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WHO SITS ON TEXAS CORPORATE BOARDS? TEXAS CORPORATE DIRECTORS: WHO THEY ARE AND WHAT THEY DO

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TEXAS CORPORATE DIRECTORS: WHO THEY ARE & WHAT THEY DO

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Abstract

Corporate directors play an important role in governing American business, in the capital formation process, and are key to economic growth. Texas businesses play a disproportionately important role among the states in aggregate U.S. job creation, responsible for 37% of all net new American jobs since the recovery began. It is the job of the board of directors to govern the corporation. Director's duties and responsibilities include: the duty of care; duty of loyalty; and duty of good faith. The recently published Trautman's Guide™ to Texas Corporate Directors, provides biographical data for most of the approximately 20,000 for-profit corporate directors serving on the boards of Texas companies. It also provides details about standing committee composition, leadership and membership for audit, compensation, executive, nominating and governance, and strategic planning committees.

Corporate directors are among the most influential and affluent in our society. Many present or former chief executive officers are sought to serve on corporate boards due to their expertise and experience overseeing corporations at the highest level. The average age of Texas directors of for-profit entities is fifty-seven years old; and only about six percent of corporate directors are women. Texas corporate directors are highly educated: over ninety-nine percent are college graduates; eighty percent hold advanced college degrees; twenty-eight percent have law degrees; and twenty percent of Texas corporate directors hold an MBA degree. Most Texas corporate directors serve the banking and finance sector (thirty-nine percent), next largest is the energy sector (at eighteen percent), and technology companies account for nine percent.

Most boards look to recruit someone who understands their business and former CEOs are preferable. Every board of directors of a public company must now have an audit committee comprised of entirely independent directors, and each publicly-traded company is required to have at least one qualified "financial expert" on its audit committee. Therefore, along with a growing recognition that every board needs expertise to govern the enterprises' information technology--- these have become "must have" skills represented on every board.

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I. TEXAS CORPORATE DIRECTORS: WHO THEY ARE & WHAT THEY DO

A recent study of those listed in Trautman's Guide™ to Texas Corporate Directors¹ shows that Texas’ boardrooms tend to be male, and middle-aged. Moreover, they represent society's entrepreneurs and captains of industry, are highly educated and extraordinarily affluent, having an average personal household income of \$327,000 and

¹ Lawrence J. Trautman, Trautman’s Guide™ to Corporate Directors: Texas, (2011) *available at* <http://www.trautmansguide.com>.

an average household net worth approximating \$13.7 million. This data is produced by Public documents and Trautman's Guide™ estimates based primarily on disclosure documents in the public domain and information provided directly by corporate directors.

Corporate directors play an important role in governing American business, in the capital formation process, and are key to economic growth. Therefore, corporate directors as a group are largely responsible for job creation. The recently published Trautman's Guide™ to Texas Corporate Directors provides biographical data for most of the approximately 20,000 for-profit corporate directors serving on the boards of Texas companies. For larger companies, Trautman's Guide™ provides details about standing committee composition, leadership and membership for such standing committees as: audit, compensation, executive, nominating and governance, and strategic planning.

Importance of the Texas Economy

Texas business plays a disproportionately important role among the states in aggregate U.S. job creation. Richard Fisher, president of the Federal Reserve Bank of Dallas has observed that “37% of all net new American jobs since the recovery began were created in Texas.”² Mr. Fisher notes that

Using Bureau of Labor Statistics (BLS) data, Dallas Fed economists looked at state-by-state employment changes since June 2009, when the recession ended. Texas added 265,300 net jobs, out of the 722,200 nationwide, and by far outpaced every other state. Using straight nonfarm payroll employment, Texas accounts for 45% of net U.S. job creation... Professional and business services accounted for 22.9% of the total jobs added, health care for 30.5% and trade and energy for 10.6%.³

² Editorial, *The Lone Star Jobs Surge*, WALL ST. J., June 10, 2011, at A14.

³ Editorial, *The Lone Star Jobs Surge*, WALL ST. J., June 10, 2011, at A14.

What Directors Do

It is the job of the board of directors to govern the corporation. After all, “corporations are created by state-granted charters, their governance dictated by state law, with corporate directors responsible for managing the affairs of the corporation.”⁴ The State of Delaware has granted charters to more than half of all publicly-owned United States corporations.⁵ A number of duties required of corporate directors have been found by the Delaware courts. These have previously been summarized by Lawrence J. Trautman and Kara Altenbaumer-Price as follows:⁶

Business Judgment Rule

Delaware courts have held the Business Judgment Rule “to be a presumption that in making a business decision the directors of a corporation acted on an informed basis, in good faith and in the honest belief that the action taken was in the best interests of the company.”⁷ Under Delaware law, directors owe their corporation and shareholders fiduciary duties of care and loyalty.⁸

Duty of Care

⁴ Lawrence J. Trautman & Kara Altenbaumer-Price, *The Board’s Responsibility for Information Technology Governance*, 28 J. MARSHALL J. COMPUTER & INFO. L., ___ (2011), AT _ citing DEL. CODE ANN. tit. 8, § 141(a) (1991) (“The business and affairs of a corporation organized under this chapter shall be managed by or under the direction of a board of directors, except as may be otherwise provided in this chapter or in its certificate of incorporation.”).

