to read 'TK Kerstetter'.

**TK Kerstetter**  
President and CEO  
*Corporate Board Member*



A handwritten signature in black ink, appearing to read 'Catherine Bromilow'.

**Catherine L. Bromilow**  
Partner and U.S. Leader for  
Corporate Governance  
PricewaterhouseCoopers LLP

# Executive Summary

In this year's comprehensive What Directors Think study, *Corporate Board Member* and PricewaterhouseCoopers LLP offer detailed results of their annual survey of U.S. corporate directors. The study encompasses what directors perceive to be their toughest challenges as they strive to meet standards of best practices and to increase value for shareholders in the year ahead. Chief among the areas investigated were board members' increasing levels of responsibility and accountability, directors' perception of boardroom risk, and the changing nature of the director/shareholder relationship.

## Board Performance and Responsibilities

Board members are honing their skills to become more effective in their jobs, the scope of which has grown substantially in recent years. As a result, the number of corporate boards participating in board evaluations and ongoing education has increased more than twofold since 2002, according to our 2007 study. Moreover, 79% of directors believe the board evaluation is the most important tool for ensuring director effectiveness.

Among the most time-consuming and demanding responsibilities are those related to the audit committee. More than half of those who identified themselves as audit committee members spend between three and four hours in each committee meeting, and 16% spend nearly six hours per meeting. There is no doubt the onus of shareholder and public scrutiny has led to an upswing in emphasis on the work of the audit committee. Indeed, the scope of the audit committee's responsibility widened greatly after the passage of Sarbanes-Oxley and the promulgation of guidelines by the NYSE and NASDAQ.

"Audit committees continue to work diligently to address the past expansion of their core responsibilities. And they are spending the needed time not only overseeing the integrity of the financial statements and the audit processes, but also monitoring compliance and risk management functions that are so important to the ongoing success of their companies," says Catherine L. Bromilow, a partner with PricewaterhouseCoopers and U.S. leader of its Corporate Governance Group.

## Director Risk and Liability

This year, fewer board members report feeling the pressure of growing risk. In the 2007 What Directors Think study, only 35% of directors say their risk as a director increased over the past year, compared with 44% who said they felt their risk increased in 2006, and 73% in 2005. In fact, this year there is an upswing in the number of directors who say their risk stayed the same. This leads to the conclusion that directors' risk perception jumped in the post-Sarbanes-Oxley era and continues to remain relatively

high today. This year, 62% of directors (compared with 52% in 2006 and 26% in 2005) say their risk is just as high in the last 12 months as it was the previous year.

"Efforts that focused on internal control and financial reporting systems related to Sarbanes-Oxley have taken hold, providing directors with greater assurance over one key element of risk. However, having 35% reporting a perceived increase in risk is still significant and shows that directors take seriously their ongoing oversight responsibilities," says Bromilow.

Although 98% of directors we surveyed are satisfied with their understanding of their D&O coverage, our study revealed a notable gap in the knowledge directors have about the specifics of their D&O policies. Nearly one-third of participating directors do not know what their Side A coverage is and what it means to them as part of their D&O liability coverage.

"Some boards will unfortunately find out about Side A coverage the hard way, when they are named in a lawsuit and suddenly realize their policy was used up defending the company, and there are no insurance funds left to defend the directors. Smart board members should take time to investigate their D&O policy," says TK Kerstetter, president and CEO of *Corporate Board Member*.

## Shareholder Access to the Board

Shareholder access to the boardroom is shaping up to be a huge issue. In fact, in our survey, directors rate shareholders (as a whole) as their most important constituency, above institutional investors, customers, creditors, and management.

To gauge directors' readiness to interact directly with shareholders, we asked our survey participants to tell us if they would be prepared to speak up publicly in the event a shareholder at the company's annual meeting asked their opinion of the company vision. An overwhelming 96% said yes.

## Additional Highlights

*Directors perceive majority voting rules will cause very little change on company boards.* Only 10% of directors say they believe majority voting will bring significant changes to boards in the short term. Over the long term, less than 30% of directors expect such voting policies to effect significant change on boards.

*Directors rate regular executive sessions without the CEO as the leading hallmark of good governance.* Our survey asked directors to rate several items according to how important they are as a component of good governance. Directors rated having regular executive sessions without the CEO first, followed closely by

having a board composed mostly of independent outside directors. Directors also placed significant weight on conducting regular CEO reviews and having a formal management succession plan.

***Directors favor serious action in response to board-level press leaks.*** A strong majority of directors (81%) say asking for resignation is the most appropriate board action against a director who has leaked information to the press. However, 12% of directors say the board should stop short of asking the guilty director to resign and instead should give him or her a stiff warning.

***Directors are tuning in to different cues that it is time to step up their involvement in the company.*** Directors continue to rate an earnings restatement as the most important signal that they should take a more active role in the company.

“Earnings restatements are the ultimate red flag for a director. While one would hope that the increased involvement by directors in the post-Sarbanes era would decrease the likelihood of such restatements, the complexity of accounting and financial reporting and the existence of unanticipated events, such as errors related to options backdating, mean boards will still need to address restatements in the future,” says Bromilow.

Moving into second place as the most important prompt for more involvement (up from fourth in the 2006 study) is research data showing a poor customer satisfaction track record. More boards (51%, compared with 43% in 2006) now receive data on customer satisfaction.

