

Lead Directors: A study of their growing influence and importance



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The heart of the matter

Lead director's challenge: Helping pilot the company through choppy seas

Facing pressure from shareholders, regulators, and economic forces and also seeking to improve the performance of corporate boards, US companies came up with a solution to corporate governance and leadership issues with the concept of a lead director. Since its inception, the lead director role has grown in importance and influence. A lead director is particularly helpful in focusing the board's talent and wisdom when difficult situations arise: management performance and succession, risk management, mergers and acquisitions, and a host of other internal and external matters.

We compiled survey and other data to look at lead directors' backgrounds, what they do, and what they see as the most important elements of their service now and in the future. Respondents from 16 sectors represent the spectrum of US industries, and their companies range largely in revenue from \$4 billion to \$100 billion. These companies' lead directors were chosen most frequently by other independent directors and for either an indefinite term or a one-year term, according to the respondents. Almost half have been a lead director for four or more years, and most often they also serve on the governance/nominating committee or the compensation committee.

Looking ahead, those surveyed expect the lead director to delve further into shareholder and governance issues, be more involved in risk management, drive succession planning to ensure the process produces top leaders, and strengthen the independence of the board.

On the horizon also are issues related to how the lead director's role will change if companies alter their organizational structure. At the surveyed companies, 67 percent still have a combined position of board chairman-CEO despite increasing pressures from stakeholders and regulators to split these functions. Some commentators have asserted that with effective lead directors becoming increasingly active in managing the board, there will be less pressure to appoint an independent board chairman.

Typically, the lead director's background is in general management of a public company, often as a past chair, CEO, or president, although a small number have not had any prior position with a public company. With experience in leadership and past exposure to corporate crises and complex problems, a lead director is well situated to offer helpful guidance to other independent members of the board and serve as a key advisor to the CEO.

A majority of those surveyed have input on the chairman's development of agendas for board meetings and materials to be sent to the board, and all of them have authority to call and preside over executive sessions. As for communicating with the chief executive between board meetings, everyone surveyed talks to the CEO, and half talk to the CEO more than five times. Depending on the number of board meetings held each year, these conversations can be quite frequent. Some companies meet quarterly, and larger and more complex companies may meet as many as eight to 10 times.¹

The job is a demanding one requiring the majority of the survey group to spend six to 10 hours a month beyond the time they spend as a director. In some cases, that commitment grows considerably to 16–20 hours or more. The vast majority, 75 percent, receive additional compensation to be lead director, regardless of how much time they dedicate to this role. There is no consensus, however, on how much to pay. Respondents report a wide range—from \$5,000 to \$150,000 per year in additional compensation. The mean compensation reported is \$77,500, and the average is \$35,575.

¹ William G. Bowen, *The Board Book: An Insider's Guide for Directors and Trustees* (New York: W.W. Norton & Company, 2008), 155.

The effective lead director

Bill Baxley, Mike Egan, and Jeff Stein, partners, King & Spalding LLP

Six years after the New York Stock Exchange (NYSE) mandated the presiding director² position as a result of the corporate scandals of the last decade, little consensus has emerged regarding the roles presiding or lead directors should undertake and how they can act most effectively to improve the governance and performance of their companies.

20 members, who serve as lead directors of 26 companies such as Caterpillar, Coca-Cola, Delta Air Lines, Eli Lilly, Home Depot, Microsoft, Morgan Stanley, and Wal-Mart.

A key focus of the LDN has been to address the roles and activities of the lead director that add the greatest value for boards, companies, and shareholders.⁴ The LDN

“It has been fascinating to watch the lead director position evolve from a concept developed by the stock exchanges as a result of some high-profile corporate scandals into an important catalyst in the improved governance of most leading US companies.”

—Peter C. Browning, lead director, Nucor, and director, Acuity Brands, EnPro, and Lowe’s

The approach adopted by the NYSE requires boards only to establish a mechanism for the independent directors to hold executive sessions and receive shareholder communications. Boards often have appointed a single independent director to preside at these executive sessions, and the lead director position has evolved from that ministerial role to a position of increasing responsibilities within public US companies.

Our law firm has worked closely with a select group of lead directors from many top American companies, principally Fortune 500 companies, in a Lead Director Network (LDN)³. These directors hold private discussions about how to improve the performance of their corporations and earn the trust of their shareholders through more effective board leadership. The LDN includes

members have recognized that lead directors are contributing to enhanced corporate performance in at least three key areas:

- Taking responsibility for improving board performance,
- Building a productive relationship with the CEO, and
- Providing leadership in crisis situations.

Lead directors in the LDN also foresee a growing role for board leadership in communications with shareholders. Ironically, these areas where lead directors are making the most valuable contributions are not among those officially mandated for the role as originally envisioned by the NYSE.

Driving a high-performance board

While boards must have an independent nominating and corporate governance committee accountable for certain aspects of board and committee operations, increasingly, lead directors are also taking respon-

² For purposes of the survey, a lead director was defined as a lead director, presiding director (serving a term of at least one year), or nonexecutive (independent) board chair.

³ King & Spalding and Tapestry Networks created the Lead Director Network, which meets three times a year. Additional information regarding the LDN (including reports from each of its meetings) may be found on the King & Spalding website at the following link: <http://www.kslaw.com/portal/server.pt?space=KSPublicRedirect&control=KSPublicRedirect&CommunityId=433>.

⁴ See question 35 of this PwC survey, where the respondents confirm that shareholder communication is not currently an important part of their role.

sibility for monitoring and improving board performance. For example, many lead directors are active in facilitating board discussions, helping directors reach consensus, and formulating “next steps” to be taken on important matters. Often, lead directors keep the discussion at the right altitude—ensuring the board effectively engages on corporate issues without meddling in management’s day-to-day decision making. This engagement is particularly valuable in shaping the corporation’s strategy.

Many lead directors also are handling a task that has always been difficult for the chairman-CEO: dealing with difficult or underperforming directors. Rather than letting these situations fester until annual board self-evaluations or nominations, lead directors can proactively and diplomatically address them. The lead director also can take an active role in an often-overlooked issue, board succession. By working with (or often chairing) the nominating committee, the lead director can help ensure the board has the range of experience and attributes necessary to address key issues affecting the corporation.

Building a productive relationship with the CEO

Building a productive relationship between the board and the CEO may be the lead director’s most important contribution. Lead directors report that their role in supporting effective CEO performance can be especially rewarding. In some instances, a lead director with considerable experience in the corporate world may be the primary mentor for the

CEO. The lead director may draw on his or her own experience as a CEO as the basis for this relationship and can funnel recommendations from other directors without the appearance of the directors ganging up on the CEO.

The study indicates that 73 percent of lead directors are former or current chairmen, CEOs, or presidents of public companies, which facilitates the effective performance of this role. It is natural, then, that 50 percent of the lead directors participating in the survey report that they confer with CEOs more than five times between board meetings.

Leadership in a crisis

Because they often have considerable prior experience in dealing with difficult corporate matters, lead directors often make valuable contributions in times of crisis. Whether facing a challenge for corporate control or evaluating responses to a government investigation, a corporation may benefit from drawing on the experiences of an additional seasoned corporate leader. In such important situations, the lead director may collaborate with the CEO to provide more judgment and perspective.

In other settings, the lead director’s contributions may be especially important if the corporation faces issues with CEO performance. Here, the lead director may work intensely to support the CEO or, if necessary, lead the board’s process of replacing the CEO. Not surprisingly, the survey indicates that 88 percent of lead directors feel that the position has been very helpful in resolving corporate crises.

Supporting effective shareholder communications

With the recent increase in shareholder activism, companies are increasingly considering roles for lead directors in communicating with shareholders. Although management remains principally responsible for investor relations, having a lead director who can assist in certain types of communications may add a useful voice. Since independent directors often are viewed as carrying the flag for shareholders, in some instances it may be natural for lead directors to communicate directly with shareholders, particularly activist hedge fund or institutional shareholders who are voicing concern about company strategy or management performance. Lead directors can also play a key role in communicating with shareholders on questions involving management compensation.

Our experience with the LDN and in board situations generally leads us to expect that the participation of lead directors in direct communications with shareholders will become a more important role.

Conclusion

The lead director position was created as a compromise between having a board with no leader of its independent directors and mandating that every company have a nonexecutive chairman. So far, the most important contributions of lead directors have come **not** from the duties mandated by stock exchange requirements, but from the responsibilities that lead directors in fact have undertaken for their companies as the de facto leaders of the independent board members.

The lead director role will continue to evolve as companies have more experience with the concept and as the spotlight remains on corporate governance issues. Moreover, as some activist shareholders and lawmakers renew their call for the required separation of the chairman and CEO positions, it will be interesting to see if the continued bolstering of the roles assumed by lead directors serves as an acceptable compromise for corporations and their stakeholders.



An in-depth discussion

Dealing with a crisis

Approximately one-third of lead directors who responded to the survey indicate that their company has experienced a business crisis in the last three calendar years, and in many cases that crisis overlapped in more than one internal or external area (see Figures 1 and 2).

Lead directors tell us they take an active and substantive role in managing a crisis. These difficult situations cover a surprisingly wide range of subjects both internal to the company and in external areas involving third parties. In all, the respondents identified 22 areas where their companies have had a crisis.

