Description of document:	Two (2) Pension Benefit Guaranty Corporation's (PBGC) memoranda relating to governance, 2008, 2013
Requested date:	07-February-2017
Released date:	03-April-2017
Posted date:	22-May-2017
Source of document:	Disclosure Officer Pension Benefit Guaranty Corporation 1200 K Street, N.W., Suite 11101 Washington, D.C. 20005 Fax: (202) 326-4042 Email: disclosure@pbgc.gov

PBGC
Protecting America's Pensions
Pension Benefit Guaranty Corporation
1200 K Street, N.W., Washington, D.C. 20005-4026

PBGC 2017-000584

April 3, 2017

Re: Request for PBGC Memorandums

I am responding to your request, dated February 7, 2017, to the Disclosure Division of the Pension Benefit Guaranty Corporation (PBGC). You requested the following records:

1. PBGC's Board Structure and Governance, dated September 4, 2008;
2. PBGC Memo, titled Authorizations, Budget and Investments, dated November 10, 2008;
3. PBGC Memo, titled History of PBGC's Governance, dated March 15, 2010;
4. Presidential Document, Federal Registry Vol 78, No.25, dated February 1, 2013;
5. PBGC Memo, titled Corporate Governance Options, dated April 21, 2003; and
6. PBGC Memo, titled Look Ahead (Four Part Series), dated April/May 2006.

Your request was processed in accordance with the Freedom of Information Act (FOIA) and the PBGC's implementing regulation. Pursuant to your request, we conducted a search of agency records and located **111 pages** of records responsive to your request. I have determined the records listed below may be released to you as follows.

Item 1. PBGC's Board Structure and Governance (70 pages, fully released); and
Item 4. Presidential Document, Federal Registry Vol 7.8, No.25 (2 pages, fully released).

We did not locate any records responsive to items 2 and 5 of your request. Unfortunately, it was necessary to withhold 39 pages responsive to Items 3 and 6 in their entirety. Two exemptions of the FOIA were relied upon to withhold this information.

The applicable exemption, 5 U.S.C. §552(b)(4), permits the exemption from disclosure of matters that are "trade secrets and commercial or financial information obtained from a person and privileged or confidential." The records you have requested contain "commercial or financial information" within the meaning of the above-cited statutory language and the Pension Benefit Guaranty Corporation's (PBGC) regulation 29 C.F.R. §4901.21(b)(2) and, therefore, I have determined these records are exempt from disclosure.

The applicable FOIA exemption, 5 U.S.C. § 552(b)(5), protects from disclosure internal documents: inter agency or intra-agency memoranda or letters consisting of judgments, opinions, advice or recommendations that would not be available by law to a party other than an agency in litigation with the Pension Benefit Guaranty Corporation (PBGC) and as such are not required to be disclosed under 5 U.S.C. § 552(b)(5). In addition, draft, pre-decisional, attorney-client, attorney-work product and deliberative documents would also be protected by this exemption. I have determined that these records are exempt from disclosure.

Since this constitutes a partial denial of your records request, I am providing you your administrative appeal rights in the event you wish to avail yourself of this process. The FOIA provides at 5 U.S.C. § 552(a)(6)(A)(i) (2014) amended by FOIA Improvement Act of 2016, Pub. L. No. 114-185, 130 Stat. 538 that if a disclosure request is denied in whole or in part by the Disclosure Officer, the requester may file a written appeal within 90 days from the date of the denial or, if later (in the case of a partial denial), 90 days from the date the requester receives the disclosed material. The PBGC's FOIA regulation provides at 29 C.F.R. § 4901.15 (2015) that the appeal shall state the grounds for appeal and any supporting statements or arguments, and shall be addressed to the General Counsel, Attention: Disclosure Division, Pension Benefit Guaranty Corporation, 1200 K Street, N.W., Washington, D.C. 20005. To expedite processing, the words "FOIA Appeal" should appear on the letter and prominently on the envelope.

In the alternative, you may contact the Disclosure Division's Public Liaison at 202-326-4040 for further assistance and to discuss any aspect of your request. You also have the option to contact the Office of Government Information Services (OGIS) at the National Archives and Records Administration to inquire about the FOIA mediation services they offer. The contact information for OGIS is as follows: Office of Government Information Services, National Archives and Records Administration, 8601 Adelphi Road-OGIS, College Park, Maryland 20740-6001; e-mail at ogis@nara.gov; telephone at 202-741-5770; toll free at 1-877-684-6448; or facsimile at 202-741-5769.

This completes the processing of your request.[1] For any future request for PBGC records, you may submit your request by accessing FOIAonline, our electronic FOIA processing system, at https://foiaonline.regulations.gov, or by email to Disclosure@pbgc.gov.

Sincerely,

D. Camilla Perry
DISCLOSURE OFFICER

Enclosures

[1] The OPEN Government Act precludes an agency from charging search fees to a FOIA requester if the agency does not meet the FOIA's twenty-day time limit. As such, all search fees associated with this request have been waived.

PBGC's Board Structure and Governance

PENSION BENEFIT GUARANTY CORPORATION

September 4, 2008

Contents

1. Executive Summary

The Pension Benefit Guaranty Corporation (PBGC) is a U.S. government corporation that insures employee pensions. It is governed by a Board of Directors composed of the Secretaries of Commerce, Labor, and Treasury.

In July 2007 GAO published a report questioning whether PBGC could receive a sufficient level of oversight from a board of this structure. The GAO report recommended that Congress consider expanding the size of PBGC's board.

In late 2007, the PBGC commissioned this report to provide background information to assist the PBGC board in its review of alternative corporate governance structures and practices. The report describes the governance structure of other U. S. government corporations, large U.S. public pensions and 11 analogous organizations. It also reviews best practices in corporate governance. It then discusses the strengths and weaknesses of several alternatives for the governance structure and practices for PBGC. The intent of this report is to provide PBGC's board with information to inform its corporate governance review. This document does not seek to advocate any particular governance option.

Of the 11 organizations studied in depth, ten have boards, and each board has nine or more members. Many of these organizations have ex-officio board members, who serve on the board by nature of the public office they hold, but ex officio members never make up the majority of the board. In two thirds of the cases, the CEO is a member of the board, and the CEO is the chair of the board about half the time. Board members have terms ranging from one to seven years, although in practice most board members are re-elected and serve for more than five years. In all these organizations, the boards meet at least four times per year. Similarly, all of these organizations have board committees.