***Succession planning is important, and more boards should be taking the lead on getting this job done.*** Although the majority (65%) of directors in our study are satisfied with their companies’ management succession plans, 35% are unhappy with the way their board has tackled this particular issue. About half (52%) of those who are dissatisfied say their displeasure stems from the fact that management succession is not a regular item on the agenda.

“This is the sixth year boards have identified succession planning as one of their least effective processes. Unfortunately, replacing a CEO is not always something you can predict, so not having a plan in place is poor governance on the board’s part,” says Kerstetter.

***CEO compensation practices are ripe for change, but who will bring it about?*** Two-thirds of participating directors say U.S. companies are having trouble controlling the size of CEO pay, a finding consistent with our 2006 study.

So what will bring about change? The vast majority of directors (92%) say they believe shareholders should not have a vote in

approving CEO compensation packages; however, approximately one-third say the application of pressure by stockholders and institutional investors will be the most likely way to control CEO pay growth. Forty-one percent say boards and compensation committees will take a firm stand to bring about change.

***Boards could be getting more from their full-board and individual director evaluations.*** While nine out of 10 boards evaluate the entire board’s performance on a regular basis, 43% of directors say their boards’ evaluation processes could be improved. The study also provides a solution for the 23% of directors who feel there is a member of their board who should be replaced: 79% of directors say an effective board evaluation is the most important technique for ensuring directors continue to perform at peak levels.

***General counsel run the majority of board evaluations.*** This year, evaluations were facilitated by general counsel for 53% of participating boards, and 79% of directors on these boards say their GC is effective in this role.

“While it’s hard to argue that using inside counsel isn’t an efficient way to complete this task, I don’t feel it’s right to place general counsel in this position. If there is a sensitive board issue, I can’t imagine directors will be as candid with their concerns talking to an insider versus using an experienced third-party facilitator or trusted outside counsel,” says Kerstetter.

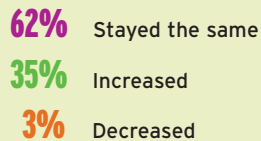
***Directors support board education, but most companies don’t designate funds for that purpose.*** An overwhelming 90% of directors in our study say they believe board members should attend director education seminars; however, only 40% of boards have a formal budget for director education.

## Conclusion

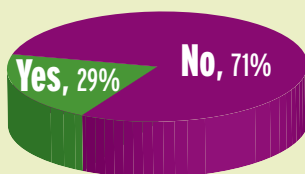
The What Directors Think study shows board members are taking their responsibilities seriously. And while directors could benefit from a closer look at their D&O policies, especially their Side A coverage, our overall results indicate they are concentrating on activities that help maintain a high standard of corporate governance. Board evaluations, continuing education for directors, and ongoing attention to important matters such as CEO succession can help directors mitigate their personal risk as they attempt to successfully discharge their most important duty: protecting the interests of shareholders.

**Figure 1**

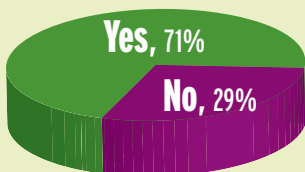
In the last 12 months, my risk as a director has

**Figure 2**

In the past year, have you resigned or thought seriously about resigning from any of the boards on which you serve?

**Figure 3**

Do you know what your Side A coverage is and what it means to you as part of your D&O liability policy?



The role of the director encompasses many responsibilities, chief among them to oversee a system of ethics and accountability and to maintain the balance of risk versus reward within the company. Yet, this oversight role leaves directors inherently exposed to liability, as courts, shareholders, and others see fit to determine whether, in any given situation, the board made judicious decisions and acted in an appropriate fiduciary manner. Financial liability, personal reputation, and even criminal charges for board members can hang in the balance when the propriety of their activities is called into question. The best-functioning boards strive to minimize risk by following accepted best practices and adhering to society's highest ethical standards. Even so, while there are myriad ways to mitigate director risk, there is no way to completely eliminate it.

### Director risk

According to the 2007 What Directors Think study, director risk—at least from the perspective of the directors themselves—appears to have plateaued. This year, more directors (62%, up from 52% in 2006, 26% in 2005, and 30% in 2004) say their risk stayed the same over the previous 12 months. Accordingly, fewer directors (35%, down from its 2005 peak of 73%) say they feel their risk as a director increased over the same period. The small number of directors (3%) who say their risk decreased is consistent with results we've seen for the past several years—evidence that although most directors aren't experiencing a sense of increasing risk, their overall perception of risk levels remain high (*Figure 1*).

We also asked directors to choose the worst-case scenario from a list of possible risk events. Having an investigation turn up evidence that the company illegally backdated stock options and having a director charged with insider trading are the two worst situations a board can face, say one-third of directors. Being forced to restate company earnings is next with 28% of the vote. Only 6% of directors say dealing with a *Wall Street Journal* report that the company CEO was the highest paid in a down year is the worst-case scenario.