⁵ Trautman & Altenbaumer-Price, *supra* note _ citing Bradley R. Aronstam, *The Interplay of Blasius and Unocal—A Compelling Problem Justifying the Call for Substantial Change*, 81 OR. L. REV. 429-30 n.4 (2002) (discussing why corporations prefer Delaware as their choice for incorporation); Gilson & Kraakman, *Delaware’s Intermediate Standard for Defensive Tactics: Is There Substance to Proportionality Review?*, 44 BUS. LAW. 247, 248 (Feb. 1989) (“Delaware corporate law... governs the largest proportion of the largest business transactions in history”).

⁶ Trautman & Altenbaumer-Price, *supra* note _.

⁷ Trautman & Altenbaumer-Price, *supra* note _ citing *Unitrin, Inc. v. Am. Gen. Corp.*, 651 A.2d 1361, 1373 (Del. 1995) (*quoting* *Aronson v. Lewis*, 473 A.2d 75 (Del. 1992)).

⁸ Trautman & Altenbaumer-Price, *supra* note _ citing *Smith v. Van Gorkom*, 488 A.2d 858 (Del. Super. Ct. 1985).

The duty of care for directors “arises in both the discrete decision-making context and in the oversight and monitoring areas.”⁹ Before the 1985 landmark decision in *Smith v. Van Gorkom*,¹⁰ except when accompanying disloyal acts are present, “courts had rarely found individual directors liable for breaching their duty of care.”¹¹ One explanation of why the experienced and sophisticated directors in *Van Gorkom* were not entitled to business judgment rule protection states:

the duty of care specifies the manner in which directors must discharge their legal responsibilities... includ[ing] electing, evaluating, and compensating corporate officers; reviewing and approving corporate strategy, budgets, and capital expenditures; monitoring internal financial information systems and financial reporting obligations, and complying with legal requirements; making distributions to shareholders; approving transactions not in the ordinary course of business; appointing members to committees and discharging committee assignments, including the important audit, compensation and nominating committees; and initiating changes to the certificate of incorporation and bylaws.¹²

⁹ Trautman & Altenbaumer-Price, *supra* note _ citing Lyman P.Q. Johnson and Mark A. Sides, *Corporate Governance and the Sarbanes-Oxley Act: The Sarbanes-Oxley Act and Fiduciary Duties*, 30 WM. MITCHELL L. REV. 1149, 1197 (2004) (citing *Citron v. Fairchild Camera & Instrument Corp.*, 569 A.2d 53, 66 (Del. 1989)); *Brehm v. Eisner*, 746 A.2d 244, 264 (Del. 2000) (“Due care in the decision making context is process due care only.”).

¹⁰ Trautman & Altenbaumer-Price, *supra* note _ citing *Smith v. Van Gorkom*, 488 A.2d 858 (Del.Supr. 1985). The Delaware Supreme Court found that the experienced and sophisticated directors of Trans Union Corporation were not entitled to the protection of the business judgment rule and had breached their fiduciary duty to their shareholders “(1) by their failure to inform themselves of all information reasonably available to them and relevant to their decision to recommend the Pritzker merger; and (2) by their failure to disclose all material information such as a reasonable shareholder would consider important in deciding whether to approve the Pritzker offer.” *Id.* at 888; see also *See Peter V. Letsou, Cases and Materials on Corporate Mergers and Acquisitions* n21 at 643 (2006) (observing “Trans Union’s five ‘inside’ directors had backgrounds in law and accounting, 116 years of collective employment by the company and 68 years of combined experience on its Board. Trans Union’s five ‘outside’ directors included four chief executives of major corporations and an economist who was a former dean of a major school of business and chancellor of a university. The ‘outside’ directors had 78 years of combined experience as chief executive officers of major corporations and 50 years of cumulative experience of Trans Union. Thus, defendants argue that the Board was eminently qualified to reach an informed judgment on the proposed ‘sale’ of Trans Union notwithstanding their lack of any advance notice on the proposal, the shortness of their deliberation, and their determination not to consult with their investment banker or to obtain a fairness opinion.”).

¹¹ Trautman & Altenbaumer-Price, *supra* note _ citing Jacqueline M. Veneziani, *Note & Comment: Causation and Injury in Corporate Control Transactions: Cede & Co. v. Technicolor, Inc.*, 69 Wash. L. Rev. 1167, 1194 n.3 (1994) (“Before *Van Gorkom* was decided, one commentator had stated that ‘[t]he search for cases in which directors... have been held liable in derivative suits for negligence uncomplicated by selfdealing is a search for a very small number of needles in a very large haystack.’ Joseph W. Bishop, Jr., *Sitting Ducks and Decoy Ducks: New Trends in the Indemnification of Corporate Directors and Officers*, 77 Yale L.J. 1078, 1099 (1968).