Figure 1. Areas of internal crisis

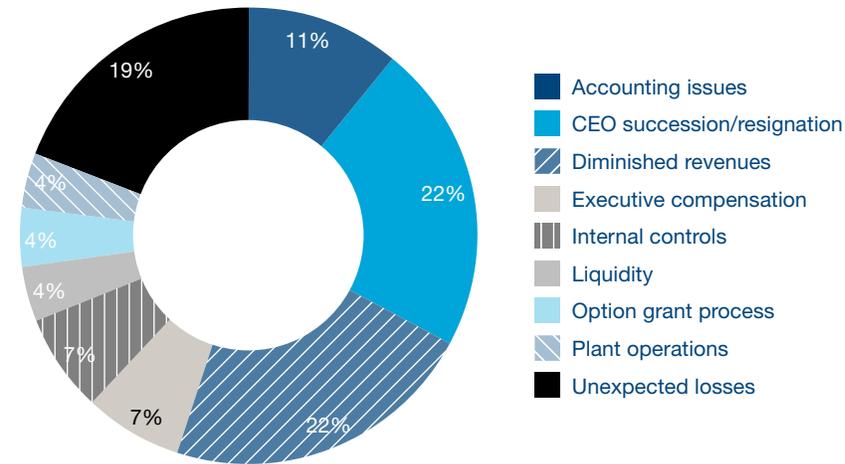
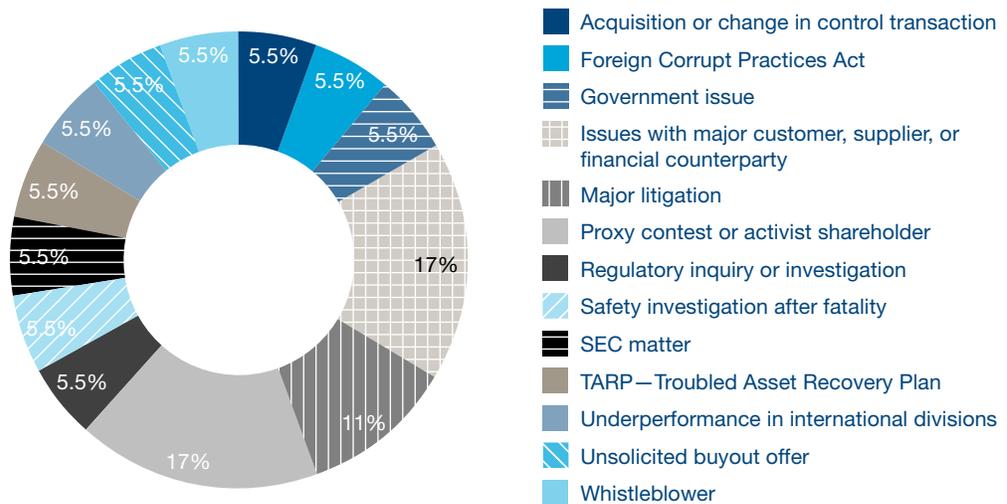


Figure 2. Areas of external crisis



Inevitably, a crisis requires the selection and retention of outside advisors such as law firms and accounting firms. About four in 10 companies rely on the CEO or other senior management to select these advisors. Five in 10 companies turn to the entire board to determine the choice or appoint a special committee to make recommendations; less frequently, the lead director makes a recommendation to the board.

The surveyed directors whose companies had a crisis overwhelmingly believe (88 percent) that having a lead director was helpful in resolving the crisis. Yet the figures are lower for the perceived benefit that a lead director brings to the company. Among all respondents, 65 percent say the lead director adds a significant benefit to the company; 35 percent find the value limited or between limited and significant.

Ranking their personal attributes, the lead directors put integrity at the top of the list by far, followed by judgment and ability to collaborate with the CEO—all valuable characteristics, especially in a crisis.

Advising directors in a time of crisis

H. Rodgin Cohen, senior chairman, Joseph B. Frumkin, and Glen T. Schleyer, partners, Sullivan & Cromwell LLP

A corporate crisis can arise at any time and in many ways. We all lived through the seriatim crises that imperiled the US financial system in 2008. These crises were extreme in their threat to individual corporations, their potential for collateral economic effects, their visibility, and the speed with which they developed. But the principles that constitute the touchstone of director responsibilities are the same in any crisis—whether that crisis is the incapacity of the CEO, a product recall, or the discovery of a financial fraud.

One important lesson to take away from the financial crises of 2008 is that the role of directors in a crisis situation is vitally important. The perspective that directors can

Although every crisis facing a board of directors will differ in its details, some basic principles should guide directors in almost any crisis. These principles include the following:

- **Fundamental legal duties—duty of care and duty of loyalty—are unchanged.** The exigencies of the matter do not impose higher standards, but they also do not relieve the directors of their responsibility to be as well informed as feasible under the circumstances. Although a crisis may force decisions to be made in compressed periods, directors must still do the best they can under the circumstances to obtain all the information reasonably available to help them make these decisions.

“Whether facing a crisis or not, a board should seek legitimate outside advice relevant to the event and act deliberatively as a group. Making sure this happens is one of the chief obligations of a lead director.”

—Patricia Hammick, lead director, Dynegy

bring to decision making can and should significantly assist management teams attempting to navigate a complex, stressful, and often novel business challenge. Lead directors help to organize, focus, and lead the board’s efforts.

Another important lesson to take away from the events of 2008 is that directors need not be unduly concerned about risks of personal liability in crisis decision making. All the usual legal protections available to directors remain available even in times of crisis, and the courts considering and evaluating director conduct in the midst of the 2008 crises uniformly and correctly took into account the circumstances under which directors were forced to act.

Board advisors and management must be charged with providing the board timely information necessary to make appropriately well-informed decisions.

Directors and their advisors also must consider whether any directors, officers, or advisors have conflicting interests that should be disclosed and whether those conflicts merit recusal from all or part of the decision-making process. This should be done early in the process, and directors, managers, and outside advisors should have a clear, shared understanding of the board’s expectations.

- **Fundamental legal protections, such as the business judgment rule and right to rely on management and third-party experts, are similarly unchanged.** Increased anxiety of directors in a crisis situation is understandable, but as long as sufficient care is taken and conflicting interests are identified, the risk of personal liability is minimal. The board should review legal duties and risks with counsel at the outset of any crisis, so that directors can clearly understand the range of protections available to them.

- **Preparation, even for the unexpected, can be critical.** Although the source of every crisis is different—for example, a financial reporting issue requires a different response than the incapacity of a CEO—some preparations may be useful for a variety of crises. For example, personal knowledge and direct experience with a CEO’s direct reports, including the CFO, general counsel, head of human resources, business unit heads, and the like, will be helpful to directors in many types of crises, permitting a more nuanced judgment of advice being received in the boardroom.

Some boards find it useful to retain their own outside counsel, or to meet in executive sessions with company outside counsel on issues that come up in the ordinary course. This experience with outside counsel would help the board determine in a crisis whether the counsel is appropriate for the crisis at hand.

As lead directors consider the board’s agenda for the future, they should anticipate the potential for crisis and try to prepare the board to deal as effectively as possible with any crises that arise.

- **Create a thoughtful, detailed record of the board’s deliberations.** The written record of board deliberations becomes critically important if board actions are subsequently challenged as hasty or uninformed. The appropriate written record is different for every situation, but as a general matter should accurately reflect the information presented, the advice received from management and outside advisors, a summary (the detail of which can vary depending on the circumstances) of the substantive deliberations and important matters considered, and a record of the decisions made. Supervision of the content of this record is an important responsibility of the general counsel or the person who performs this function for the company.

Sometimes people responsible for preparing minutes shy away from recording consideration of the possible risks of a course of action, but often the fact that directors considered such risks can be helpful. Because board minutes may become available to some people from outside the company (albeit under obligations of confidentiality), such as counsel for securities underwriters and third parties performing due diligence for a merger, acquisition, or other purpose,

and in some companies may have more than a minimal distribution within the company, there may be circumstances where it is advisable to record some detail of the board's deliberations in a memorandum outside the formal minutes. This has the advantage of creating a contemporaneous record while protecting sensitive details from a wider circle of readers.

- **Don't unnecessarily rush decisions.** One hallmark of almost every variety of crisis is that a board is likely to feel great pressure to act quickly. Some of this pressure will be external, with management, the government, auditors, or others suggesting that some decision needs to be made immediately. Some pressure may be internal to the board, where personal

“As a director of a number of public companies, I found this article to be a “must read.” Directors would be well served to follow the road map laid out by the authors. Understanding the directors’ role in a time of crisis as well as suggesting a decision making process were particularly well spelled out.”

—William H. Turner, member, board of directors, Franklin Electronic Publishers, Inc., Standard Motor Products, Inc., Volt Information Sciences, Inc., New Jersey Resources, Inc., and Ameriprise Financial, Inc.

- **Be mindful of the distinction between the roles of directors and the roles of managers.** Many directors are used to taking hands-on control of difficult situations and may have an instinct in a crisis to seek to manage that crisis to an outcome. Sometimes this step will be necessary or advisable, but it should not be taken without careful consideration. Usually it will be wise for directors to resist an impulse to take over and instead focus on working collaboratively with management and providing overall guidance and supervision to management's efforts to address the crisis.

schedules and time demands can make ending discussion and forming a decision seem an attractive course.