### Few directors consider resigning

While directors are feeling the pressure of continued high risk, so far it has not been enough for most of them to consider leaving their board positions. Seventy-one percent of directors say they did not resign or think seriously about resigning from one or more of their boards in the past year. Twenty-nine percent say they resigned, or thought about doing so, during that time (*Figure 2*). Directors who considered resigning in the past year chose from a list of reasons for almost stepping down. Among that group, only 20% say they were concerned about personal liability, while 10% say they were worried about their personal reputation. Far more (40%) say they considered resigning primarily due to time constraints. Fourteen percent say they no longer find it fulfilling to be a director. Among the 16% of directors who selected "other," write-in reasons for contemplating departure include disapproval of the company's strategic direction, disagreements with management and the board, and personality conflicts, as well as more mundane reasons like travel requirements or changes in their primary employer's rules on outside board service.

## D&O liability coverage

With personal risk an ever-present component of boardroom service, it's natural for directors to be concerned about D&O insurance coverage. When asked about their level of insight on their current policy, half of directors say they are completely satisfied with how much they know about their D&O coverage. Most others (48%) are somewhat satisfied. Only 1% are dissatisfied, and the rest are not sure.

Yet, our study revealed a significant gap in directors' knowledge of coverage specifics. Nearly one-third (29%) of directors do not understand their Side A coverage (*Figure 3*). This is an area where it pays to be proactive in becoming educated about the structure of D&O policies and limits. Not all policies are created equal. Directors should demand details on all aspects of their policies, especially regarding Side A coverage, to ensure they aren't exposed to personal liability.

## Accountability to shareholders

In the past few years, a growing demand for accountability to shareholders has emerged. At some companies, pressure from shareholders has led to the elimination of staggered boards and the implementation of majority voting policies. Yet most directors do not see this as an immediate threat: Only 10% believe the majority voting rules will significantly affect company boards in the immediate future, 61% say the new rules will not have a significant, immediate effect, and 29% are uncertain (*Figure 4*). However, looking further out, 29% believe boards will see significant changes over the longer term from majority voting.

Our data shows directors feel they are already strongly accountable to shareholders. In fact, when asked to rate the most important constituencies they serve, directors rank all shareholders first, followed by institutional investors, customers, creditors, management, employees, analysts and Wall Street, activist shareholders, and the community (*see Table 1*). When asked about their knowledge of the broader purpose and strategic plan of their companies, nearly all directors we surveyed (96%) are confident they would be prepared to speak up at the company's annual meeting if a shareholder asked for their opinion of the company's vision (*Figure 5*).

**Table 1**

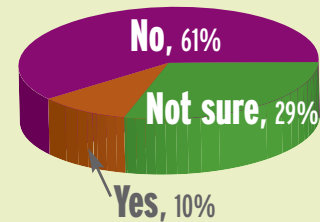
Given that directors serve multiple constituencies, which are the most important? (*Listed in order, according to director responses.*)

- All shareholders
- Institutional investors
- Customers
- Creditors
- Management
- Employees
- Analysts and Wall Street
- Activist shareholders
- The community

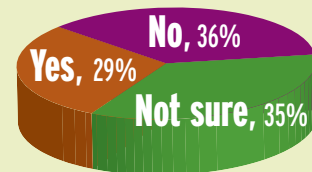
**Figure 4**

Do you believe the majority voting rules will significantly impact company boards

in the immediate future?



in the long-term future?



**Figure 5**

Would you be prepared to answer if a shareholder at the company's annual meeting asked your opinion of the company's vision?

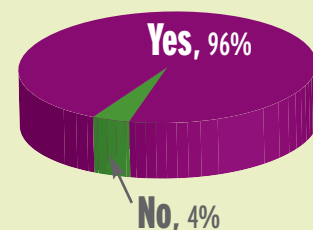


Figure 6

Should the chair position be held by an independent director?

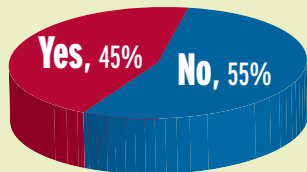


Figure 7

Is the position of chair/CEO separate on your board?

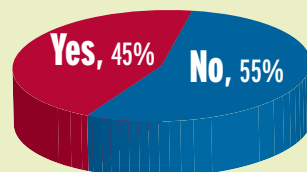


Figure 8

If a member of the board leaked sensitive board meeting information to the public, the appropriate action would be to

- 81%** ask the director to resign immediately.
- 12%** give the director a stiff warning but let him/her stay on the board.
- 2%** take no action if the prohibition on public statements was not stated in any code of conduct or governance guideline.
- 5%** take some other action.

The scandals and subsequent reforms of the last five years have solidly established the requirement for boards to remain above reproach in their standards of ethical behavior and independence in the boardroom. Now, more than ever before, directors understand the need to maintain objectivity and to employ the tools necessary for good decision making, accountability, and oversight of their corporations. In this vein, our study sought to gauge directors' responses to a number of issues related to ethics and board governance, to establish trend lines, and to measure both progress and ongoing challenges within this realm.

### Hallmarks of good governance

We asked directors to rate the importance of 16 potential hallmarks of good governance. The top five hallmarks, in order, according to directors' ratings, are as follows: the board holds regular executive sessions without the CEO; the board is composed mostly of independent directors; the board or a committee conducts regular, formal CEO performance reviews; the company has a formal management succession process in place; and the board evaluates both whole-board and director performance. Term limits and mandatory retirement ages have the least contribution to good governance, directors say.