¹² Trautman & Altenbaumer-Price, *supra* note _ citing Lyman P.Q. Johnson and Mark A. Sides, *Corporate Governance and the Sarbanes-Oxley Act: The Sarbanes-Oxley Act and Fiduciary Duties*, 30 WM.

Duty of Loyalty

The duty of loyalty in Delaware requires “that there shall be no conflict between duty and self-interest.”¹³ The core concept of the fiduciary “duty of loyalty” has been described as:

[t]he requirement that a director favor the corporation’s interests over her own whenever those interests conflict. As with the duty of care, there is a duty of candor aspect to the duty of loyalty. Thus, whenever a director confronts a situation that involves a conflict between her personal interests and those of the corporation, courts will carefully scrutinize not only whether she has unfairly favored her personal interest in that transaction, but also whether she has been completely candid with the corporation and its shareholders.¹⁴

Conflicts of interest “do not per se result in a breach of the duty of loyalty. Rather, it is the manner in which an interested director handles a conflict and the processes invoked to ensure fairness to the corporation and its stockholders that will determine the propriety of the director’s conduct...”¹⁵

Duty of Good Faith

In order for a director to have the protection of the business judgment rule against a claim for breach of fiduciary duty, a director must be able to demonstrate that she acted in “good faith.”¹⁶ Many factors “define what it means for a corporate director to act in good faith... includ[ing] the judicial application of state corporate law, federal and state legislation, shareholder activism... corporate governance ratings, and the expectations of the public in response to the

MITCHELL L. REV. 1149, 1197 (2004) *citing* *Citron v. Fairchild Camera & Instrument Corp.*, 569 A.2d 53, 66 (Del. 1989); *Brehm v. Eisner*, 746 A.2d 244, 264 (Del. 2000) (“Due care in the decisionmaking context is process due care only.”).

¹³ Trautman & Altenbaumer-Price, *supra* note _ *citing* *Guth v. Loft*, A.2d 503, 510 (Del. 1939).

¹⁴ Trautman & Altenbaumer-Price, *supra* note _ *citing* Charles R.T. O’Kelley and Robert B. Thompson, *CORPORATIONS AND OTHER BUSINESS ASSOCIATIONS: CASES AND MATERIALS* (Aspen, 5th ed. 2006).

¹⁵ Trautman & Altenbaumer-Price, *supra* note _ *citing* Byron Egan, Director Duties: Process and Proof, TexasBarCLE Webcast: Corporate Minutes/ Director Duties (Oct. 23, 2008) (available at www.jw.com/site/jsp/publicationinfo.jsp?id=1044).

¹⁶ Trautman & Altenbaumer-Price, *supra* note _ *citing* Byron Egan, Director Duties: Process and Proof, TexasBarCLE Webcast: Corporate Minutes/ Director Duties, n. 45 (Oct. 23, 2008) (available at www.jw.com/site/jsp/publicationinfo.jsp?id=1044).

media's treatment of current issues in corporate governance.¹⁷ *Stockbridge v. Gemini Air Cargo, Inc.*, holds that the board of directors of a Delaware corporation is charged with the legal responsibility to manage its business for the benefit of the corporation and its shareholders with "due care, good faith, and loyalty."¹⁸

Delaware Chief Justice E. Norman Veasey observes, "Failure to follow the minimum... evolving standards of director conduct... Sarbanes-Oxley... NYSE or NASDAQ Rules ... might likewise raise a good faith issue. There is no definitive answer to that question, but counsel should advise the directors of that possible exposure and encourage the utmost good faith behavior."¹⁹ Moreover,

The evolving business and judicial expectations of director conduct over the years are part of the common law grist for the fiduciary duty mill. As Chancellor Allen stressed in *Caremark*, the kind of sustained inattention of directors exemplified by the failure to institute law compliance programs contemplated by the federal sentencing guidelines and expected of prudent businesses could be held to be a violation of fiduciary duty of good faith. That standard of conduct – good faith – is key to director conduct, and it must be considered when one looks at the directors' processes and motivations to be certain that they are honest and not disingenuous or reckless.²⁰

II. PROFILE OF AFFLUENCE

Corporate directors are among the most influential and affluent in our society.

Many present or former chief executive officers are sought to serve on corporate boards due to their expertise and experience overseeing corporations at the highest level. Our data regarding director affluence may appear skewed toward a high bias because of

¹⁷ Trautman & Altenbaumer-Price, *supra* note _ citing Janet E. Kerr, *Developments in Corporate Governance: The Duty of Good Faith and Its Impact on Director Conduct*, 13 Geo. Mason L. Rev. 1038 (2005-06).

¹⁸ Trautman & Altenbaumer-Price, *supra* note _ citing Janet E. Kerr, *Developments in Corporate Governance: The Duty of Good Faith and Its Impact on Director Conduct*, 13 Geo. Mason L. Rev. 1038, 1045 (2005-06) (*citing Stockbridge v. Gemini Air Cargo, Inc.*, 611 S.E. 2d at 606 (quoting *Malone v. Brincat*, 722 A. 2d 5, 10 (Del. 1998))).