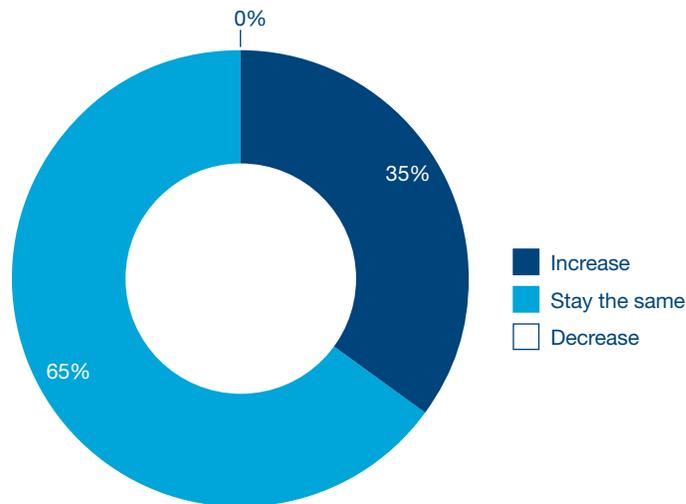
Directors always should be mindful that, especially in the midst of a crisis, the quality of information tends to improve and circumstances can change with each passing hour and day—and a lead director can be an effective counterweight to the pressures to move too quickly. Unless the correct course of action seems completely clear or delay will lead to unacceptable harm, directors should consider whether there are advantages to avoid rushing an important decision to allow the situation and information to develop. This is not intended to be an excuse for procrastination, but as a reminder not to be unduly rushed.

What this means for your business

Growing role of the lead director

A new voice—the lead director—is emerging to provide leadership to the board and company as many fundamental assumptions about the role of the board and its relationship to the senior leadership of the company are being challenged and revisited. Clearly, the board is going to have to be more informed about the aspects of the company’s operations, risks, strategies, regulatory requirements, and ethical standards. More boards are turning to a lead director as the person to coordinate and focus their efforts to be responsive to these trends. Across the entire landscape of the American business community, from energy to retail and consumer to technology, the lead director role is evolving to guide the board and support the company through a complex thicket of issues.

Figure 3. Views on the powers of the Lead Director over the next two years (i.e., increase, decrease, or stay the same)



The CEO and other top officers of public companies need to develop trust relationships with the lead director to facilitate the board’s work in an environment where the board is expected to be more independent of management and more assertive about its stance on policy and major decisions. Like it or not, the lead director position is here to stay and will expand into an even more meaningful role under pressure from stock exchange requirements,⁵ Securities and Exchange Commission disclosure requirements, demands of institutional shareholders, and the board members. For example, management might see the lead director having increased involvement in the strategic direction of the company; mergers and acquisitions; management of risk; crises and difficult situations; succession planning; board composition; development of executive compensation programs; and regulatory matters.

Additional tasks the lead director might take on include more responsibilities in dealing with, and communicating with, large shareholders; governance issues; and board agendas. Directors want better information, better access to management/communications, and better use of third parties (advisors/experts). Management can smooth the path for a board to do its work by providing effective administrative support for the lead director through either the corporate secretary or general counsel’s office.

⁵ See New York Stock Exchange corporate governance standards, Section 303A of the NYSE Listed Company Manual.

The secrets of lead director success

John F. Olson, senior partner, Gibson, Dunn & Crutcher LLP

Having counseled boards of directors and board committees for several decades, I have closely observed the development of the lead or presiding director role at a number of companies. I have seen lead directors perform their responsibilities in good times and bad, through issues ranging from a CEO succession emergency, through accounting and fraud allegations and product liability problems, to the recent changes in corporate strategy to deal with the financial crisis. I have seen lead directors who have made tremendous positive contri-

chairman) who usurps all or part of the CEO's role risks conveying a confusing message as to who is in charge and irreparably damages his own ability to counsel effectively, advise the CEO, and serve as a liaison with the board.

- 2. You and the CEO (and nonexecutive board chairman, if there is one) are on the same team.** Although you are an independent director, with all of the perspective and constructive skepticism that entails, your role is also interdepen-

“I wholeheartedly agree with the ‘Six Secrets,’ particularly **you are not the CEO and you and the CEO (and nonexecutive board chairman, if there is one) are on the same team.** An atmosphere of dialogue and respect between the lead director and the CEO is essential for a successful boardroom culture.”

—Dan Kearney, lead director, MBIA Inc., and member, board of directors, MGIC Investment Corp.

butions to resolving such crises and have observed others who have not performed well. Whether in crisis mode or more normal times, the way a lead director approaches the job determines how successful this approach to board governance will be.

Based on my observations, I offer the following rules of the road to success for lead directors:

- 1. You are not the CEO.** The lead director must remember that he or she is not the CEO of the company, is not the leader of the management team, and is not the company's “public face.” A lead director (or, for that matter, a nonexecutive

dent with the company's CEO and other board leaders. Your formal responsibilities include working with the CEO and management team to assure that the board gets the right information, in sufficient but not overwhelming detail, in time to make soundly based decisions and helping to set an agenda that addresses the key issues and provides time for deliberation. This is a collaborative, not adversarial, task. You can't be effective in this and your other responsibilities if you don't have a relationship of mutual respect and trust with the company's senior management or if you get out in front of the CEO and appear to employees and other constituencies to be “the boss.”

3. You must keep the board focused and the CEO informed. The lead director presides over meetings of nonmanagement and independent directors. This can be, and in many companies is, a valuable oversight tool not only for evaluating CEO performance and discussing succession issues in confidence, but also for surfacing issues of concern to board members and identifying information gaps. But such sessions can be destructive and divisive if they become unplanned “gripe” sessions or if they focus on issues that management is not told about. You, as lead director, must take the responsibility to plan thoughtfully for such meet-

One technique for more effective executive sessions of nonmanagement directors is to schedule some of those meetings at the beginning or midpoint of the board meeting day rather than at the end, when directors are tired and ready to rush to catch airplanes. Lunches or dinners for nonmanagement directors only are fairly common, but the bar should be closed and the wine cellar locked until after the business is done, and afterward, the lead director should be sure that the CEO is appropriately informed of issues raised. I have seen serious mischief done by directors in poorly planned executive sessions fueled with adult beverages.

“The “Six Secrets” represent sound advice for a director taking on the lead director role. Lead director success is all about how one approaches the job. If one views themselves as a proactive enabler for the board, individual directors, the CEO and his/her management, one will be effective and deliver.”

—Nina Henderson, Former lead director, Del Monte Foods Company; member, board of directors, Del Monte Foods Company, AXA Financial Inc. and Pactiv Corporation

ings, consulting with other directors to develop and follow an informal agenda, and to guide the discussion to conclusions as to next steps. Most importantly, the lead director should communicate feedback promptly to the CEO to allow issues raised in the closed session to be addressed without delay. There are occasions—such as when nonmanagement directors are considering a CEO change—when communication to the CEO may be limited or delayed, but these should be rare exceptions.

4. You should be an honest broker, rarely an advocate. You will be most effective if your fellow board members, as well as the CEO and her team, see you as a good listener and wise counselor rather than as an advocate for a particular position or point of view on the board. Ninety-nine percent of the time, your job is to facilitate consensus within the board and be viewed by both board members and the management team as a reliable and unbiased communicator, rather than as advocate for a particular position or point

of view. This requires self-restraint; in leading, you listen as much or more than you speak.

5. You should insist on tenure that enhances your effectiveness. Rotation of the lead or presiding director role from meeting to meeting or even on an annual basis does not result in effective leadership, in my experience. You must have time to work into an effective relationship with the CEO and your fellow directors and to pursue key issues to conclusion. Constant changes of board leadership are a favorite tactic of imperial CEOs. Such frequent changes lead to role confusion and weaken board effectiveness. In my view, a term of at least three years is desirable; five years is quite common. Of course, if you have such a term, your performance should be reviewed by your fellow directors as part of their annual evaluation of board effectiveness, and you should get a report on that review.

6. You have a natural “cabinet” of other board leaders; use them. Your team within the boardroom consists of the chairs of each of the board committees. They have been chosen, hopefully, by your governance committee in consultation with, but not at the direction of, the CEO, as the board members best qualified to lead each committee’s functions. Consult with them regularly; be available to them when they have concerns or agenda item suggestions; be sure they are each getting the corporate staff support and resources they need.

The best lead directors I have known have adhered to these rules of the road. They are men and women with a wide range of experience and backgrounds. Some previously served as CEOs of another company; others come with governmental, academic, or other backgrounds. What these successful lead directors have in common is modesty of personal style; an impartial and organized leadership approach; a collaborative spirit focused on building consensus within the boardroom; and a commitment to honest, prompt, and unbiased communication between the nonmanagement directors and the CEO and senior management.

Thinking about risk management— reflections for lead directors

By Brian G. Cartwright, Alexander F. Cohen, and Andrew S.H. Ting, Latham & Watkins LLP⁶

Risk and risk management are hot topics. How public company boards handle risk is being closely scrutinized. Legislation pending before Congress would go so far as to require public companies to create a separate standing committee of independent directors responsible for risk management.⁷ The SEC recently adopted rules requiring a discussion of the board's role in risk management when a public company seeks proxies for the election of directors.⁸ The press has shown itself eager to find executives and directors to shame in the court of public opinion for faulty risk management. And as for the courts of law, it does not take much imagination to predict cases against executives and directors for faulty risk management.

a topic that has captured the attention of powerful potential antagonists. So, what's to be done, and more specifically, what role should a lead director play in this drama?