### Board leadership

Directors ranked having an outside director chair low on the list of hallmarks of good governance (13th among 16 items), and 55% did not agree the chair should be an independent director (*Figure 6*). An identical percentage of boards in our study separate the CEO and chair positions. Over half (55%) combine the CEO/chair position. (*Figure 7*).

### Information leaks

In light of high-profile, board-level press leaks, some boards are revisiting their confidentiality agreements, strengthening the wording and drawing a more definitive line between dos and don'ts. But it's important to note a director who releases sensitive information to the press may be violating more than just his or her contract with the board. If the leak harms the company, such conduct could be tantamount to a failure of fiduciary responsibility to protect the interests of shareholders.

In the 2007 What Directors Think survey, we asked directors to select the most appropriate action the board could take against a director who leaked sensitive information to the public. Choosing from a list of possible actions, most (81%) say the board should ask the director to resign immediately (*Figure 8*). Twelve percent say the board should give the director a stiff warning, but allow him or her keep the seat. A few (2%) say if there is no explicit confidentiality agreement in the code of conduct or governance guidelines, the board should not take action. Most of the 5% of respondents who say the board should take other action indicate the board's action should depend on the information leaked.

## Red flags signal need for director involvement

We asked directors to rank several key indicators according to their importance as signals for directors to step up involvement on the board. As in our previous study, according to the average director rating, the number one sign a director should become more involved on the board is an earnings restatement. Other red flags (listed in order) include research showing a poor customer satisfaction track record; management's failure to meet strategic performance goals; an adverse 404 opinion; and study results showing poor employee morale (*Table 2*).

**Table 2**

Red flags that signal a director should step up his or her involvement in the board (*listed in order according to director responses*):

- An earnings restatement
- Research showing a poor customer satisfaction track record
- Management's failure to meet strategic performance goals
- An adverse 404 opinion
- Study results showing poor employee morale
- Company is the target of employee lawsuits
- Stock price is declining
- Quarterly financial results miss analysts' whisper numbers
- Low ISS governance quotient rating

## Lack of information shows communication breakdown

While directors rate customer satisfaction and employee morale among the top five risk indicators, a number of boards don't receive information that would alert them to problems in these areas, according to our study. Only 51% of boards received general or specific information on customer satisfaction in the previous two years, and only 58% saw data on employee values or satisfaction. Although the numbers are still relatively low, they indicate improvement over the 2006 results (*Figure 9*).

## Board influences

Slightly fewer directors in this year's study (45%, compared with 51% in 2006) say institutional investors are the strongest influence on their board (*Figure 10*). Meanwhile, the influence of analysts appears to be growing: 32% of directors say they are the most influential group, compared with 26% last year. Other directors say the strongest board influences are ISS and rating agencies (17%), activist hedge funds (4%), and the plaintiffs' bar (2%).

## Earnings integrity

This year the vast majority of directors again say they are satisfied with their company's quality of earnings, specifically the degree of conservatism versus aggressiveness in accounting policies, judgments, and estimates (*Figure 11*).

**Figure 9**

Boards received the following types of information in the last two years:

General or specific customer satisfaction research

**51%** 2007 **43%** 2006

Comparison peer group financial business data

**92%** 2007 **83%** 2006

Information on employee values or satisfaction

**58%** 2007 **48%** 2006

**Figure 10**

Which of the following groups do you believe influences your board the most?

- 45%** Institutional investors
- 32%** Analysts
- 17%** ISS and rating agencies
- 4%** Activist hedge funds
- 2%** Plaintiffs' bar

**Figure 11**

How comfortable are you with the company's quality of earnings?

- 83%** Very comfortable
- 17%** Somewhat comfortable
- 0%** Uncomfortable

Figure 12

Are you satisfied with the planning of your company's management succession?

Yes	65%	2007	57%	2006	53%	2005
No	35%	2007	43%	2006	47%	2005

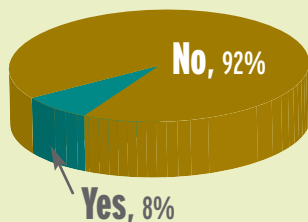
Figure 13

In general, do you believe U.S. company boards are having trouble controlling the size of CEO compensation?

Yes	67%	2007	66%	2006
No	25%	2007	23%	2006
Not sure	8%	2007	11%	2006

Figure 14

Do you believe shareholders should have a vote in approving CEO compensation packages?



Among the many critical issues boards must grapple with, few are more important than ensuring there is a well-thought-out and efficient management succession plan in place. Boards should address the company's succession plan well in advance of an executive departure, so no matter what event precipitates the need for change, shareholders, employees, and the public will be assured of continuity of leadership at the helm.

Related to the issue of executive succession is the board's responsibility to address the retention of the current CEO and other senior executives, both to assure management continuity and to design compensation packages that motivate management to improve company performance and build shareholder value.

This year's study asked directors their opinions on several topics related to CEO succession, recent reforms in the disclosure of CEO compensation, and the means by which such reforms are likely to have a positive effect.

### Succession planning

The CEO is the most influential person in the company, and when boards go through the process of filling that position, they can spend an enormous amount of time selecting the best candidate. Once a new CEO is hired, however, it's human nature to postpone dealing with ongoing succession planning. For many boards, in fact, this is an area of critical weakness. But identifying several internal or external candidates and having a chain of succession is the only way to protect continuity when key members of management step down or an unforeseen crisis occurs. It is up to directors to take the lead on CEO succession planning and demand a strategy, no matter how far in the future they hope management changeover may be.