¹⁹ Trautman & Altenbaumer-Price, *supra* note _ citing E. Norman Veasey, *Policy and Legal Overview of Best Corporate Governance Principles*, 56 SMU L. REV. 2135, 2141 (2003).

²⁰ Trautman & Altenbaumer-Price, *supra* note _ citing E. Norman Veasey, *Policy and Legal Overview of Best Corporate Governance Principles*, 56 SMU L. REV. 2135, 2141 (2003).

inclusion of high profile billionaires such as Warren Buffet (BNSF), Michael Dell (DELL Computer), and the wealth represented by the Texas petroleum industry (Boone Pickens and many others).

Personal Household Income:

\$ 327,000 Average
\$ 268,000 Median

Household Net Worth:

\$ 13,722,000 Average
\$ 1,630,000 Median

III. AGE

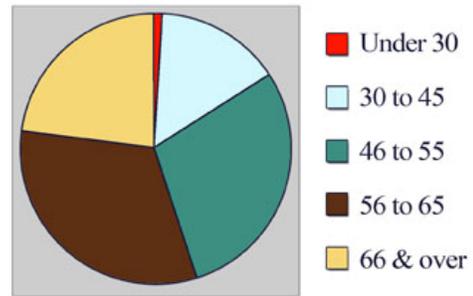
The average age of Texas directors of for-profit entities is fifty-seven years old. Despite the recent publicity surrounding age twenty-something social media entrepreneurs and internet-related start-ups (Google, Facebook, LinkedIn, etc.), less than one-percent of all Texas corporate directors are under the age of thirty. Twenty-two percent of Texas corporate directors fall between the ages of 31 to 45, and twenty-nine percent are between the ages of 46 to 55. The largest age group, at thirty-nine percent, of all Texas directors consists of those between the ages of 56 to 65.

Even with some corporations having mandatory director retirement, fully twenty percent of those serving on Texas corporate boards are 66 years of age or older. A pictorial view of age distribution is presented below:

Age

Under 30:	1%
30 to 45:	15%
46 to 55:	29%
56 to 65:	32%
66 & over:	23%

Average Age = 57 years old

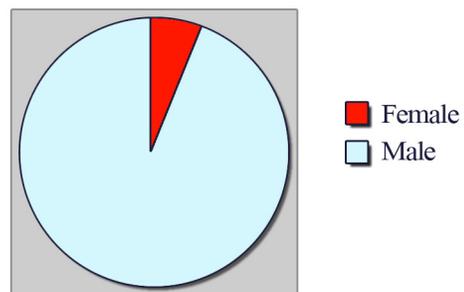


IV. SEX

In Texas, it appears that only about six percent of corporate directors are women; ninety-four percent male. Why is the participation rate so low for women in Texas? Many experienced directors speculate that the historical low levels of participation by women in the engineering and energy (oil and gas) industries may account for these results. During recent years, enrollment by women in professional schools (law and medicine) has grown from very little representation to a majority of those graduating. Accordingly, it seems reasonable to assume that participation by women in Texas board rooms will grow considerably during years to come.

Sex

Male:	94%
Female:	6%



V. EDUCATION

Texas corporate directors are highly educated. Over ninety-nine percent of Texas directors are college graduates. Eighty percent hold advanced college degrees. Twenty-eight percent have law degrees; a surprising result since to me, since many law firms are reluctant to allow their partners to assume director liability by serving on boards. Twenty-six percent of all Texas directors have earned other advanced degrees. Twenty percent of Texas corporate directors hold an MBA degree.

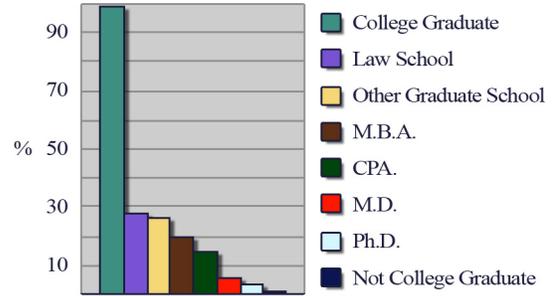
Because the Securities and Exchange Commission and exchange rules require every publicly-traded board to have an audit committee consisting solely of independent directors, with at least one director serving on the audit committee who qualifies as a “financial expert,”²¹ we would expect to see a large number of directors from the accounting and auditing profession. Accordingly, fifteen percent of Texas directors hold a CPA designation. Six percent of directors in this survey are medical doctors, having reported an MD designation. Three percent hold PhD degrees and only one percent of those listed in Trautman’s Guide™ to Texas Corporate Directors were not college graduates, as follows:

²¹ SEC Releases No. 33-8177; 34-47235, Disclosure Required by Sections 406 and 407 of the Sarbanes-Oxley Act of 2002 (January 24, 2003), available at <http://www.sec.gov/rules/final/33-8177.htm>. [Final Rule Release].