The place to start, in our view, is to recognize that the current controversy about risk management is unfolding according to a pattern very familiar by now. Back in the 1980s, for example, a wave of takeovers—especially hostile takeovers—captured the public's attention, and boards' handling of takeover situations began to be closely scrutinized.⁹ Suddenly, when deciding whether to approve a merger, a company found it was no longer good enough just to exercise sound business judgment; you also had to be able to demonstrate to sometimes skeptical audiences that you had done so. How

“Risk management is perhaps the toughest challenge yet. Boards need assurance that risk has been assessed, documented, and tested.”

—Donald T. Nicolaisen, member, board of directors, Morgan Stanley, MGIC Investment Corp., Verizon Communications Inc., and Zurich Financial Services

As a result, seasoned directors now find themselves subject to countless presentations and publications lecturing them on how to manage risk. We can well understand why you might be skeptical about whether all this advice can really be helpful. After all, balancing risk and reward is what doing business is all about, and as a lead director you already have at the heart of your career success a track record of achievement in seeking reward while controlling risk.

In fact, much of the advice being offered strikes us as little more than tedious repetition of bromides and pabulum of the sort Polonius dispenses to Laertes in “Hamlet.” Nonetheless, directors can ill afford to ignore

to do that? By following a process that self-evidently established that you had made the decision with all due care—and ensuring that that process was meticulously documented.

As another example, at the beginning of the last decade, a series of high-profile accounting scandals captured the public's attention, and boards' handling of companies' financial statements began to be closely scrutinized.¹⁰ Suddenly, when approving financial statements, your company found it was no longer good enough just to exercise sound business judgment; once again, you had to be able to demonstrate to sometimes skeptical audiences that you had done so. How to do that?

⁶ Brian Cartwright is a senior advisor, Alexander Cohen is a partner, and Andrew Ting is an associate.

⁷ The “Shareholder Bill of Rights Act of 2009,” S. 1074, 111th Congress § 5 (2009).

⁸ Release No. 34-61175, Final Rule: Proxy Disclosure Enhancements (December 16, 2009).

⁹ As just one example, in the case of *Smith v. van Gorkom*, 488 A. 2d 858 (Del. 1985), directors were held personally liable for money damages for the way in which they had approved the sale of their company.

¹⁰ The Sarbanes-Oxley Act of 2002 exemplifies the scrutiny resulting from accounting scandals at Enron, WorldCom, Tyco, Adelphia and other public companies.

The same way: by following a process that self-evidently established that the financial statements had been developed with all due care—and ensuring that the process was meticulously documented.¹¹

Armed with this history, we see that the answer for lead directors seems straightforward. Take a page from the playbook developed for takeovers and financial statements, and help ensure that the company (and the board) follows a meticulously documented process, one that self-evidently establishes that the company's risk management has been carried out with all due care.

We can already hear the objection that such an approach will simply add costly bureaucracy where it is unneeded and unlikely to add substantive value. That's possible, but unfortunately, additional layers of bureaucracy are an inevitable incremental cost of being a public company. You can't avoid it, so your goal, as always, should be to do what's necessary as efficiently as possible, and maybe even manage to generate some net benefit as well.

How best to go about this? As a lead director, for you it would make little sense to somehow try to micromanage risk. Instead, focus on the goal of ensuring that your company has a process that self-evidently establishes that the company's risk management has been carried out with all due care. Each company needs to tailor its risk management efforts to its own circumstances, so generalities won't be of much help.

The following questions, however, are representative of those you as a lead director could think about:

- Are the company's risk management

¹¹ Of course, legislators and regulators nudged this process along in various ways, such as by requiring management to establish and maintain "an adequate internal control structure and procedures for financial reporting," as well as requiring the company's independent auditors to attest to management's assessment of the effectiveness of internal control. Section 404 of the Sarbanes-Oxley Act of 2002.

efforts—to analogize to the financial statements—both auditable and audited? That is, is there thorough documentation that provides sufficient evidence that reasonable and appropriate steps have been taken, and have senior management and the board properly overseen and monitored these efforts?

- What are the documented plans for risk management, and what are the documented procedures? As appropriate, has the board been engaged in overseeing plans and procedures for continuity of operations or crisis management?
- Do the board minutes reflect that the board paid significant attention to these topics?
- Is the board organized to address risk management issues? Is there a board committee that should be tasked explicitly with risk management? If so, should it be the audit committee, or is that committee already close to being overloaded?
- How about management—does it have the right risk management organization in place? Who's responsible? Is risk management part of the charter of the executive committee, or is there a separate, top-level risk-management committee?
- Are the processes and procedures being followed? A company would never want to find itself in the position of trying to explain why it said it would do X and then failed to follow through.
- Do the relevant lower-level employees know what to do and have the required skill sets?

Asking questions like these (and following up on the answers), not micromanaging risk, is what boards are expected to do. Establishing the right "tone at the top" is a core board responsibility, and in this area, as in so many others, lead directors can help ensure that the company is on the right path.

The survey results

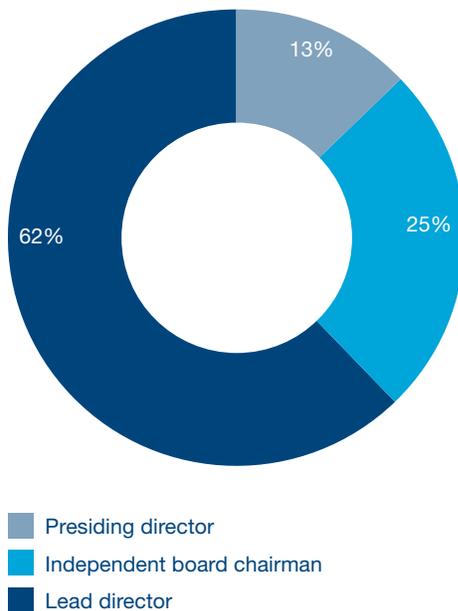
The survey results

Question 1. How long have you been a director of this company?



Veteran directors of the company are the overwhelming choice to be the lead director; 83 percent of the respondents have served for five or more years as a director.

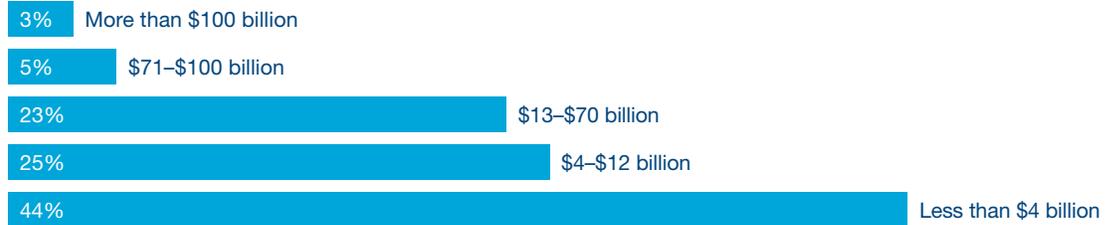
Question 2. Which of the following positions on the board do you currently hold?



For purposes of the survey, a lead director was defined as also including a presiding director (13 percent) or independent board chairman (25 percent). A large majority, 62 percent, are known as lead directors. The term *presiding director* may not adequately describe the level of responsibilities associated with the position because the presiding director does not merely preside; but the term is still in use, albeit on a comparatively smaller scale. Of note is the 25 percent of responders who hold the position of independent board chairman. As the roles and responsibilities continue to be debated, it will be interesting to see if the occurrence of *independent board chairman* increases or decreases in relation to the use of *lead director*. There are questions whether lead directors are considered “the equivalent of board chairmen by the board or shareowners, even when such directors are provided with comparable authorities.”¹²

¹² The Millstein Center for Corporate Governance and Performance, Yale School of Management, “Policy Briefing No. 4—Chairing the Board: The Case for Independent Leadership in Corporate North America,” page 3 (2009).

Question 3. What are the annual revenues of the company?



Question 4. What is the size of the company's board?



The size of a company's board can have a distinct impact on its effectiveness, with too large or too small a board posing its own unique challenges. When a board is too small, it "runs the risk of being insufficiently diverse in the range of backgrounds, experiences, skill sets, and perspectives."¹³ In the inverse, a board that is too large can impact the quality of discussion and hinder individual accountability.¹⁴ Among respondents, boards predominantly have nine to 12 directors, with almost 70 percent falling into this range.

¹³ William G. Bowen, *The Board Book: An Insider's Guide for Directors and Trustees* (New York: W.W. Norton & Company, 2008), page 126-127.

¹⁴ Ibid.