The good news from our study is that boards are becoming more proactive on this front. This year, 65% of directors report they are satisfied with their company's management succession plan; this number is up from 57% in 2006 and 53% in 2005 (*Figure 12*).

Of the 35% of directors who say they are not satisfied with succession plans at their company, a majority (52%) attribute their displeasure to the fact that management succession is not a regular item on their board's agenda. Others say they are dissatisfied because their board tries to handle management succession only as the need arises (35%) or because their CEO is uncomfortable with the topic (20%).

### Executive compensation

Both the amount and structure of executive compensation have attracted media and shareholder attention in the past year. Pay for performance was a major topic for shareholders in 2007, and it isn't likely to disappear anytime soon. Part of the outcry has centered on large severance payouts, which some shareholders view as inappropriate, especially in the case of poor company performance. For the second year in a row, approximately two-thirds of directors in our study say U.S. company boards are having trouble controlling the size of CEO compensation (*Figure 13*).

These findings indicate the perception of excess in CEO pay is pervasive, yet the bigger question will be to determine how boards will address the issue. Directors are somewhat divided on their predictions of which group will ultimately step in to control rapid growth in CEO pay. Under half (41%) say board compensation committees will take a firm stand to promote change, while approximately one-third (31%) say stockholders and institutional investors will apply enough pressure to companies to control CEO pay growth (Table 3). This will be an important issue to watch; in a related question, the vast majority (92%) of directors say they believe shareholders should not have a vote in approving CEO compensation packages (Figure 14).

**Table 3**

Which of the following is most likely to curtail the rapid growth of CEO compensation in many of today's companies?

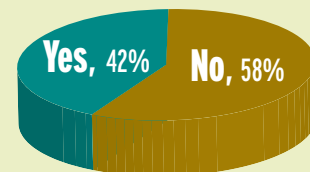
Boards and compensation committees will take a firm stand to promote change.	41%
Stockholders and institutional investors will apply enough pressure to companies to bring a change.	31%
I don't believe many companies have the problem of rapid CEO compensation growth.	16%
I'm not sure rapid growth can be curtailed in certain companies.	6%
CEOs themselves will recognize the need for change.	3%
SEC regulations will give rise to change.	2%
Congress will have to get involved.	1%

Though the pressure to create more transparency for CEO pay is strong, few directors (3%) say CEOs themselves will recognize the need for change and initiate a slowdown in the growth of their pay; 42% say they believe the fact that a few CEOs are agreeing to work without contracts could indicate a trend (Figure 15).

New disclosure requirements have certainly had an impact in the compensation arena this year. Even so, three-quarters of responding directors say they believe providing full disclosure of senior management compensation in the proxy is a positive step for publicly listed companies (Figure 16). Most (89%) are either not concerned or only somewhat concerned about SEC rules requiring greater disclosure of senior management compensation. With the first year of reporting under the new rules behind them, it is likely most companies will find the process more straightforward in the future.

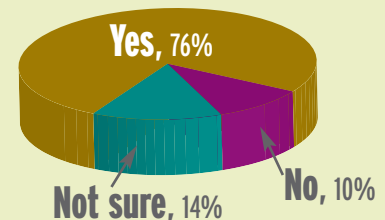
**Figure 15**

Could the fact that a few respected CEOs are agreeing to work without employment contracts become a trend?



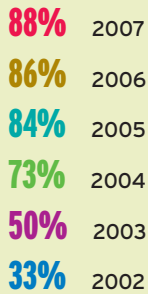
**Figure 16**

Do you feel providing full disclosure of senior management compensation in the proxy is a positive step for publicly listed companies?



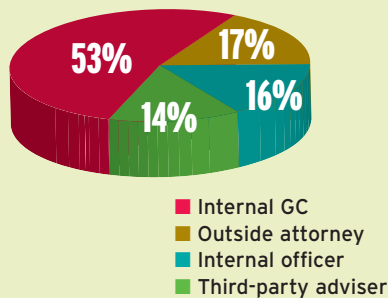
**Figure 17**

What percentage of boards conduct a full-board performance evaluation on a regular basis?



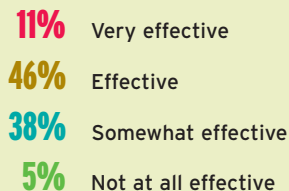
**Figure 18**

Who facilitated the evaluation process this year?



**Figure 19**

How effective is the evaluation process at improving your board's performance?



The periodic need to look inward and accurately gauge one's own performance is a necessary function for all high-performing organizations. Corporate boards are no different. An honest evaluation helps ensure the board as a whole and its individual members are maintaining peak performance and operating effectively.

In 2002, the first annual What Directors Think study asked directors whether their entire board's performance was evaluated on a regular basis. At that time, only 33% of directors said yes. We've asked the question every year since and have seen a clear trend: The number of boards that conduct regular full-board evaluations has grown markedly (*Figure 17*). In the second year of our survey (2003), the number of boards engaging in the practice jumped to 50%. However, the largest leap forward was in 2004, when the NYSE requirement that boards perform annual self-evaluations went into effect. That year, the number of boards reporting a policy of regular self-evaluations was 73%. And the number continues to grow. According to our 2007 survey, 88% of boards conduct a full-board performance evaluation on a regular basis—a more than twofold increase over the 2002 figure. Interestingly, a substantial majority (78%) of respondent companies listed on NASDAQ also do a formal evaluation of board performance regularly, even though NASDAQ does not mandate it.