In contrast, PBGC has three board members, all of whom are ex-officio. The Director of PBGC is not on the board. Board members serve at the discretion of the President, which in practice has led to terms of two to three years. PBGC's board has historically met infrequently, but under the leadership of the current administration, the PBGC board has usually met twice a year, and senior representatives of the board meet monthly in person or by phone. The PBGC board does not have committees.

Based on analogies with other institutions, this report considers five alternatives for PBGC's governance structure: a larger, fully autonomous board; a larger board with some government members, a larger board with all government members, a small board with all government members, and folding PBGC into a cabinet department. Each of these alternatives has strengths and weaknesses.

A large board could infuse PBGC's governance processes with perspectives and expertise on public policy, business management, investment management, insurance, and pensions. A large board could also well suited to provide continuity of oversight, since it would be less likely for the entire board to turn over at the same time. Finally, a large board could provide substantial oversight, through a greater time total commitment by the board and by allowing board members to specialize into various governance committees. On the other hand, a large board might be more difficult to manage and might require substantial effort to confirm additional board members, and any board members from outside the public sector could have conflicts of interest vis-à-vis their duties on PBGC's board.

Within any board structure, there are several other important design choices, such as whether to include PBGC executives on the board, who should be the chair of the board, the degree to which the board members use dedicated or outside staff, and the degree to which decision-making processes are formalized. There are viable alternatives in each of these areas.

Instead of expanding PBGC's board, PBGC could be folded into a cabinet department, eliminating its board. Folding PBGC into a department would streamline governance by leveraging the governance infrastructure of that single department. On the other hand, this option would limit the amount of external perspectives and expertise that were brought to bear on PBGC governance. This option would also be unprecedented for an organization holding a large and diverse portfolio of assets like PBGC's.

2. Introduction

The Pension Benefit Guaranty Corporation (PBGC) is a wholly owned U.S. government corporation, formed by the Employee Retirement Income Security Act (ERISA) of 1974, to act as a government guarantor of pensions. When a private business fails, PBGC takes over its pension liabilities and ensures that pensioners are paid. Today, PBGC insures the pensions of over 44 million U.S. workers and actively administers the pensions of 631,000 retirees.

PBGC's board of directors is composed of the Secretaries of Commerce, Labor, and Treasury. In July 2007 GAO published a report[1] questioning whether PBGC could receive a sufficient level of oversight from a board of this structure. The GAO report recommended that Congress consider expanding the size of PBGC's board.

PBGC commissioned this report to assist the Board in its review of alternative corporate governance structures and practices. In accordance with the Statement of Work governing this effort, this report does not seek to assess PBGC's governance nor advocate any particular option for PBGC's governance. See Appendix I for the formal Statement of Work.

As part of the effort, interviews were conducted with several dozen members of PBGC's past and current executive team, members of PBGC's board and their current and former staffs, and other key stakeholders. In addition, a wide range of PBGC documents were reviewed, including minutes of all prior PBGC board meetings, PBGC memos addressing governance topics, and PBGC's key governance documents, such as the bylaws of its board. Substantial external evidence was brought to bear, drawn from academia and private-sector research on governance in commercial, nonprofit, and public-sector institutions. The governance of institutions analogous to PBGC was also assessed, focusing especially on 11 in-depth case studies, based on publicly available sources. Appendix II contains further details of the approach.

This document is a synthesis of the findings from the independent review. Chapter 3 describes the governance context of PBGC. Chapter 4 explains how governance functions in 11 organizations that are analogous to PBGC. Chapter 5 lays out best practices in corporate governance, based on evidence from the private sector, detailed case studies on governance, a broad review of government corporations and large public pensions, and expert views. Chapter 6 lays out five high-level options for PBGC's governance structure and assesses their merits relative to best practice and ability to help PBGC meet its mission. Chapter 7 discusses governance questions that stem from the governance structure. Chapter 8 concludes.

3. Governance Context at PBGC

PBGC is growing in size and complexity. In the past few years, its assets and liabilities have grown at more than 20 percent per year. Meanwhile, PBGC's mission is becoming more complex due to industry trends, such as the rise of risk transfer and derivatives. Within this context, PBGC's governance will be crucial.

A. HISTORY AND EVOLUTION OF PBGC

ERISA,[2] which created PBGC, lays out a three-part mission for the organization:

1. Encourage the continuation and maintenance of voluntary private pension plans for the benefit of their participants
2. Provide for the timely and uninterrupted payment of pension benefits to participants and beneficiaries under plans that PBGC assumes
3. Maintain premiums established by the corporation at the lowest level consistent with carrying out its obligations

To carry out this mission, PBGC relies on insurance premiums paid by solvent pension plans, assets assumed from terminated pension plans, and investment returns from PBGC's existing assets. PBGC is not funded by general tax revenues, but it is a wholly owned U.S. government corporation, and there is a broad consensus view that there is an implicit guarantee that taxpayers would fund PBGC if its other sources of revenue proved insufficient to meet its obligations.[3]

The obligations of PBGC have grown substantially. In the previous five years, PBGC's liabilities have grown by 23 percent per year and now stand at $83 billion. Meanwhile, PBGC's assets have grown less quickly, at 21 percent per year, and stand at $68 billion, leading to a $14 billion deficit.

PBGC is likely to grow. PBGC estimates that even without taking over additional pension plans, the number of pension beneficiaries it actively serves will more than double, from 631,000 today to 1.3 million in the coming decades, as insured workers retire.[4] Future plan terminations are inevitable and will lead to additional growth. For example, PBGC's bankruptcy case load was 40 percent larger in 2007 than in 2005. The financial obligations of PBGC will undoubtedly increase in the coming decade.

Changes in the marketplace are also likely to make PBGC's operating context more complex. For example:

- Plan sponsors are undertaking diverse investment strategies, with some plans exhibiting more risky behavior to attenuate the earnings impact of pensions, given the extent of underfunding and new accounting treatments
- Plan sponsors are increasingly using more-sophisticated financial instruments, such as derivatives, and alternative asset classes, such as hedge funds, making it more difficult for PBGC to quantify its risks

All these trends suggest that PBGC will be bigger and more complex in the coming years. Within this context, strong corporate governance will be all the more important for PBGC.