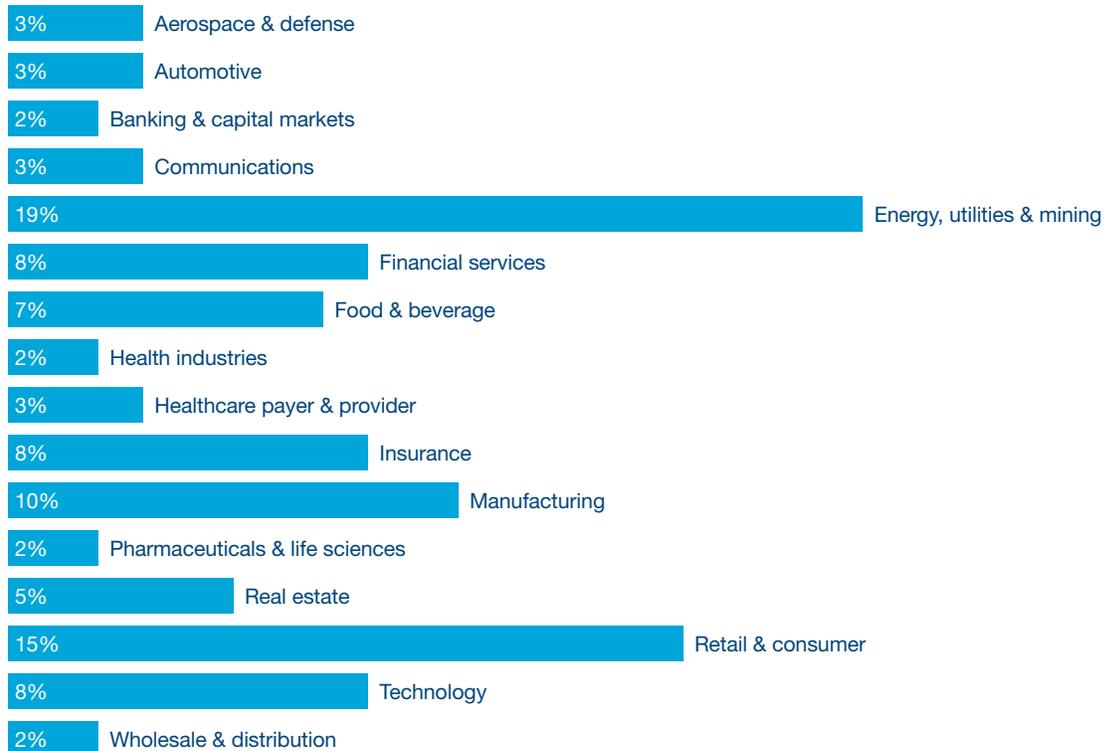
Question 5. In addition to your position, which of the following board leadership positions does your board currently have?



Although there is a great deal of current debate about separating the combined position of chairman and CEO, the survey group includes two-thirds from companies that still have this traditional form of organization. Some companies questioned the benefits of separating these roles and instead chose to adhere to the dictates of the stock exchanges, which call only for an independent director who presides over executive sessions. While conceptually weaker than most had hoped for, the lead director role has grown in both its influence and responsibilities, thereby providing hope that it is a viable alternative to a separate chairman and CEO. However, if in the long run the lead director role fails to deliver, it is likely that calls for separating the chairman/CEO position will continue and grow.¹⁵

¹⁵ For additional commentary, see King & Spalding's article on page 4.

Question 6. What industry best describes the company's type of business?

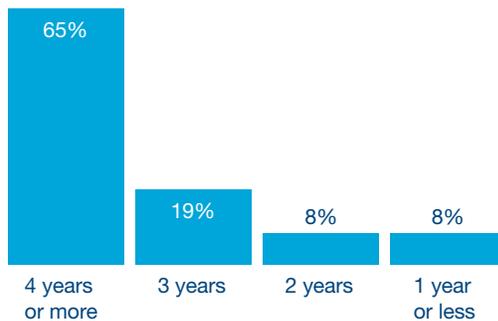


Question 7. At how many other public companies are you a director?



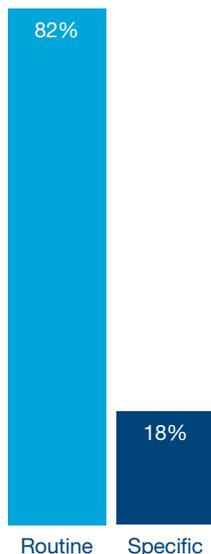
Lead directors are apparently sensitive to serving on too many boards, an oft-made criticism recently, with the majority, 60 percent, serving on only one or two other public company boards. Twenty percent of lead directors are not directors of any other companies.

Question 8. How long has the company had the lead director position?



Many companies created the lead director position in response to the new and enhanced standards imposed in 2002 by the Sarbanes-Oxley Act, including demands for greater transparency, accountability, and integrity. In the wake of the new regulatory and corporate governance environment created by Sarbanes-Oxley, the lead director position was viewed as an important tool in strengthening the checks and balances between the CEO and board functions.

Question 9. Did the company create a lead director position because of some specific event or situation, or was this a routine corporate governance development?



Specific reasons provided by respondents:

- CEO became chairman
- Change of CEO and retirement of former chairman
- Evolved from chair/CEO to chair and president/CEO
- Following an attempt by a shareholder to force his way on the board
- Founder, CEO, and chairman retired
- I retired from management
- Spin-off with a governance stipulation
- I was nonexecutive chairman for 5 years and then moved to lead as we recognized CEO by naming him chairman
- When the company went public

Surprisingly, the majority of survey participants, 82 percent, created the lead director position as a routine corporate governance development and not because of some specific event or situation as often believed.

Question 10. How long have you been lead director of this company?



In most cases, lead directors are likely to be trusted advisors, having intimate familiarity with the major issues the company faces, the CEO’s preferences, and management styles because of the lead director serving on the board three years or more.

Question 11. Is the CEO of the company also the chairman of the board?



Question 12. How were you selected to serve as lead director?

By independent directors	65%
By nominating/governance committee	21%
By chairman	3%
Board	3%
As part of the spin-off requirement	2%
By former owners and management when the company went public	2%
Creditors’ committee	2%
Current CEO and retiring lead director	2%

Question 13. What other committees do you serve on or chair?

Governance/nominating	42%
Compensation	28%
Audit	21%
Executive committee	2%
Finance	2%
Investment	2%
Nuclear/environmental/safety	1%
Public policy	1%
Strategic planning	1%

Question 14. What other positions have you held with this company or another public company?

CFO	23%
General counsel	2%
COO	22%
President	38%
CEO	52%
Chairman	38%
None	28%

Among respondents, more than half currently serving as lead director of the company have previously served as a CEO and more than one-third as chairman. The leadership and executive skills garnered in these roles make for an easy transition to the lead director post and will help better position the lead director as an important advisor to the chairman/CEO.

Question 15. Have you advised companies in this industry in any of the following capacities?

Lawyer	8%
Accountant	7%
Banker	13%
Consultant	15%
CEO mentor	2%
Private equity investor	2%
None	55%

Lead directors generally have significant management experience in the corporate world and bring that experience to the advice they provide. People who are professional advisors, such as lawyers, accountants, bankers, and consultants, are less likely to be lead directors. The majority of respondents, 55 percent, have not advised companies in any of these capacities.

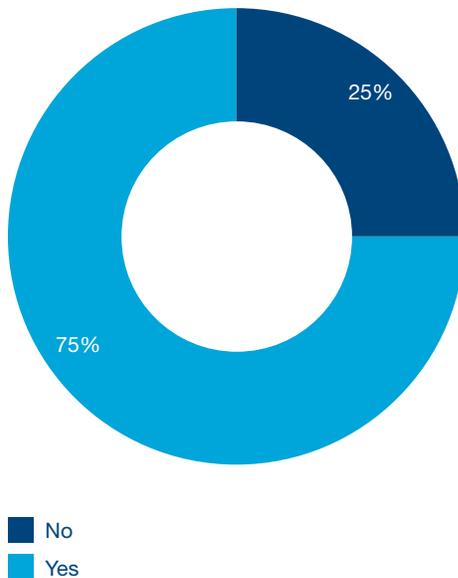
Question 16. How many additional hours per month do you devote to the lead director role on average, beyond the time you spend as a director?



Lead directors are usually spending an additional six to 10 hours on their responsibilities, our survey respondents say. But the typical director spends about 20 hours a month on average on board work, according to another recent PwC survey.¹⁶

¹⁶ PricewaterhouseCoopers, in conjunction with Corporate Board Member Magazine, surveyed 1,021 corporate directors and submitted their results in a 2009 Special Supplement titled “What Directors Think.”

Question 17. Do you receive additional compensation to be lead director?



Companies have no commonality on the level of compensation lead directors should receive. Salaries vary widely from as low as \$5,000 to \$150,000 (only 3 percent of the cases). The most common figure was \$15,000, in 16 percent of the cases.

If so, how much additional compensation?



If not, do you believe that you should receive additional compensation?

Yes	47%
No	53%

Question 18. How long is your term as lead director?



Companies show a distinct divergence in the length of service for lead directors, with 45 percent responding that they have created an indefinite term and 35 percent a one-year term. Clearly, there is no consensus on which is more effective for a lead director, serving indefinitely or with a term limit. However, a shorter term can pose difficulties for a lead director's ability to lead. The lead director may not be able to develop a solid relationship with the CEO/chairman and might have difficulty in bringing important initiatives to conclusion in such a limited time frame. Additionally, the constant "changing of the guard" could lead to board confusion and an overall lack of momentum.¹⁷

¹⁷ For continued discussion on the length of lead director terms, see the Gibson Dunn article on page 16.

Question 19. Who provides administrative support for the lead director?

Corporate secretary	58%
General counsel	75%
Other company lawyer	10%
Separate staff (counsel, accountants, other experts, etc.)	8%

Question 20. Does the company have a written charter, corporate governance guidelines, or another document describing the duties of the lead director?