Education

99% of Texas Directors are College Graduates
80% Have Advanced Degrees

College Graduate:	99%
Law School:	28%
Other Grad School:	26%
M.B.A.:	20%
CPA.:	15%
M.D.:	6%
Ph.D.:	3%
Not College Graduate:	1%

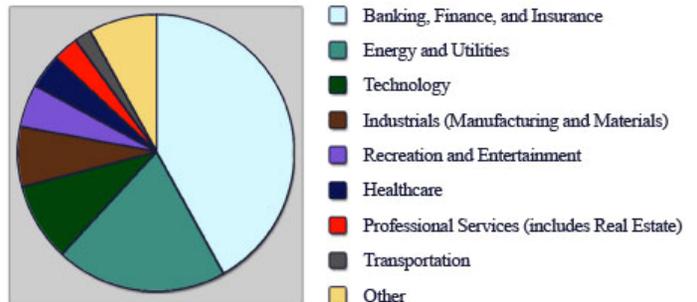


VI. INDUSTRY

Those listed in Trautman's Guide™ to Texas Corporate Directors comprise the nation's corporate elite, representing companies engaged in banking and finance, education, electronics / computer technology, energy, entertainment & recreation, government / public administration, healthcare, insurance, manufacturing, materials, professional services, real estate, telecom, transportation, utilities, venture capital, and other industries. Most Texas corporate directors serve the banking and finance sector (thirty-nine percent). More than four out-of-every 10 directors fall into this category if insurance is included. The second most prevalent category of corporate directors is found in the energy sector (at eighteen percent). Technology companies account for the next largest group of directors at nine percent. Detailed results for Texas corporate directors by industry are as follows:

Total Number of Texas Corporate Entities Represented

Banking and finance	39%
Energy	18%
Electronics/Computer Tech.	9%
Recreation & Entertainment	5%
Healthcare	4%
Manufacturing	4%
Materials	3%
Government/public admin.	2%
Insurance	2%
Professional services	2%
Real Estate	2%
Telecom	2%
Transportation	2%
Utilities	2%
Education	1%
Venture capital	1%
Other industries	2%



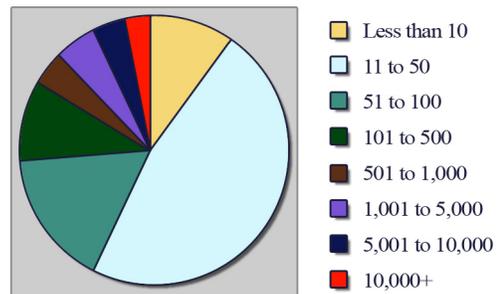
VII. COMPANY SIZE

Most Texas companies for which Trautman's Guide™ was able to compile information have less than fifty employees. Job creation takes place in small companies. Ten percent of companies located by Trautman's Guide™ have less than ten employees.

Forty-seven percent of Texas directors serve on company boards having eleven to fifty employees; seventeen percent of Texas corporate directors govern companies having one-hundred-one to five hundred employees. Of the larger employers, five percent of Texas corporate directors serve on boards of companies employing from one to five-thousand; four percent of directors have five to ten thousand employees and the largest companies, having more than ten thousand employees are governed by three percent of those directors listed in Trautman's Guide™ to Texas Directors.

Number of Employees

Less than 10:	10%
11 to 50:	47%
51 to 100:	17%
101 to 500:	10%
501 to 1,000:	4%
1,001 to 5,000:	5%
5,001 to 10,000:	4%
10,000+	3%



VIII. SALES / REVENUES

As we have already seen, Texas has led the nation in job creation since the recovery began after the 2008 financial crisis.²² Many of these start-up companies are (1) bootstrapped by their entrepreneurial founders, or (2) venture capital sponsored pre-revenue or early stage situations. Start-ups and revenue-challenged enterprises need directors and skilled corporate governance, just as those large-scale businesses. This

²² Editorial, *The Lone Star Jobs Surge*, WALL ST. J., June 10, 2011, at A14.

seems to account for the large number of modest revenue companies found in our universe of Texas corporate directors. It is most probable that our statistics vastly undercount these small companies because many are purposefully in stealth-mode and others simply lack visibility.

By Sales / Revenue

\$1 billion or more:	6%
\$100 to \$999 million:	9%
\$1 to \$99 million:	17%
Less than \$1 million:	68%



IX. PARTICULAR SKILLS IN DEMAND

So what director skills are in highest demand? To get meaningful answers to this question, an attempt was made to survey those considered to be at the top of the director search industry. David C. Anderson, founder of Dallas-based Anderson-Partners, observes “Having served as the Chairman of a Nominating and Corporate Governance Committee and currently serving as a member of a N&CG Committee, I can appreciate the challenges associated with identifying the skills, experience and personal traits appropriate for a new Corporate Director and subsequently identifying and attracting an individual who possesses those traits.”²³ Mr. Anderson continues

²³ E-mail from David C. Anderson, Founder, Anderson Partners. to Lawrence J. Trautman (Jun 29, 2011, 15:27 CST) (on file with author).