B. CORPORATE GOVERNANCE AT PBGC

ERISA, which established PBGC, laid out its governance structure. Its Board of Directors is composed of the Secretaries of Commerce, Labor, and Treasury, with the Secretary of Labor as the chair of the board. There is also an Advisory Committee, composed of private-sector individuals, that provides non-binding guidance on investment strategies, plan terminations, and other issues.

PBGC's board members have historically relied on their "board representatives" and their staffs to help with oversight of PBGC. The board representatives are themselves Presidentially-appointed officers in their respective departments. The board representatives meet more often than the full PBGC board, so they can work through the various governance issues and provide real-time oversight of PBGC. The board representatives typically use their staffs within the cabinet departments to prepare for PBGC meetings and to work through the issues that will be decided by the PBGC board.

ERISA established PBGC "within" the Department of Labor. There have been long-running debates about the intent of this language, but in practice this has led to varying levels of administrative oversight of PBGC by the Department of Labor. For example, the Department of Labor processes and approves PBGC's budget.

As enacted, ERISA provided that the Secretary of Labor, in his or her capacity as chair of PBGC's board was to be responsible for the "administration" of PBGC, but the legislation did not specifically address day-to-day leadership of and accountability for PBGC. From PBGC's inception, the Secretary of Labor filled this void by appointing an Executive Director of PBGC. Historically, the Executive Director acted as the chief executive of PBGC, playing the leading role in managing day-to-day operations, setting strategy, and guiding the development of policy. The fact that the Secretary of Labor appointed PBGC's Executive Director underscored the authority the Department of Labor had over the administration of PBGC.

In 2006, the Pension Protection Act (PPA) changed the structure of the executive leadership of PBGC. PPA states that PBGC "shall be administered by a Director, who shall be appointed by the President, by and with the advice and consent of the Senate, and who shall act in accordance with the policies established by the board."[5] PPA did not specifically address which authorities and accountabilities resided with PBGC's board versus the Director.

In 2007, GAO published a report[6] questioning whether PBGC received a proper level of oversight within its current governance structure. The report said that PBGC had too few board meetings, there was a weak articulation of governance roles and responsibilities, and there was ambiguity associated with PBGC's degree of separation from the Departments of Commerce, Labor, and Treasury. The GAO report recommended that Congress consider expanding PBGC's Board membership, to improve oversight.

A review of PBGC's governance confirms the accuracy of GAO's factual observations. For example, there were many years in which PBGC's board did not meet at all. On the other hand, governance at PBGC has improved in recent years. For example, the board has met at least once a year for each of the past five years, PBGC's board has recently approved a new set of bylaws that clarify many of the governance roles and responsibilities, and PBGC now has a career-professional Deputy Director who will stay in office across Presidential administrations.

The remainder of this document lays out best practices in corporate governance and their implications for governance options for PBGC.

4. Setting the Stage: 11 Case Studies

Effective corporate governance stems from a variety of elements working in concert. It begins with a clear articulation of the organization's mission and strategy. This is the benchmark against which to assess the efficacy of corporate governance. For example, if a corporation has a business imperative to make sound decisions quickly, then the governance model should support that.

Building from the mission and strategy, there are three areas of governance design: formal structure, roles and responsibilities, and processes and support functions. Figure 1 lays out typical design elements in each of these three areas.