### Role of the nominating committee

NYSE governance rules require the nominating and governance committee to oversee the board's evaluation, but they are silent on the practical details, such as who should facilitate the evaluation process. Our survey found that the internal general counsel facilitates the board evaluation for approximately half (53%) of represented boards (*Figure 18*). Among those boards, 79% of directors say their general counsel is an effective facilitator, while 19% say their general counsel is only somewhat effective, and 2% say the GC is not at all effective. Other boards use an outside attorney (17%), an internal officer (16%), or a third-party adviser (14%) to facilitate the evaluation.

### Getting the most from your board evaluation

More than half of directors say their board's evaluation process improves performance. Fifty-seven percent characterize the board evaluation process as effective or very effective, 38% say their board's process is only somewhat effective, and 5% say it is ineffective (*Figure 19*).

These results show many boards are not maximizing the usefulness of this process, which, among other things, directors have told us can improve board communication, provide focus for board and management recruitment efforts, and identify ways to streamline board processes to make the best use of directors' time. With these benefits, it seems worthwhile for all directors to ensure their boards are conducting the most efficient and effective evaluations possible.

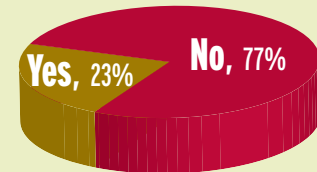
## Evaluating individual directors

Even the best-performing boards can have a weak link. Nearly one-quarter (23%) of directors say a member of their board should be replaced (*Figure 20*). Among those, 36% say the director in question should be removed because he or she lacks the necessary skill set, 31% say the director is not engaged, 18% say the director comes to board meetings unprepared, and 17% say the director has been on the board too long.

A robust board evaluation examines board functions from at least three perspectives—full board, committee, and individual director—and aims to identify areas for continued improvement so directors can manage problems and better attend to business. The majority (79%) of directors say an effective board evaluation process is the most important technique for ensuring directors continue to perform at peak levels (*Figure 21*). Far fewer say mandatory retirement ages (11%) or term limits (5%) are the best means for achieving that end. The latter are consistent with director ratings of hallmarks of good governance (discussed earlier in Part Two of this report), further supporting the finding that directors feel these are the least important factors in good governance.

**Figure 20**

Is there a director on your board you feel should be replaced?



If so, why do you feel that director should be replaced? (Some directors made multiple selections.)

- 36%** The director does not have the skill set needed.
- 31%** The director is not engaged.
- 18%** The director comes to meetings unprepared.
- 17%** The director has been on the board too long.

**Figure 21**

Which of the following techniques is most important in ensuring directors continue to be effective on the board?

- 79%** Effective board evaluation process
- 11%** Mandatory retirement age
- 5%** Term limits

Figure 22

Do you believe board members should attend director education seminars?

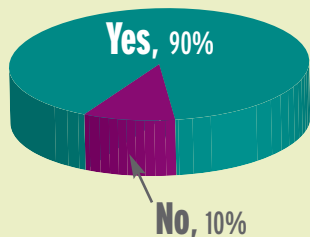


Figure 23

Does your company have a formal budget for board education?

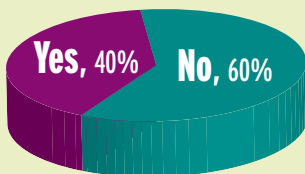


Figure 24

Companies that have a formal budget for board education, by revenue range:

56%	Over \$10B
52%	\$5.1B–\$10B
41%	\$1B–\$5B
27%	Under \$1 billion

Director education is an ever-growing focus in a business environment that has undergone wave after wave of regulatory change, leading to increased board responsibilities. Quite simply, without access to continuing education, it's difficult for even the most capable directors to keep up with everything they need to know to fulfill their roles as competent fiduciaries for shareholders. And new directors experience an even steeper learning curve, making the job of director recruitment more challenging than ever.

### Board education

Our study shows directors continue to support the concept of director education. This year, 90% (up from 83% last year) say they believe board members should attend director education seminars (Figure 22). But 60% of boards have no formal budget for board education (Figure 23). When we narrow the results to include only responses from directors at NYSE-listed companies, the numbers remain virtually the same—57% of those boards do not have a formal budget for board education, despite NYSE rules requiring that public companies' corporate governance guidelines address director orientation and continuing education. Our survey shows directors of companies with higher annual revenues are more likely to report their board has a formal budget for board education. Yet, even among directors from companies with more than \$10 billion in revenues, only 56% say their company has a formal director education budget (Figure 24). Perhaps this is the reason 42% of directors report they had four hours or less of outside director education over the previous 12 months (Figure 25). And while 11% say they spent 25 hours or more in outside education sessions in the 12 months prior to the survey, that number also means nine of every 10 directors spent no more than three working days in educational sessions in the 12 months prior to the survey.