I believe a corporation, and shareholders, can be best served by a board that demonstrates a diversity of background, experience, and functional skills. Diversity includes not only gender and ethnicity, but also a diversity of industry and functional experience. It is difficult to generalize which are the most critical skills since the board must first identify requisite critical skills and experience followed by conducting an audit of skills and career experience that currently exist on the board. Any missing skills or experience form the foundation for identifying candidates for the board.

In addition to relevant industry experience and functional skills required for a balanced board, boards need individuals that can provide strategic and visionary guidance to support management while protecting shareholder interests. Other skills in high demand include the ability to establish the "tone at the top", set clear expectations, and monitor company performance/results while focusing on the long term. Other attractive personal traits include the ability to build consensus and provide objective/independent assessments of complicated issues facing the board.

The skills most difficult to identify, and subsequently attract, are often related to personal traits of strategic thinking and guidance, intellectual rigor, and the ability to distill complex issues into workable action plans. All too often board members have difficulty addressing strategic issues without getting into the "weeds" of tactical plans which should be the responsibility of management. In order to confirm that board candidates possess these personal traits, whenever possible references should be contacted who can comment on observed personal traits that are important for the position.²⁴

Houston-based energy search specialist David E. Preng, founder and president of Preng & Associates believes that boards today are doing a very good job of determining what skills are needed to perform their fiduciary duty and the primary characteristics currently desired in director candidates are: "independence, conviction, team player, and financial and business acumen." Most boards look to recruit someone who understands their business and former CEOs are preferable."²⁵ They also look for

²⁴ E-mail from David C. Anderson, Founder, Anderson Partners. to Lawrence J. Trautman (Jun 29, 2011, 15:27 CST) (on file with author).

²⁵ Telephone interview with David E. Preng, Founder & President, Preng & Assoc. (June 29, 2011).

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candidates who have “skills and expertise in *strategy* and *risk management*.” Often boards will require that a new director bring particular expertise such as international experience or accounting skills so that the person can serve on the Audit committee. “It’s much easier to teach someone from your industry corporate governance skills, than to start from scratch and try to teach them your business,” he continues. “Expertise in *compensation* is also valuable, given the considerable increase in the board’s proxy responsibilities--- tying achievement of the articulated strategies to the compensation schematic is an important role for the board,” Mr. Preng observes. With particular reference to the energy business, “if someone presently sits on the board of an exploration & production company, they can’t serve on a competing board due to conflicts of interest. This does tend to create a supply and demand dynamic for my industry,” he continues.²⁶

Robert L. Pearson, Founder and Chief Executive Officer of Dallas-based Pearson Partners International, Inc., says “skills most in demand is a sitting CEO with technology savvy; hard to find is diversity at the C level.”²⁷

“One-third of our board searches are for audit committee financial experts,” says Theodore L. Dysart, Vice Chairman of Chicago-based executive search firm Heidrick & Struggles. “Those who technically qualify are relatively easy to find: every public company CEO; retired major accounting firm senior executives; and most chief financial officers and controllers meet the technical requirements,” he continues.²⁸

The challenge is to find those qualified candidates who will make a great board member; those with industry experience at the proper level

²⁶ Telephone interview with David E. Preng, Founder & President, Preng & Assoc. (June 29, 2011).

²⁷ E-mail from Robert Pearson, , Founder and Chief Executive Officer, Pearson Partners International, Inc. to Lawrence J. Trautman (Jun 30, 2011, 12:42 CST) (on file with author).

²⁸ Telephone interview with Theodore L. Dysart, Vice Chairman, Heidrick & Struggles (July 14, 2011).

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and also bring the right perspective, stature and presence--- and will be able to meaningfully contribute to the future strategy of the enterprise. Following Sarbanes-Oxley, best practice seems to call for the new financial expert director to serve on the audit committee for a year or two in order to provide for orderly succession planning...

I would characterize the next general category of director searches as focusing on those candidates having industry operating experience. Finally, probably one-quarter of our current searches are for diversity candidates.²⁹

Audit Committee “Financial Expert”

Every board of directors of a public company must now have an audit committee comprised of entirely independent directors. In addition, each board is required to have at least one qualified “financial expert” on its audit committee. Therefore, these skills are no longer optional for every board--- they are “must have” skills.

The Board of Directors must determine whether any given director meets the qualification guidelines as an “audit committee financial expert” as such term is defined in Item 407(d)(5)(ii) of Regulation S-K promulgated by the SEC.³⁰ Accordingly, an “audit committee financial expert” is defined as a person who has the following attributes:

(i) an understanding of generally accepted accounting principles and financial statements; (ii) the ability to assess the general application of such principles in connection with the accounting for estimates, accruals and reserves; (iii) experience preparing, auditing, analyzing or evaluating financial statements that present a breadth and level of complexity of accounting issues that are generally comparable to the breadth and complexity of issues that can reasonably be expected to be raised by the registrant’s financial statements, or experience actively supervising one or more persons engaged in such activities; (iv) an understanding of internal

²⁹ Telephone interview with Theodore L. Dysart, Vice Chairman, Heidrick & Struggles (July 14, 2011).