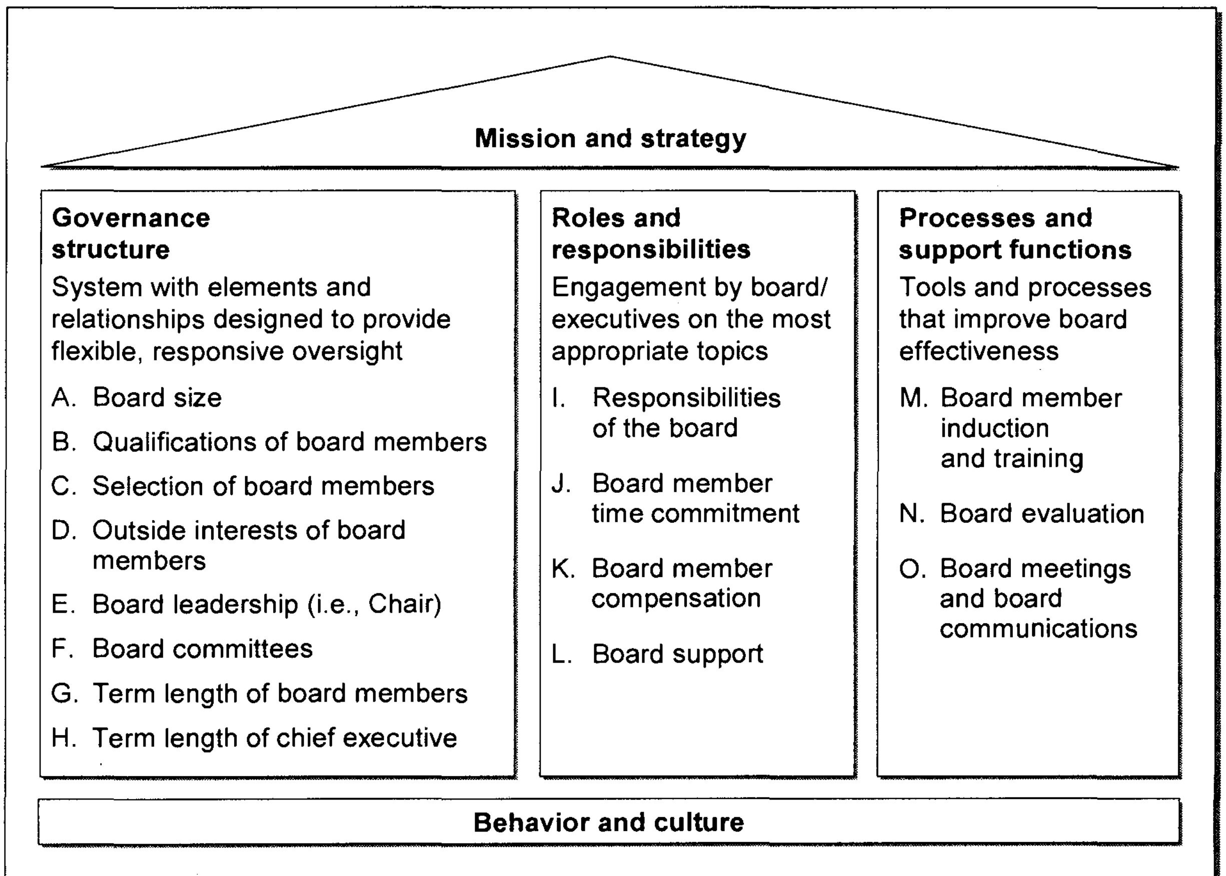


Figure 1: Elements of governance design

		Selection criteria					
		Similarity to PBGC				Attractive performance	
Case example	Country	Government corporations, GSEs	Pension, insurance, finance	Large (>$25B in assets)	Underwent governance transition	High performance	Reputation for good governance
CalPERS	U.S.	✓	✓	✓		✓	
Ontario Teachers' Pension Plan	Canada	✓	✓	✓		✓	✓
Federal Deposit Insurance Corp.	U.S.	✓	✓	✓	✓	✓	✓
Pension Protection Fund	U.K.	✓	✓		✓		
Natl. Railroad Ret. Investment Trust	U.S.	✓	✓	✓			
Overseas Private Investment Corp.	U.S.	✓	✓				
Tennessee Valley Authority	U.S.	✓		✓	✓		
United States Postal Service	U.S.	✓		✓	✓		
Ginnie Mae	U.S.	✓	✓				
Freddie Mac	U.S.	✓	✓	✓			
Procter & Gamble	U.S.			✓		✓	✓

Figure 2: Selection criteria for in-depth case studies

The behavior of employees and the culture of the organization underlie all these design elements. A strong culture of collaborative, fact-based, and open decision-making is often the most-important driver of strong corporate governance. In organizations that lack such a culture, other elements of governance must be strengthened to compensate. For example, in organizations with many executives that are inclined to make decisions on their own, behind the scenes, it is often more important to have a formal committee structure and checks on the power of any one individual.

There is no single ideal model for corporate governance. Rather, each organization must tailor its governance to its own objectives and context. Within that context, the various elements of corporate governance interact with each other and need to be solved jointly. For example, all else equal, the smaller a board is, then the greater the time commitment of each board member should be.

In order to provide an integrated view of corporate governance, this chapter lays out summaries of in-depth case studies of corporate governance at 11 organizations. The detailed case studies are in Appendix III. These organizations were chosen in consultation with the PBGC board and executive team. Organizations were deemed to be more-attractive candidates if they were similar to PBGC or if they had a record of attractive performance. See Figure 2.

Organizations were deemed to be "similar to PBGC" if they were government corporations or GSEs, if they were in a similar industry or served a similar function, if they were large, and if they had undergone a governance transition, as PBGC has done as a result of PPA, with changes to PBGC's bylaws, and with potential changes to PBGC's governance structure in the coming years.

Organizations were deemed to have "attractive performance" if they had objectively good results relative to their missions or if they had a subjective reputation for effective governance. FDIC is an example of the former, since it has effectively prevented major bank failures since the 1990s. Procter & Gamble is an example of the latter, based on citations in the press and general reputation within industry.

The remainder of this chapter briefly characterizes governance at each of these 11 organizations and then summarizes some of the major lessons that can be drawn from the cases as a whole. Appendix III contains more-detailed information on each organization.

A. CALIFORNIA PUBLIC EMPLOYEES RETIREMENT SYSTEM

The California Public Employees Retirement System (CalPERS) is the largest pension fund in the U.S., managing defined-benefit pensions and health benefits for approximately 1.5 million state, county, and local public employees and retirees in California.

CalPERS is governed by a Board of Administration that is composed of 13 members. Six members are elected by all active and retired public employee pension members through a mail-in ballot, three members are appointed by public officials of the state of California, and four members serve in an "ex-officio" capacity. These ex-officio members are on the CalPERS board automatically, by nature of the public offices they hold. For example, the California State Treasurer is on the CalPERS board. The board has five committees that oversee particular subject areas, such as investment policy, and make recommendations to the broader board.

The CalPERS board is responsible for asset management and plan administration, including the setting of employer contribution rates, determining investment strategy, and approving actuarial assumptions. In the past, investment decisions were influenced by political considerations and shareholder activism. To counteract these influences, CalPERS (a) strengthened the role of the Chief Investment Officer, (b) created greater transparency around investment decision-making, (c) increased the use of fund-of-fund managers, and (d) set higher investment targets that left little room for non-financial objectives. The CalPERS CEO has responsibility for operational management and execution of board decisions. Professionals in the Investments Office are responsible for implementing the overall investment strategy and making tactical investment decisions.

Historically CalPERS struggled to attract and retain top talent due to its restrictive government pay scale, but recently CalPERS gained a legislative exemption to allow it to pay more to attract talented investment professionals.

B. ONTARIO TEACHERS' PENSION PLAN

The Ontario Teachers' Pension Plan (OTPP) is an independent Canadian corporation created by the Teachers' Pension Act of 1990. OTPP is governed by a Board of nine members who have the "fiduciary duty to administer the plan and manage the investment fund in the best interests of present and future plan members and their survivors."[7] These members currently include 271,000 current and retired Ontario teachers.

The Ontario government and the Ontario Teachers' Federation each appoint four members to OTPP's board, and they jointly appoint the board's chair. The board is composed of individuals with a high concentration of commercial experience and skills. For example, eight of the nine current members possess significant expertise in investments, business, or accounting. Board members are all independent: They may not be executives of OTPP or employed by the Ontario government. OTPP has a detailed seven-page Code of Business Conduct that outlines the responsibilities of board members and explains how they are to manage potential conflicts of interest.[8]

New OTPP board members participate in an orientation program that includes formal education on financial topics, such as actuarial valuation of liabilities and the use of derivatives. The board's Governance Committee reviews the performance of the board through self-evaluation surveys and written questionnaires completed by board members.

C. FEDERAL DEPOSIT INSURANCE CORPORATION

The Federal Deposit Insurance Corporation (FDIC) is a U.S. government corporation that insures deposits in banks and thrifts and is the primary regulator of state-charted banks.

The FDIC is governed by a Board of Directors that is composed of five members. The board's chair and two other board members serve at FDIC full time. The remaining two members of the board are the Comptroller of the Currency and Director of the Office of Thrift Supervision. Notably, these two ex-officio members of the board are not cabinet-level executives. All five board members are appointed by the President of the United States and approved by the Senate. A maximum of three members may be of the same political party, and at least one member must have experience as a bank regulator at the state level.