Yes	90%
No	10%

Question 21. If the company has combined chairman/CEO, how are agendas for board meetings determined?

By chairman/CEO alone	5%
By chairman/CEO with input from lead director	57%
Jointly by chairman/CEO and lead director	17%
By chairman/CEO with input from all directors	19%
By the lead director with input from all other directors	2%

Question 22. Who selects the materials to be sent to directors for each board meeting (board packages)?

Chairman	35%
CEO	45%
Lead director	5%
Chairman and CEO	5%
Chairman, CEO, and lead director	3%
Lead director with input from CFO and other directors	2%
CFO and corporate counsel	3%
Driven by agenda	2%

Question 23. As the lead director, do you have meaningful input into the selection of the materials to be sent to the board?

Yes	90%
No	10%

Question 24. Do you, as lead director, have a significant role in communication of substantive business or governance issues to the following people:



The lead director's most important role is communication about substantive business or governance issues with the CEO or senior management and other board members. The lead director is much less involved in communication issues with institutional investors, the media, and the public. The low survey percentage seen in the area of institutional investors is interesting as the lead director has sometimes been viewed as someone who could improve these relations. Communication with shareholders/investors remains an important initiative of management and may be an area where lead directors can get more involved in the future. However, communication with the media and public will likely not change because the lead director should defer to the CEO/chairman as the principal representative of the company.

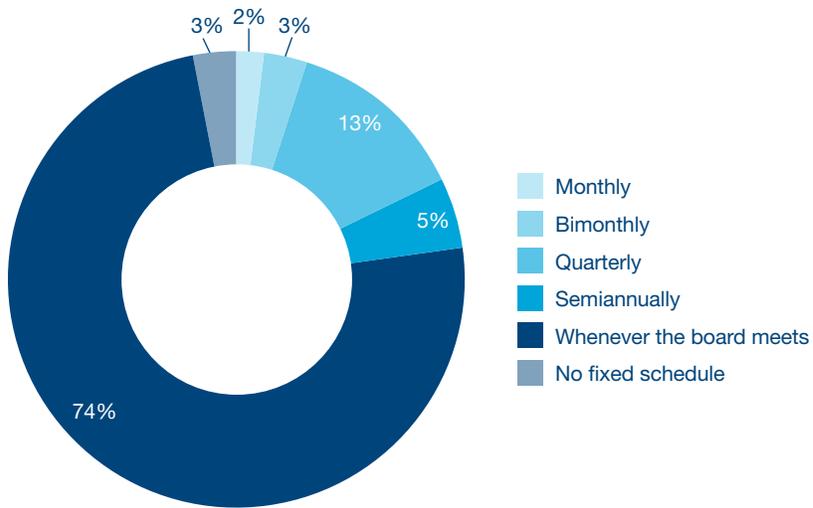
Question 25. Do you have authority to call executive sessions?

Yes	100%
No	0%

Question 26. Do you preside over executive sessions?

Yes	100%
No	0%

Question 27. How often are executive sessions held?



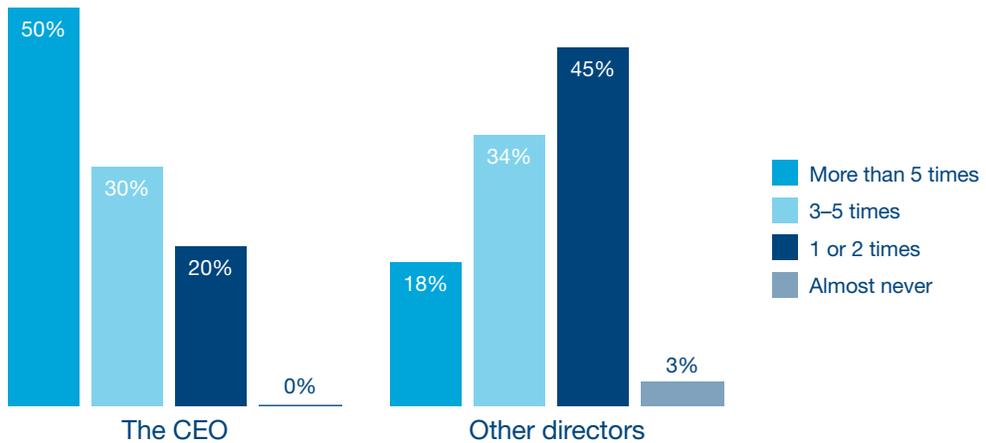
Question 28. Do you prepare the agenda for the executive session?

Yes	93%
No	7%

Question 29. When are executive sessions usually held?

Before board meetings	7%
During a break in board and committee meetings	2%
After board meetings	73%
Before and after board meetings	18%

Question 30. Between board meetings, how frequently do you speak with:



Again, a bit of a surprise, half of the lead directors speak to the CEO more than five times between board meetings, more often than they speak with other directors. Between meetings, other directors mostly hear from the lead director one or two times (45 percent) or three to five times (34 percent). This provides strong evidence that lead directors find it beneficial to develop a strong rapport with the CEO and view their position in relation to the CEO as being collaborative, not adversarial. A continuous flow of information between the CEO and the board, facilitated by the lead director, will create a stronger and more effective board.¹⁸

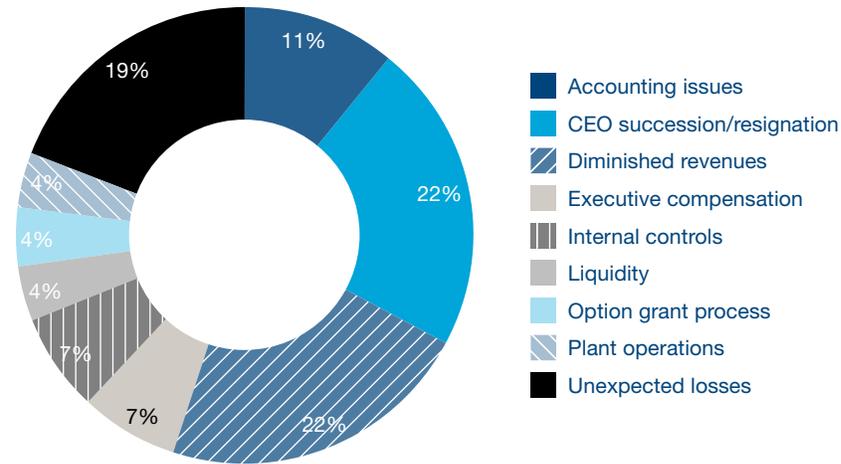
¹⁸ For additional thoughts, refer to the Gibson Dunn article on page 16.

Question 31. Has the company had a “crisis” in the last three calendar years?

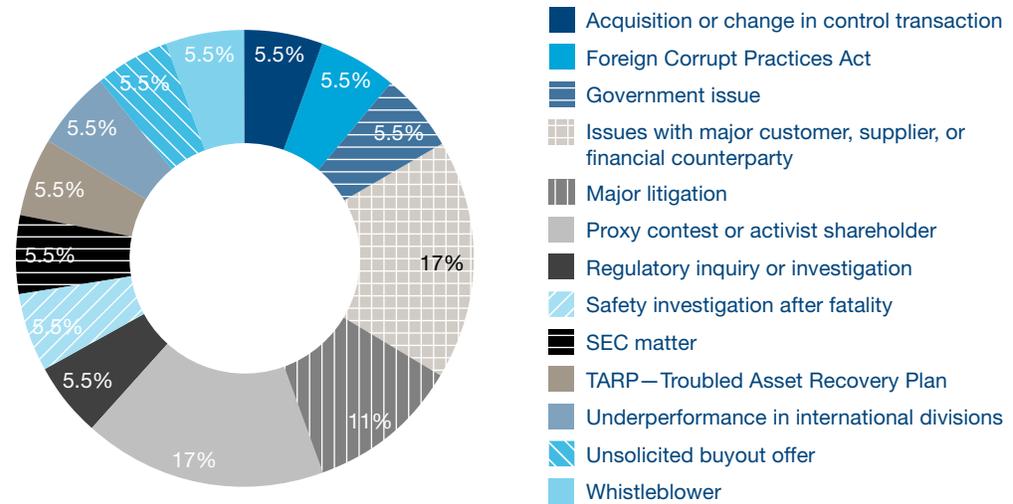
Yes	37%
No	63%

In which internal area(s) and external area(s) has the company had a crisis?

Areas of internal crisis



Areas of external crisis



Question 32. In your experience during a crisis, who selects and retains the primary outside advisors such as law firms, accounting firms, etc.?

Board appoints special committee to make recommendations	15%
CEO or other senior management selects	40%
Entire board selects advisors	30%
Lead director recommends to board	5%
Board is consulted by management and management selects advisors	5%
CEO, CFO, and board	5%

Question 33. As the lead director, if you've had a crisis, did you have an active and substantive role in managing a crisis in the last three calendar years?

Yes	73%
No	27%

Do you believe that the company having a lead director was helpful in resolving the crisis?