³⁰ SEC Releases No. 33-8177; 34-47235, Disclosure Required by Sections 406 and 407 of the Sarbanes-Oxley Act of 2002 (January 24, 2003), available at <http://www.sec.gov/rules/final/33-8177.htm>. [Final Rule Release].

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controls and procedures for financial reporting; and (v) an understanding of audit committee functions.³¹

How then, Under the Final Rules, Might These Attributes Have Been Acquired?

Under the final rules, the Commission states that “a person must have acquired such attributes through any one or more of the following:

- (1) Education and experience as a principal financial officer, principal accounting officer, controller, public accountant or auditor or experience in one or more positions that involve the performance of similar functions;
- (2) Experience actively supervising a principal financial officer, principal accounting officer, controller, public accountant, auditor or person performing similar functions;
- (3) Experience overseeing or assessing the performance of companies or public accountants with respect to the preparation, auditing or evaluation of financial statements; or
- (4) Other relevant experience.³²

Information Technology

As might be expected, every board needs expertise to govern the enterprises’ information technology. A reasonable question voiced from many boardrooms is “How can I be expected to govern something I know so little about?”³³ However, to be

³¹ SEC Releases No. 33-8177; 34-47235, Disclosure Required by Sections 406 and 407 of the Sarbanes-Oxley Act of 2002 (January 24, 2003), available at <http://www.sec.gov/rules/final/33-8177.htm>. [Final Rule Release].

³² SEC Releases No. 33-8177; 34-47235, Disclosure Required by Sections 406 and 407 of the Sarbanes-Oxley Act of 2002 (January 24, 2003), available at <http://www.sec.gov/rules/final/33-8177.htm>. [Final Rule Release].

³³ Trautman & Altenbaumer-Price, *supra* note _ citing PETER WEILL & JEANNE W. ROSS, IT GOVERNANCE: HOW TOP PERFORMERS MANAGE IT DECISIONS RIGHTS FOR SUPERIOR RESULTS 6 (Harv.

successful, IT governance requires enterprise commitment at the very top. Boards and executive management need to extend governance, already exercised over the enterprise, to IT by way of an effective IT governance framework that addresses strategic alignment, performance measurement, risk management, value delivery, and resource management.³⁴ A recent law review article by Lawrence J. Trautman and Kara Altenbaumer-Price, observed that IT (information technology) “risks are inherent in a company’s operations, including, for example, risks to third parties in operations, such as the inadvertent disclosure of sensitive customer data either by the company itself or third parties; theft of data by cybercriminals; or exposure of your customers to viruses from hackers.”³⁵ Moreover, “IT risks also include direct risks to a company such as the infiltration of viruses in internal systems, business interruption due to security breaches or viruses, the costs of restoring damaged or lost data, or the costs of notifying customers when their data has been compromised.”³⁶

The Trautman and Alterbaumer-Price law review article warns that “These risks are being realized in costly private and regulatory lawsuits related to cyber issues. For example, a payment systems processor was sued in a securities fraud class action after cybercriminals stole credit and debit card information.”³⁷ In another case, a “company was sued after a hacker infiltrated its online job application system and sent phishing e-

Bus. Sch. Press) (2004). Peter Weill, Director of the Center for Information Systems Research ("CISR") and Senior Research Scientist at the Massachusetts Institute of Technology's Sloan School of Management led research during 2001-2003 which studied 256 enterprises in Europe, Asia Pacific and the Americas. During the same general time period parallel studies were conducted by Jeanne Ross and Cynthia Beath (University of Texas).

³⁴ Trautman & Altenbaumer-Price, *supra* note _ at _.

³⁵ Trautman & Altenbaumer-Price, *supra* note _ at _.

³⁶ Trautman & Altenbaumer-Price, *supra* note _ at _.

³⁷ Trautman & Altenbaumer-Price, *supra* note _ at _.

mails to job applicants asking for additional personal information.”³⁸ Elsewhere, “A retailer found itself embroiled in multiple lawsuits and a multi-state regulatory probe after hackers stole millions of credit and debit card numbers over a two-year period³⁹ and an educational institution was sued by its alumni after hackers stole social security numbers.”⁴⁰ Trautman and Altenbaumer-Price conclude that “best practice for many will dictate that an audit committee include IT expertise and be composed of a qualified vice chairman, familiar with the company’s particular audit issues by virtue of experience gained from audit committee service.”⁴¹ Should unexpected developments require it, this strategy will “provide an instant replacement for the committee chair... Therefore, every board should have at least two qualified financial experts populating the audit committee and seek IT expertise and experience in director recruitment... [and assist] ongoing vigilance and recognition of the mission critical nature of Information Technology to the enterprise.”⁴²

X. CONCLUSION

Corporate directors play an important role in governing American business, in the capital formation process, and are key to economic growth. Texas businesses play a disproportionately important role among the states in aggregate U.S. job creation, responsible for 37% of all net new American jobs since the recovery began. It is the job of the board of directors to govern the corporation. Director’s duties and responsibilities

³⁸ Trautman & Altenbaumer-Price, *supra* note _ at _.