The board's chair also acts as FDIC's chief executive. The two other full-time board members typically lead or spearhead key initiatives within FDIC, thus acting in an executive capacity. These three board members have a dedicated staff of six FDIC employees. The Chief Operating Officer is the highest-ranking career executive at FDIC. He or she reports to the chair and provides management continuity that spans political administrations.

FDIC is able to attract and retain talent, for its board and in its senior executive ranks, by offering compensation that exceeds the government General Schedule (GS) pay scale.

D. PENSION PROTECTION FUND

The Pension Protection Fund (PPF) in the United Kingdom is an independent government corporation created by the Pensions Act of 2004. Like the PBGC in the U.S., PPF guarantees private defined-benefit pension plans in the U.K.

The PPF is governed by a board of 11 members, composed of a chair, seven independent non-executive members, the Chief Executive Officer and two additional PPF executives. The Secretary of State for Work and Pensions selects the chair, who then selects the rest of the board members with the assistance of professional recruiters, in an open and publicly-advertised recruiting process. Consistent with the PPF's stated goal of being a high performing and well-managed independent corporation, the PPF board is composed of individuals with relevant private-sector expertise. Nine of the eleven current board members have experience in asset management, pension management, and law. PPF's non-executive board members receive annual compensation of £15,300 and are expected to work on PPF issues 20 days per year.

The board has a broad mandate to administer and oversee the payment of pension compensation, calculate annual levies on pension plans, and develop PPF's investment strategy. The board chose "to make extensive delegation of its functions" to the chief executive and to board committees. These delegations are explained in detail in PPF's 12-page Statement of Operating Principles and Scheme of Delegations.

E. NATIONAL RAILROAD RETIREMENT INVESTMENT TRUST

The National Railroad Retirement Investment Trust (NRRIT) is an independent U.S. government entity formed in 2001 to manage the retirement assets of U.S. railroad workers. By year-end 2006, those assets were $29 billion. A separate U.S. agency, the Railroad Retirement Board (RRB) determines who is eligible for benefits and the levels of those benefit payments.

The NNRIT has a board of trustees composed of seven members. Three of these members are appointed by major labor unions, and three are appointed by major railroad companies. These six members then choose a seventh, who is typically an executive with substantial experience in pensions. These seven members are not U.S. government employees, since NNRIT is fully independent of the government. Board members serve for staggered three-year terms.

Members of the Board of Trustees shall be appointed only from among persons who have experience and expertise in the management of financial investments and pension plans. No member of the Railroad Retirement Board shall be eligible to be a member of the Board of Trustees.

The legislation that established the NNRIT was explicit about the duties of the board members: "The Trust and each member of the Board of Trustees shall discharge their duties (including the voting of proxies) with respect to the assets of the Trust solely in the interest of the Railroad Retirement Board and through it, the participants and beneficiaries of the programs funded under this Act."[9]

The board has an Audit Committee and an Administrative Committee. The Audit Committee meets four times per year, to cover perennial issues like reviewing the financial position of the trust and performing one-off investigations, like an taking an inventory of risks faced by the NNRIT.

F. OVERSEAS PRIVATE INVESTMENT CORPORATION

The Overseas Private Investment Corporation (OPIC) is a U.S. government corporation that supports international business investment and economic development through loans, loan guarantees, insurance against political risk, and equity investments, particularly in emerging markets that do not have well-established financial institutions.

OPIC is governed by a board composed of 15 members, each appointed by the President of the United States and approved by the Senate. The chair of the board also serves as OPIC's President and CEO. Seven board members serve in an ex-officio capacity, by nature of offices they hold in the U.S. government.[10] The remaining eight board members are from the private sector and may not be OPIC executives or government employees. Two of these private-sector board members must have experience in small business, one must represent organized labor, and one must have experience in cooperatives.

OPIC's board is responsible for providing policy guidance to the organization. The board approves all major insurance, project financing, and investment projects.

G. TENNESSEE VALLEY AUTHORITY

The Tennessee Valley Authority (TVA) is a U.S. government corporation and the nation's largest public power company, supplying power to about 8.7 million residents of the Tennessee Valley region.

TVA's board is composed of nine members, each appointed by the President of the United States and approved by the Senate. Each board member is required to have management experience within a large private sector corporation, non-profit institution, governmental body, or academic institution. Five of TVA's current members have backgrounds in business, finance, or energy. The board elects the chair from among the appointed members. The board also appoints TVA's President and Chief Executive Officer. Board members are compensated $45,000 per year. The chair receives $50,000 per year.

TVA's board is responsible for the organization's strategy and policies, annual budget approval, and independent oversight. The board has delegated operational management and strategic implementation to executive management.

Many of the current governance processes at TVA are a result of recent reforms that were mandated by the Consolidated Appropriations Act of 2005. Governance changes included (a) expansion of board from three to nine members, (b) separation of the roles of board chair and CEO, (c) the addition of professional qualifications requirements for board members, and (d) the removal of the statutory government pay scale for TVA executives and employees, to allow TVA to attract and retain sufficient talent.

H. UNITED STATES POSTAL SERVICE

The United States Postal Service (USPS) is a U.S. government corporation that delivers more than 213 billion pieces of mail every year, to more than 300 million people in 146 million homes throughout the United States and territories.

USPS's Board of Governors is composed of 11 members, nine of whom may not be USPS or government employees. Each of these nine board members is appointed by the President of the United States and approved by the Senate. These board members then select the Postmaster General, who also serves on the board and as the Chief Executive Officer of USPS. These ten board members then select the Deputy Postmaster General, who also serves on the board and as the Chief Operating Officer of USPS.

Statutory requirements mandate that not more than five of the nine external board members may be affiliated with any one political party. The Postal Accountability and Enhancement Act of 2006 added professional qualification requirements to the board selection process, stating that board members must be selected solely on the basis of their experience in public service, law, accounting, or management in a large private or public corporations. At least four of the board members must have management experience in corporations with greater than 50,000 employees. Each board member receives compensation of $30,000 per year, plus $300 per day spent on USPS issues.

The USPS board is responsible for directing and controlling the budget, monitoring operations, conducting long-term strategic planning, setting policy, overseeing capital projects, and approving executive compensation. The board is supported by one employee, a full-time assistant.