It also appears boards are not making up for the lack of external training by bringing education into the boardroom. Nearly two-thirds (59%) of directors report that they spent four hours or less on internal board training in the past 12 months, while only 2% report spending 25 hours or more on that type of education. But perhaps most directors believe they get all the information they need from the company itself: 82% of directors say their companies keep them updated on the industry, competition, and technology. Also, when asked to rate their comfort level with their companies' financial statements, directors reveal that overall they feel they have a high level of understanding of their financial statements, including discussions with management and external auditors about the financial statements.

### Difficulty of tasks

We asked directors to rate the difficulty of serving on the audit committee, serving on the compensation committee, and fulfilling several other director responsibilities. While every task on our list falls into the difficult to very difficult category, directors rank some tasks as harder than others. Yet when it comes to the most difficult task at hand, not much has changed in the past six years: Directors this year say the toughest board task is serving on the audit committee, mirroring

their answer in 2002. The next most demanding tasks, in order, include serving on the compensation committee, ensuring that the company's strategy and risk appetite are appropriate, determining CEO compensation, evaluating CEO performance, ensuring the integrity of the company's financials, and understanding the company's marketplace.

### Recruiting new directors

Interestingly, 57% of boards have no reservations about recruiting directors who have not had previous board experience (Figure 26). Perhaps this is because board education—particularly orientation—is more readily available today to support new directors. Or, perhaps it is due to a growing awareness that boards need new members who will bring fresh perspectives and needed skills to assist the board in overseeing the company.

### Control of director nominations/elections

Only 13% of directors say their CEO has the most influence in nominating new directors (Figure 27). That power resides with a committee of the board, 64% say. Other directors report that the full board (18%) or the nonexecutive chair/lead director (5%) has the most say in choosing board nominees.

Figure 25

Please estimate the hours you have spent over the past 12 months on

	Outside board training	Internal board training
4 hours or less	42%	59%
5–8 hours	20%	25%
9–16 hours	17%	12%
17–24 hours	10%	2%
Over 25 hours	11%	2%

Figure 26

Does your board have any reservations about bringing in a new director with no previous board experience?

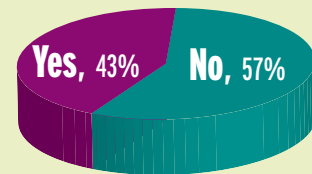


Figure 27

In selecting your next new director(s), who will have the most influence in determining nominees?

- 64%** A committee of the board
- 18%** The full board
- 13%** CEO
- 5%** Nonexecutive chair or lead director

Figure 28

Who has final responsibility for approving your board meeting agenda?

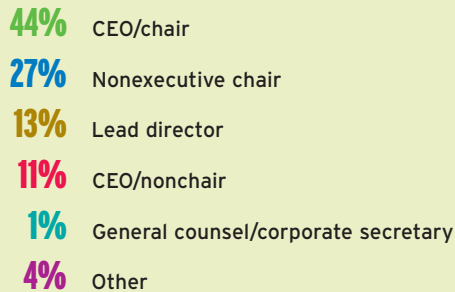


Figure 29

Has your board spent time determining the board's scope, deciding what topics are worthy of the board's time and attention?

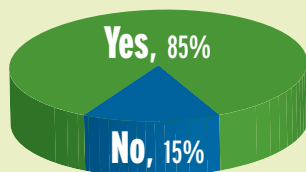
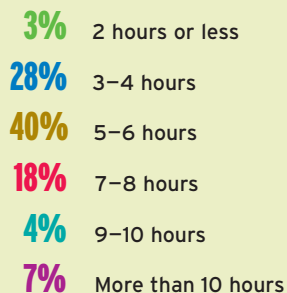


Figure 30

Typically, how long are your full board meetings?



Directors give a lot to their companies and they receive both tangible and intangible benefits in return. While it's hard to accurately describe the complexities and subtleties of that exchange, some aspects of it are black and white, such as the amount of time spent on the job and the compensation received. As a means of benchmarking these findings, the 2007 What Directors Think study captured a snapshot of director time commitments, the structure and agenda for full board and committee meetings, and directors' level of satisfaction with remuneration and additional job rewards.

### Meeting agendas and discussion topics

This year's study again looked at the balance of power within the boardroom and found that the CEO (both chair and nonchair) continues to set the agenda for 55% of boards (Figure 28). Nonexecutive chairs set the agenda for just over one-quarter of boards. On most other boards, the lead director controls the agenda.

Despite the fact that CEOs most often control the agenda, directors have a say in which issues should become board priorities. Most boards (85%) have devoted time to determining their scope and deciding what topics are worthy of board time and attention (Figure 29).

### Board meetings

Forty percent of boards report their full board meetings last between five and six hours (Figure 30). On matters pertaining to their primary board, directors spend an average of 20 hours per month, including review and preparation time, meeting attendance, and travel (Figure 31). Overall, although the time directors spend on board matters has decreased slightly from the post-Enron peak of 22 hours per month in 2005, we don't expect to see directors' monthly time commitments drop back to the pre-Sarbanes-Oxley era average of 14 hours.

### Committees

Committees are key to how the board fulfills its corporate governance obligations. In nearly all cases, the chairman of the committee exercises true control: Directors tell us committee chairs (72%) are overwhelmingly responsible for committee meeting agendas. Other parties responsible for setting committee agendas include the nonexecutive chair (7%), the CEO (6%), the general counsel or corporate secretary (6%), and the CFO (5%).