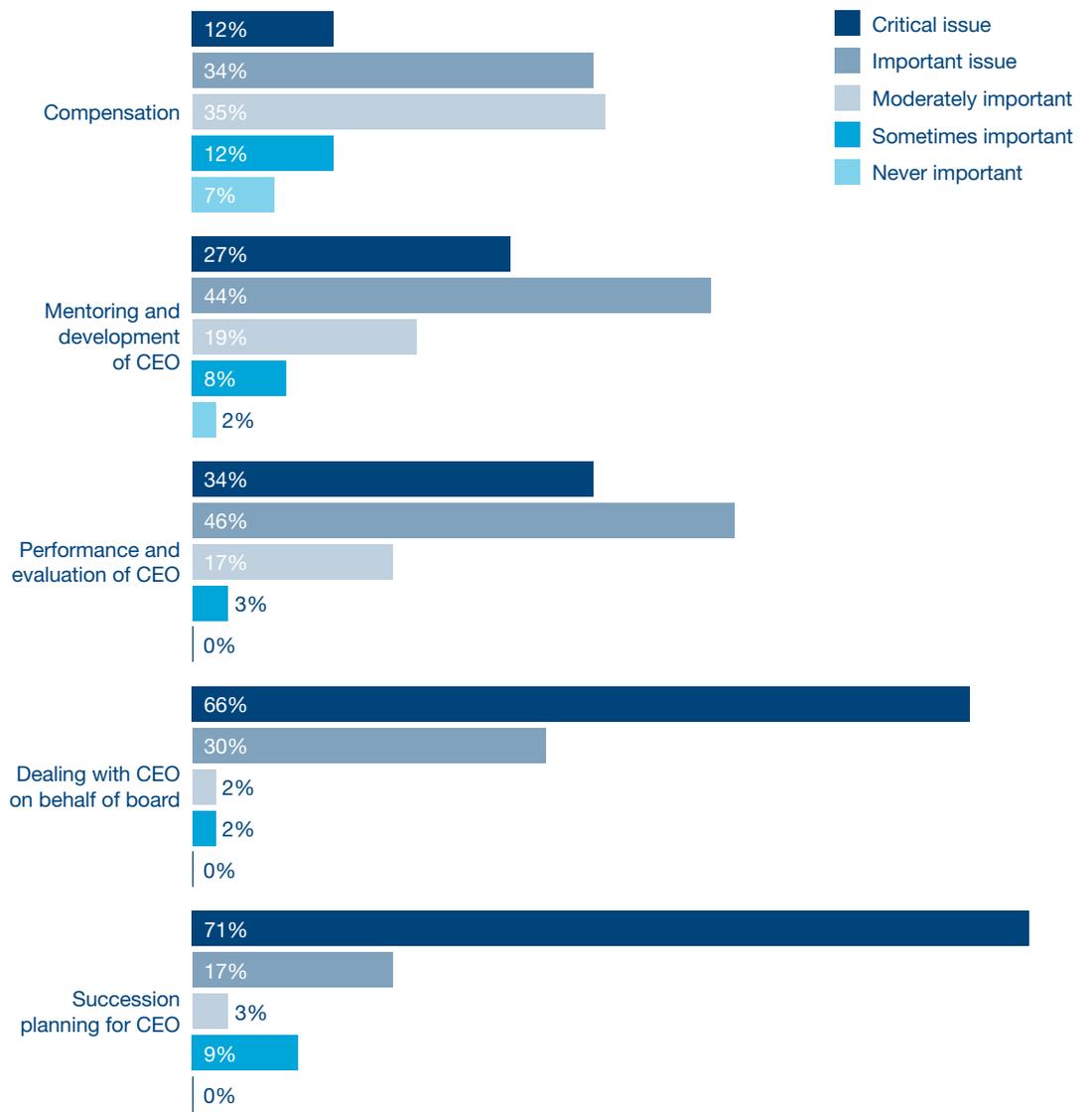
Very helpful	88%
Somewhat helpful	12%

Question 34. Is it important for the lead director to be physically near the CEO and corporate headquarters?

Yes	17%
No	83%

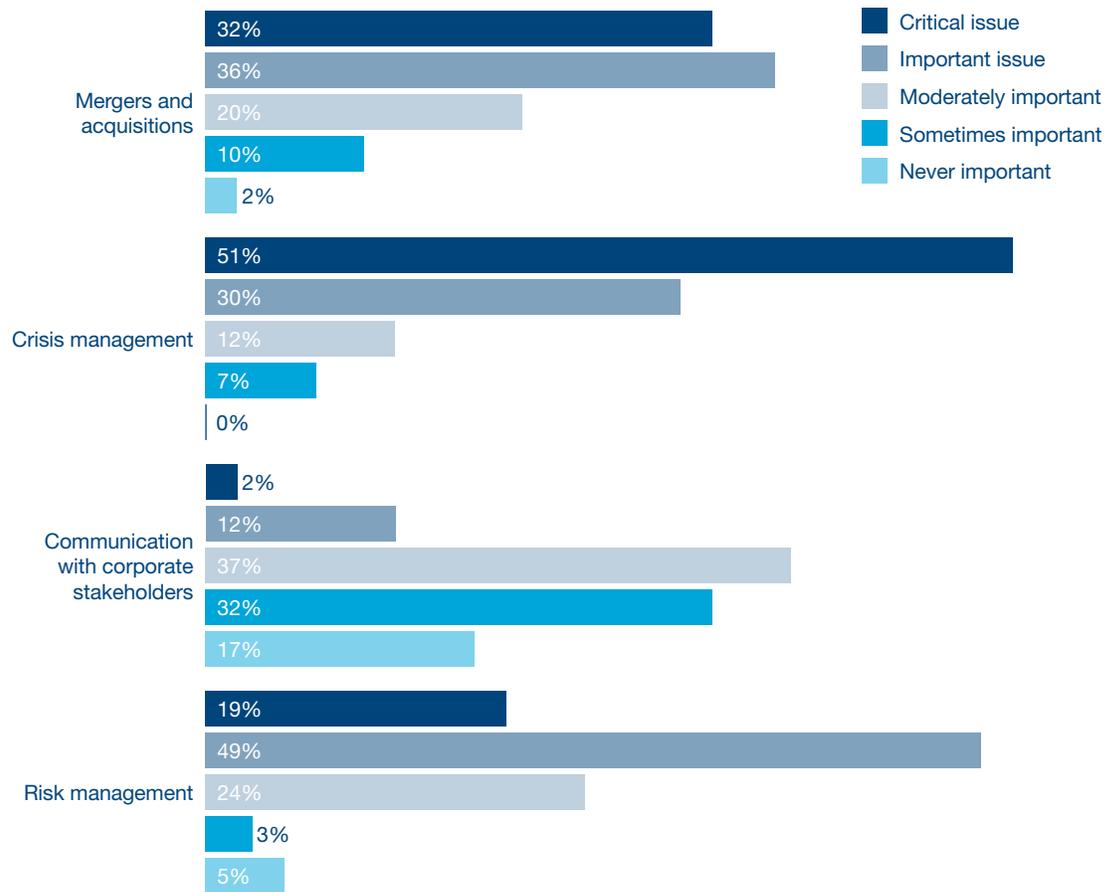
Question 35. For each of the following types of issues, indicate the importance of the lead director in addressing the issue.

CEO issues



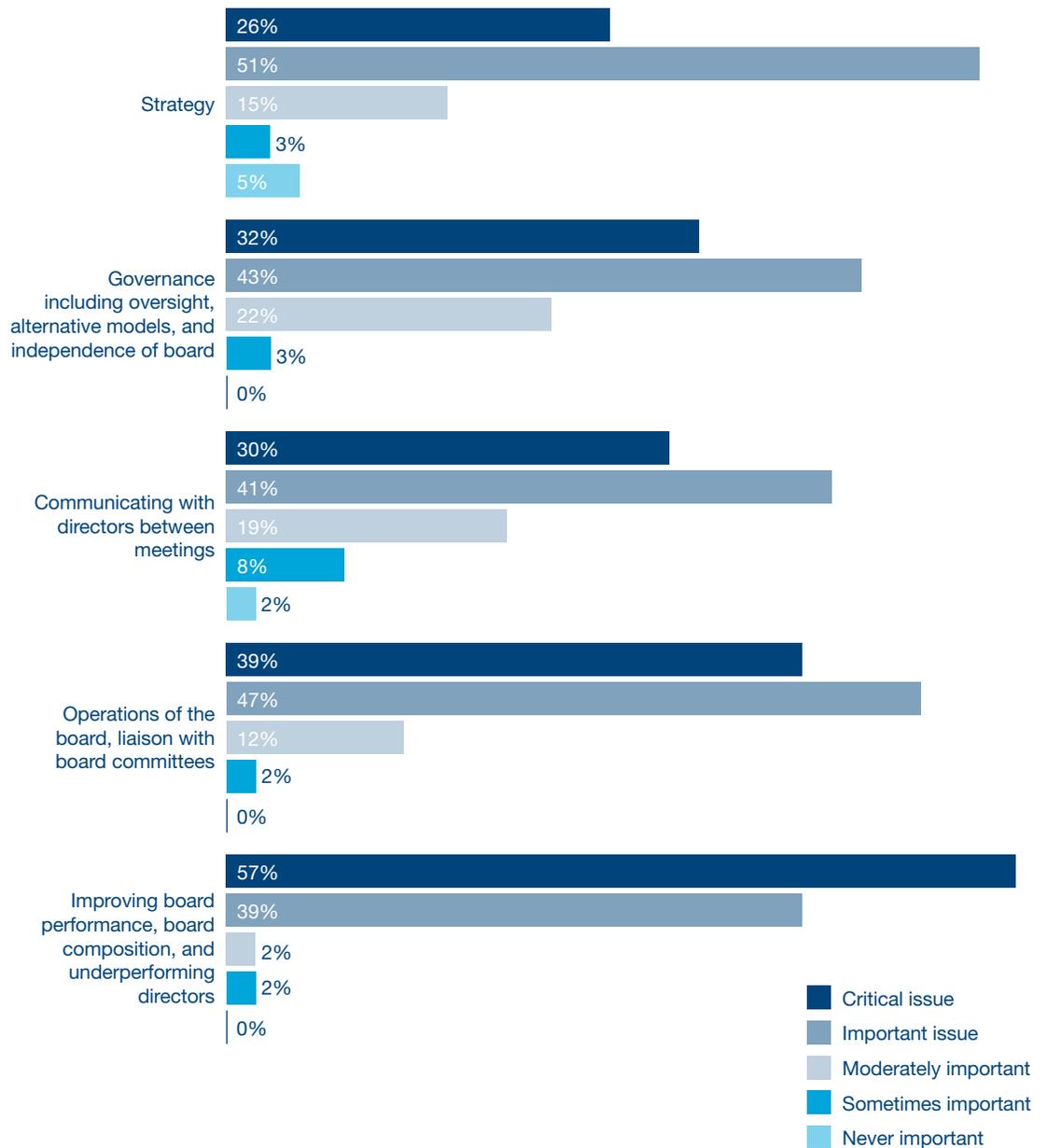
The most critical issue for the lead director when dealing with CEO-related matters is succession planning. Although issues of executive compensation have captured headlines in the business press recently, lead directors surveyed found CEO compensation to be the least important of the five issues listed.