³⁹ Trautman & Altenbaumer-Price, *supra* note _ at _ citing Chubb Group of Insurance Companies, *CyberSecurity by Chubb: Insuring Cyber Exposures for Businesses of All Kinds*, <http://www.sgdins.com/downloads/CyberSecurity%20by%20Chubb.pdf> (last visited July 20, 2010).

⁴⁰ Trautman & Altenbaumer-Price, *supra* note _ at _ citing Chubb Group of Insurance Companies, *CyberSecurity by Chubb: Insuring Cyber Exposures for Businesses of All Kinds*, <http://www.sgdins.com/downloads/CyberSecurity%20by%20Chubb.pdf> (last visited July 20, 2010).

⁴¹ Trautman & Altenbaumer-Price, *supra* note _ at _.

⁴² Trautman & Altenbaumer-Price, *supra* note _ at _.

include: the duty of care; duty of loyalty; and duty of good faith. The recently published, Trautman's Guide™ to Texas Corporate Directors provides biographical data for most of the approximately 20,000 for-profit corporate directors serving on the boards of Texas companies, and provides details about standing committee composition, leadership and membership for audit, compensation, executive, nominating and governance, and strategic planning committees.

Corporate directors are among the most influential and affluent in our society. Many present or former chief executive officers are sought to serve on corporate boards due to their expertise and experience overseeing corporations at the highest level. The average age of Texas directors of for-profit entities is fifty-seven years old; and only about six percent of corporate directors are women. Texas corporate directors are highly educated: over ninety-nine percent are college graduates; eighty percent hold advanced college degrees; twenty-eight percent have law degrees; and twenty percent of Texas corporate directors hold an MBA degree. Most Texas corporate directors serve the banking and finance sector (thirty-nine percent), next largest is the energy sector (at eighteen percent), and technology companies account for nine percent.

Most boards look to recruit someone who understands their business and former CEOs are preferable. Every board of directors of a public company must now have an audit committee comprised of entirely independent directors, and each publicly-traded company is required to have at least one qualified "financial expert" on its audit committee. Therefore, along with a growing recognition that every board needs expertise to govern the enterprises' information technology--- these have become "must have" skills represented on every board.

XI. ABOUT THE AUTHOR

LAWRENCE J. TRAUTMAN

LARRY TRAUTMAN serves as Chairman & CEO of social media enterprise Cogent Information Analytics, Inc., has over thirty years experience as a professional corporate director, and is an executive with one of the world's largest financial institutions. Mr. Trautman held numerous corporate directorships in publicly-traded and privately-owned corporations engaged in such diverse industries as dairy processing, financial services, franchising and fast food (Custom Creamery, Orange Julius and Crescott, Inc.-- all NASDAQ), mortgage banking, publishing, software and information technology, oil & gas (Comstock Resources, Inc., NASDAQ), and others. He served as chairman of the committee of independent directors in the sale of Orange Julius, Inc. to International Dairy Queen. As Senior Vice President of the New York-based investment banking firm Donaldson, Lufkin & Jenrette, he had a diverse corporate finance practice, having sole client responsibility for the origination, negotiation and processing of \$Hundreds of Millions of merger and acquisition transactions and public equity offerings for both traded and going-public situations. His other transaction experience includes: venture capital, real estate, public finance, and private debt and equity placement.

Mr. Trautman provided testimony (economic analysis and policy strategy as an investment banker) before hearings of the United States Congress. He taught accounting and finance at several colleges and universities. He is author of many articles on corporate governance, investment banking and corporate finance-related topics for numerous industry trade publications, and newspapers such as *The American Banker*, *The Baltimore Sun* and *The Washington Post*. He is author of *Trautman's Guide to Mortgage Banking and Loan Servicing Portfolio Acquisitions*, and has frequently been quoted in the financial press. Mr. Trautman previously served as Chairman and President of the Dallas Internet Society. For the Mortgage Bankers Association of America, he served as Chairman of the Industry Corporate Planning Subcommittee, as a member of the President's Economic Task Force; and has been a frequent speaker at many conferences.

At the National Association of Corporate Directors ("NACD"), he served as: President of the New York Chapter (several years) and subsequently as Chairman of the Executive Committee; Past-president of the Metropolitan Washington/Baltimore chapter; has contributed numerous articles and monographs published by the NACD; and has appeared as a frequent speaker.

Mr. Trautman earned a BA from The American University (international relations); MBA (finance & investments) from The George Washington University; and J.D. from the Oklahoma City University School of Law. He may be contacted at www.ljtrautman.com.