The work of the audit committee is by far the most taxing in terms of time commitment: 58% of audit committee members tell us their audit committee meetings last between three and four hours. While almost half (49%) of compensation committee members say their meetings last from three to six hours, the other half hold meetings that last two hours or less. The governance and nominating committees hold the shortest meetings—88% last two hours or less (see Table 4).

**Table 4**

How long do committee meetings last?

	Governance/Nominating	Compensation	Audit
2 hours or less	88%	50%	25%
3–4 hours	11%	46%	58%
5–6 hours	1%	4%	16%
All day	0%	0%	1%

### Director compensation

As many compensation consultants will attest, it's difficult to put an appropriate dollar figure both on the amount of time and energy a director provides in his or her role on the board and the amount of value each adds, which makes determining fair and proper remuneration for directors a complex issue for many boards. While most directors we surveyed (79%) say they are satisfied their director compensation is fair, approximately one-fifth (21%) believe they are not adequately compensated for the job (Figure 32).

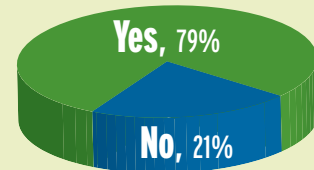
**Figure 31**

How many hours per month do you estimate you spend on board matters for your primary board, including review and preparation time, meeting attendance, and travel?



**Figure 32**

Do you believe your compensation for serving as a director is adequate?



# Profile of U.S. Corporate Boards

The profile of boards of directors from publicly traded U.S. companies, published below, is the most recent snapshot available from *Corporate Board Member's* comprehensive database of directors and officers serving on boards of publicly traded companies listed with the NASDAQ Stock Market, New York Stock Exchange, and American Stock Exchange.

## Number of Directors Per Board

At the end of 2007, directors on U.S. corporate boards totaled 48,950 from 5,772 publicly traded companies. This represents an average of 8.48 directors per board, with boards from larger companies averaging a higher number of directors than those from smaller companies, as shown below.

Revenue size (\$)	Companies	Directors	Average
>\$10B	376	4,647	12.4
1.1B-10B	1,201	11,960	10.0
501M-1B	582	4,987	8.6
101M-500M	1,384	11,082	8.0
51M-100M	584	4,414	7.6
10M-50M	845	6,221	7.4
<10M or no sales reported	800	5,639	7.0
Entire Database	5,772	48,950	8.48

## Number of Directorships Held

The highest number of directorships held by one individual is 10. The vast majority of directors, 32,408, hold only one board seat. The table below shows the distribution of the number of directorships held by U.S. corporate directors.

No. of directorships	Directors
10	1
9	0
8	0
7	10
6	38
5	142
4	439
3	1,425
2	4,743
1	32,408

## Inside Versus Outside Directors

U.S. corporate boards had 8,804 inside directors, representing an average of 1.53 inside directors per company, and 40,146 outside directors, representing an average of 6.96 outside directors per company.

Revenue size (\$)	Cos.	Inside	Avg. inside	Outside	Avg. outside
>\$10B	376	907	2.4	3,740	9.9
1.1B-10B	1,201	1,872	1.6	10,088	8.4
501M-1B	582	832	1.4	4,155	7.1
101M-500M	1,384	1,952	1.4	9,130	6.6
51M-100M	584	846	1.4	3,568	6.1
10M-50M	845	1,194	1.4	5,027	5.9
<10M or no sales reported	800	1,201	1.5	4,438	5.5
Entire Database	5,772	8,804	1.53	40,146	6.96

## Inside Versus Outside Chairs\*

Out of a total of 5,341 chairmen on U.S. corporate boards, 2,618 (49%) are inside chairmen and 2,723 (51%) are outside chairmen. These ratios hold steady among revenue size categories, as shown below.

Revenue size (\$)	Companies	Inside chair	%	Outside chair	%
>\$10B	359	194	54.0%	165	46.0%
1.1B-10B	1,161	616	53.1%	545	46.9%
501M-1B	556	297	53.4%	259	46.6%
101M-500M	1,300	623	47.9%	677	52.1%
51M-100M	534	250	46.8%	284	53.2%
10M-50M	747	314	42.0%	433	58.0%
<10M or no sales reported	684	324	47.4%	360	52.6%
Entire Database	5,341	2,618	49.0%	2,723	51.0%

## Gender of Directors

Women occupy 4,544 seats on U.S. boards, averaging 0.8 per company. Larger company boards have a significantly higher representation of women compared with smaller companies.

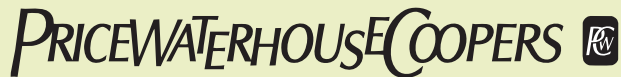
Revenue size (\$)	Companies	Female directors	Average per co.
>\$10B	376	626	1.7
1.1B-10B	1,201	1,779	1.5
501M-1B	582	408	0.7
101M-500M	1,384	763	0.6
51M-100M	584	281	0.5
10M-50M	845	381	0.5
<10M or no sales reported	800	306	0.4
Entire Database	5,772	4,544	0.8

\*At the time of this report, 431 companies did not report a chairman.

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M A G A Z I N E

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