I. GOVERNMENT NATIONAL MORTGAGE ASSOCIATION

The Government National Mortgage Association (GNMA, or "Ginnie Mae") is a U.S. government corporation within the Department of Housing and Urban Development. Ginnie Mae guarantees investments in mortgage-backed securities (MBS) backed by federally insured or guaranteed loans. In 2007 Ginnie Mae had $4.4 billion in assets held at the U.S. Treasury and $13 billion in total assets, so it was a large institution but much smaller than PBGC.

The Secretary of Housing and Urban Development (HUD) is solely responsible for oversight of Ginnie Mae, which has no board. The President of Ginnie Mae is appointed by the President of the United States and approved by the Senate. The HUD Secretary selects the rest of the executive team, including Senior Vice Presidents of Management Operations, Finance, Mortgage Backed Securities, and Capital Markets.

A 2007 external audit found that Ginnie Mae had significant deficiencies in its (a) processes for monitoring MBS issuers, (b) risk management, and (c) independent management control processes.

J. FEDERAL HOME LOAN MORTGAGE CORPORATION

Federal Home Loan Mortgage Corporation (Freddie Mac) is a government-sponsored enterprise (GSE) and stockholder-owned corporation that provides stability in the secondary mortgage market by guaranteeing residential and multi-family mortgages and investing in mortgages and mortgage-backed securities.

Freddie Mac's board is composed of up to 18 members. Shareholders elect 13 of these members through a nomination and election process. The board's Governance, Nominating, and Risk Oversight Committee oversees this nomination process. Shareholders subsequently vote to elect nominees. The President of the United States may appoint an additional five members to the board, but the current President has elected not to do so. Current board members have a high level of relevant experience across a number of fields including finance, law, accounting, and economics. All board members receive compensation of $60,000 per year, as well as per meeting fees and equity compensation.

The board selects the CEO, who has historically also served as the chair of the board, but Freddie Mac has committed to separating the roles of board chair and CEO in the near future. In order to counterbalance role of the board chair and CEO, the board also elects a lead outside director.

On an annual basis, Freddie Mac's board conducts a review of current members' independence against an eight-point standard. For example, the board assesses potential conflicts of interest that may arise from board member affiliations with charities, consultancies, and companies that do business with Freddie Mac.[11]

K. PROCTER & GAMBLE

Procter & Gamble (P&G) is a Fortune 100 multinational public corporation that produces a wide variety of consumer goods, from soap to disposable diapers. It is renowned for its strong corporate governance.

P&G's is governed by a board that is composed of 10-15 members. The majority of board members must be independent, i.e., not company executives and without a material relationship to the P&G. The independent board members elect a board chair. If the chair is the Chief Executive Officer, corporate bylaws require an independent board member to serve as the Presiding Director, to lead executive sessions and oversee the assessment of executive performance.

P&G's policy is to seek board members who are well equipped to judge strategic and policy questions, who have management experience in large organizations, who are able to commit ample time to P&G's board, and who do not have conflicts of interest, such as being employees of P&G's competitors, customers, contractors, or consultants. Board members must recuse themselves from discussions and votes that may affect their personal or business interests.

P&G's board is responsible for guiding P&G's strategy, monitoring and managing risks, selecting, evaluating, and determining compensation for the management team, and succession planning. In order to empower board members to carry out these responsibilities effectively, all board members receive a formal orientation and ongoing education.

P&G's board meets seven times a year. Board members are expected to attend all board meetings. If any board member's attendance drops below 75 percent, the board chair and Governance and Public Responsibility Committee initiate a review of that board member's conduct.

L. LESSONS LEARNED FROM IN-DEPTH CASE STUDIES

Figure 3 summarizes some of the major findings from the in-depth case studies. Ginnie Mae doesn't have a board. All the other organizations have sizable boards, with all but one having a board of nine or more members. Many organizations have ex-officio board members, but ex officio members never make up the majority of the board. In two thirds of the cases, the CEO is a member of the board, and the CEO is the chair of the board about half the time. Board members have terms ranging from one to seven years, although in practice most board members are re-elected and serve for more than five years. Boards tend to meet often; in all the case studies, the boards meet at least four times per year. Similarly all these organizations have board committees.

It is instructive to compare PBGC's structure with these examples. PBGC has only three board members, all of whom are ex-officio, who serve on PBGC's board by nature of the public office they hold. The head of PBGC is not on the board at all. Board members serve at the discretion of the President of the United States, which in practice has led to terms of two to three years. PBGC's board has historically met only rarely, and even under the active leadership of the current administration meets no more than twice per year, although senior representatives of the board meet monthly, either in person or by phone. Finally, PBGC's board is too small to have board committees.

Case example	Number of board members	Number of ex-officio members	CEO role on board	Term length for board members	Number of board meetings per year	Number of standing Committees
CalPERS	13	4	• No role	• 4 years	12+	5
Ontario Teachers' Pension Plan	9	0	• No role	• 2 years • 4 term maximum	12	5
Federal Deposit Insurance Corp.	5	2	• Chair	• 6 years • 5 years (Chairman)	12+	3
Pension Protection Fund	11	0	• Member	• 3 years • 2 term maximum	12	6
Natl. Railroad Ret. Investment Trust	7	0	• No role	• 3 years	4+	2
Overseas Private Investment Corp.	15	7	• Chair	• 3 years	4	1
Tennessee Valley Authority	9	0	• No role	• 5 years	4+	7
United States Postal Service	11	0	• Member	• 7 year staggered • 2 term maximum	12+	4
Ginnie Mae	0	N/A	• N/A	• N/A	N/A	N/A
Freddie Mac	18	0	• Chair	• 1 year • 10 term maximum	4+	5
Procter & Gamble	10-15	0	• Chair	• 3 years • 6 term maximum	7	5

Figure 3: Overview of results from in-depth case studies

5. Best Practices in Corporate Governance

The previous chapter laid out an integrated view of corporate governance for each of 11 organizations. This chapter explores best practices in corporate governance more systematically, one design element at a time. The 15 design elements explored here are the same as those depicted in Figure 1, starting with the size of the board, and ending with board meetings and communications processes.

For each design element, this chapter presents information from four different sources:

- ¶ Statistical and anecdotal information from private-sector corporations
- ¶ A broad, statistical review of all U.S. government corporations and all U.S. public pensions with assets greater than $1 billion
- ¶ The 11 in-depth case studies described in the previous chapter
- ¶ Views of experts in corporate governance, drawn from academia, government, and the private sector

Later chapters will draw on all this information and call out implications for PBGC.