External issues



When dealing with external issues, 51 percent of lead directors say crisis management is the most critical, followed by mergers and acquisitions, named by 32 percent. Lead directors are, however, less concerned with communicating with stakeholders. This follows the trend we saw earlier with the lower level of involvement lead directors have in communicating substantive business or governance issues to investors/stakeholders. Although this type of communication is still seen by many as an important function, some lead directors feel it is best left for others, including management or the CEO/chairman.

Board issues



Companies operate in an increasingly complex world of changing technologies, complicated legal regulations and financial requirements, and tougher standards for director independence.¹⁹ One of the places where the lead director can make a difference is with how the board works. And the survey shows that improving board performance and composition and dealing with underperformers are critical to 57 percent of the survey responders and important at some level to the remainder.

¹⁹ PricewaterhouseCoopers and Board Member Magazine, "What Directors Think 2009," page 13.

Question 36. Should the position of lead director be rotated over time?

Yes	68%
No	32%

How often should the position of lead director be rotated?

1 Year	3%
2 Years	10%
3 Years	20%
4 Years	18%
4.5 Years	3%
5 Years	36%
7 Years	7%
8 Years	3%

Question 38. Have other directors on your board shown any concerns about the creation of a “two-tier board” or the lead director being a “super director”?

Yes	2%
No	98%

Question 39. Do you believe that your serving as lead director of the company has:

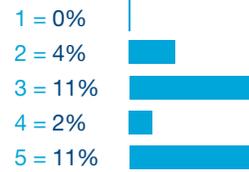
Provided a significant benefit for the company	65%
Been somewhere between significant and limited extremes	35%

Question 40. What do you think the top challenges will be in the next two years as lead director? (1 being most important and 5 being least important)

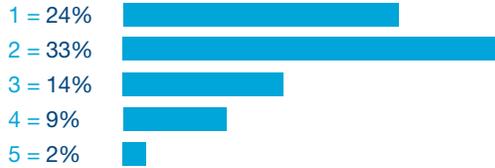
Risk management



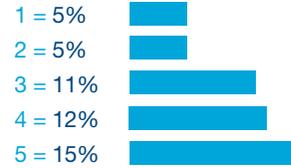
Proxy access or executive compensation



CEO performance



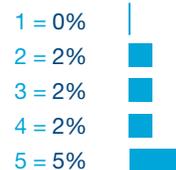
Crisis management



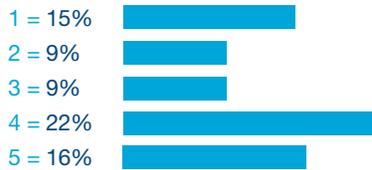
Succession planning



Ethics



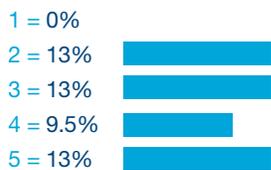
Board composition or effectiveness



New regulatory burdens



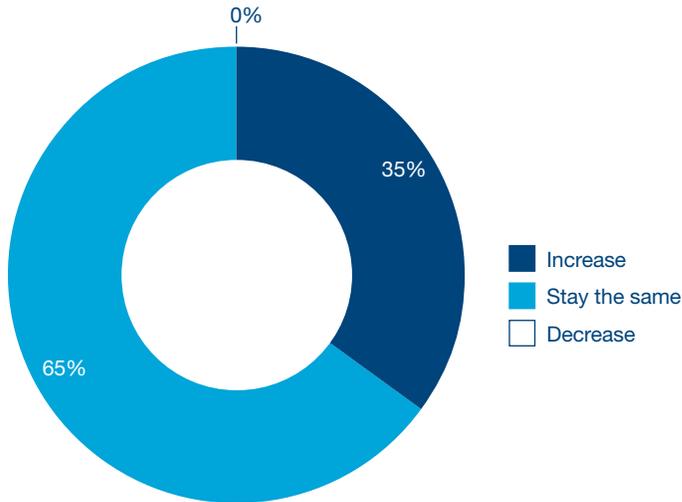
Executive compensation



Over a quarter of lead directors surveyed say that risk management is the most important issue for them to address. This finding is consistent with the views of other board members and directors, who see an overall increase in the risks they face. PwC’s survey on “What Directors Think” showed that 71 percent of directors expect risk of regulatory investigations to rise over the next two years. Likewise, 65 percent expect the risk from plaintiffs’ bar litigation to increase. “Unknown risks” keep 59 percent of them up at night. Sitting in a director’s seat is a greater risk today; 69 percent believe their risk as a director has gone up in the last year.²¹

²¹ PricewaterhouseCoopers and Board Member Magazine, “What Directors Think 2009,” page 4.

Question 41. In the next two years, do you believe the powers of the lead director in the company will increase, decrease, or stay the same?



Question 42. Do you expect any of the following to enhance the role of the lead director in the company?

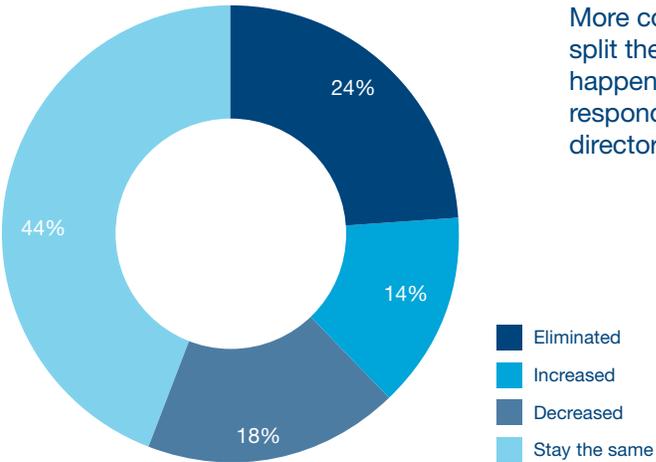
Regulatory or NYSE requirements	38%
Demands of institutional shareholders	27%
Boards choosing to expand the role	20%
None	44%

Lead directors expect to feel the most heat to do more from the regulators, the New York Stock Exchange (NYSE), or from demands of institutional shareholders. However, they do not feel the powers of their position will be altered from where they are now.

Question 43. In your view, will the company split the roles of chairman and CEO in the next five years if it has not already done so?

Yes	29%
No	71%

Question 44. If the chairman and CEO roles are split, will the lead director role be increased, decreased, or stay the same?



More companies are feeling pressure to split the chairman/CEO role. If that should happen, however, the largest number of respondents, 44 percent, feel the lead director position will remain the same.

Methodology

The PricewaterhouseCoopers (PwC) Lead Director Survey 2010 was developed from responses to a proprietary survey in fall 2009 conducted by PwC in collaboration with its consultants, Sandpiper Partners LLC. A database containing more than 400 lead directors at public companies in the United States was created from SEC filings, law firms, and clients. The survey was completed by 60 respondents. Not all respondents answered all questions. Directors were contacted through e-mails, mailings, and telephone solicitations.

The survey asked questions in four broad categories: background information, role and responsibilities of a lead director, views on the lead director concept, and the future. For some questions, respondents could select more than one answer; in these instances, the total percentage for that question will be greater than 100 percent.

An advisory board assisted in the formulation of the questions and format of this report. Its members included:

Kenneth J. Bialkin, partner, Skadden, Arps, Slate, Meagher & Flom LLP

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William Turner, member, public company boards

John W. White, partner, Cravath, Swaine & Moore LLP

For purposes of the survey, a *lead director* was defined as a lead director, presiding director (serving a term of at least one year), or nonexecutive (independent) board chair.

PwC and Sandpiper analyzed the results to prepare the findings based on the data submitted.

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