A. BOARD SIZE

Boards come in a variety of sizes, but large companies almost always have seven or more members on the board. For publicly-traded companies in the U.S. with revenues greater than $10 billion, the average board size is 12.6. Across the Fortune 1,000, the average is 11.0.[12] Historically, the average board size in the U.S. has been trending downward, from 13 in 1972 to 11 in 2006.[13]

U.S. government corporations have an average of 7.5 board members, and 88 percent of these institutions have more than three members. For large public pensions, the average board size is 10.0 members, and 98 percent have more than three members. See Figure 4. For government corporations and large public pensions, the board size is usually mandated by statute. In contrast, CalPERS' board has a policy of periodically reviewing its own size against future oversight needs, and the Ontario Teachers' Pension Plan reviews its board size every two years.

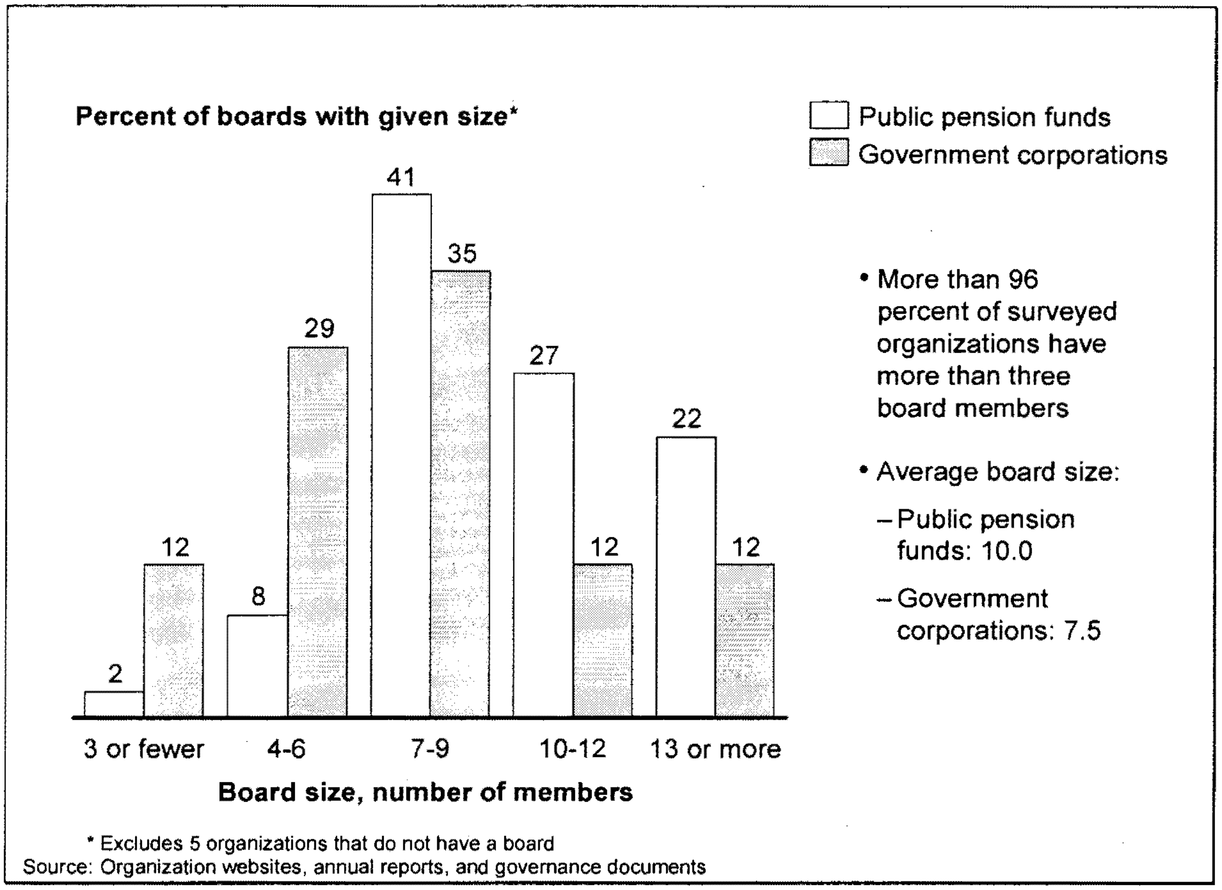


Figure 4: Board size of PBGC peer institutions

Organizational theory suggests that the larger board a board is, the more likely it is to become unstable and to require more effort to keep focused on key tasks.[14] The gradual decrease in private sector board size in the last thirty years may be a response to these challenges. Similarly, researchers have been able to correlate company performance to board size, and have found that companies with five to seven board members tend to perform better than those with larger boards[15], although this may be an incidental result of the fact that smaller companies tend to have both smaller boards and higher performance.

B. QUALIFICATIONS OF BOARD MEMBERS

Rules of the Securities and Exchange Commission (SEC), New York Stock Exchange (NYSE), and the National Associate of Securities Dealers (NASD) do not require companies' board members to meet specific skill qualifications. However, it is common for companies to leverage the expertise and experience of their board members to provide a range of perspectives on current and future challenges. A majority of private sector boards contain at least one member with each of the following profiles: a retired executive from another company, an investor in the company, a former government official, and an academic.[16]

In six of the 11 organizations selected for in-depth case studies, there are explicit and transparent qualification requirements related to functional or professional expertise. For example, both TVA and USPS require management expertise relevant to a large corporation or organization, and OPIC requires members who have professional experience in small business development and cooperatives. For the three organizations without explicit requirements on board-member qualifications (CalPERS, OTPP, and PPF), their 33 collective board members nonetheless had diverse professional and functional expertise, in finance (42 percent), government (27 percent), labor (18 percent), law (15 percent), and investments (15 percent).

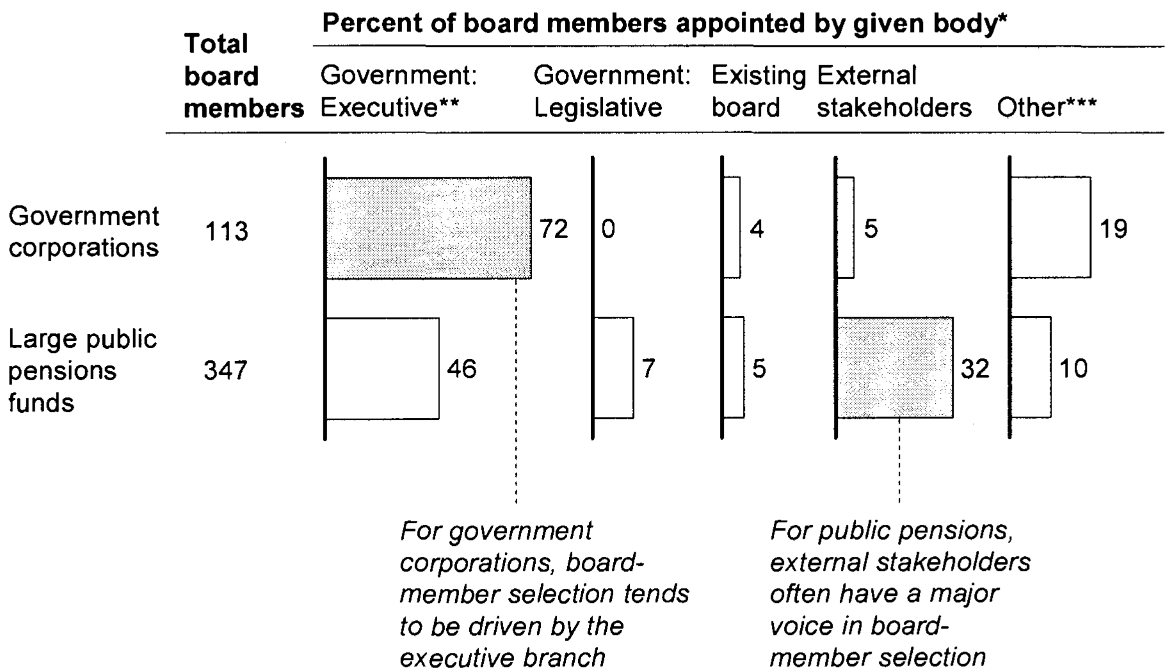
The Business Roundtable believes that "having directors with relevant business and industry experience is beneficial to the board as a whole.... A diversity of backgrounds and experience, consistent with the corporation's needs, also is important to the overall composition of the board."[17] A number of institutions share this view. For example, the Conference Board recommends that boards have a mix of knowledge and experience in accounting and finance; risk management; strategic and business planning; legal and compliance; human resources; marketing; technology; international markets; and industry knowledge.[18] The National Association of Corporate Directors suggests that the board as a whole should include competencies including accounting and finance, management, crisis response, industry knowledge, international markets, leadership, and strategic vision.[19]

C. SELECTION OF BOARD MEMBERS

In private-sector companies, board members are typically elected by shareholders. Among Fortune 1,000 companies, 97 percent have a nominating committee that is responsible for reviewing the qualifications of potential board members and proposing candidates to stand for election. The near universal reliance on nominating committees is the result of Sarbanes-Oxley and other regulatory changes; in 2001 only 48 percent Fortune 1,000 companies had a nominating committee.[20]

In the broad-based review of government corporations and large public pensions, there were notable differences between the two types of organization. In U.S. government corporations, 72 percent of board members were selected by the President of the United States, and almost all the remainder were ex officio board members, on the board by nature of a public office they hold. See Figure 5. In practice almost all of these ex officio members were selected for their public office by the President as well. In the U.K., PPF follows a different model: The chair is appointed by the Secretary of State for

Work and Pensions, but the chair then selects remaining board members through a rigorous and open civil service procedure



* Excludes organizations without a board or where data were not available
** If legislature confirms Executive nominee, appointment is attributed to Executive
*** Including ex officio board members, who are on the board by nature of a public office they hold
Source: Organization websites, annual reports, and governance documents

Figure 5: Methods for selecting board members

For large public pensions, fewer than half of board members were selected by the executive branch of government, and about a third are selected by external stakeholders, such as the pensioners covered by the plan. As a concrete example, for Ontario Teachers, the Government of Ontario and Ontario Teachers' Federation each select four board members.

D. OUTSIDE INTERESTS OF BOARD MEMBERS

For private corporations, a board member is said to be "independent" or an "outside director" if he or she is not an executive of the company. For public organizations, there is an additional notion of independence, regarding whether the board member is a full-time government employee. Evidence suggests that most board members, in private companies and public organizations, are not executives of the company, but for public organizations, most board members are full-time government employees.

In publicly-traded companies with more than $20 billion in revenues, 77 percent of board members are not executives of the company on whose board they sit.[21] In 2007, 90 percent of the companies belonging to the Business Roundtable reported that fewer than 20 percent of their board members were executives of the company.[22]

In the 11 in-depth case studies, most of the organizations require that most or all board members not be company executives. While board members of government corporations are usually not executives in those government corporations, 69 percent maintain full-time government careers. When government corporations have significant government official representation on their boards, they often place limits on how many board members can be affiliated with any particular political party. For example, FDIC requires that no more than three of its five board members be affiliated with any one political party.

The NYSE and other regulators of publicly traded companies recommend that a majority of board members not be executives of the company. The Council of Institutional Investors recommends at least two-thirds of the board not be executives of the company.

Board members are often selected so as to minimize conflicts of interest. For example, P&G requires that board members not be affiliated with corporations that are competitors. That said, board members invariably face occasional conflicts. In such situations, legal requirements and principles of good governance require that board members put those outside interests aside, as described below.

Most private-sector corporations in the U.S. are incorporated in Delaware, whose law states that board members have two types of fiduciary duty: that of "care" and that of "loyalty." The former requires that directors be well informed before making decisions and taking actions. The latter requires that directors' decisions and actions be motivated solely by the best interests of the corporation on whose board they sit.[23] Governance experts echo these legal requirements. For example, the Conference Board says that board members must put "the interests of the corporation before those of the individual director, or other individuals or organizations the individual director is affiliated with."[24]

Corporations themselves often reaffirm the principle of board-member duty. For example, NYSE-Euronext states that board members are expected to "exercise their business judgment in good faith and with due care to act in what they reasonably believe to be in the best interests of the company."[25]

The potential for conflict is particularly acute in organizations that invest funds, because boards of such organizations deliberately seek members who have investment experience, which is often obtained at companies that vie to provide goods and services to the organization. In such instances, corporations typically require the board member to fully disclose the potential conflict and to recuse himself or herself from decisions where the potential conflict could come into play. For example, Ontario Teachers has several board members who work at or are on the board of securities dealers or investment companies, but these board members do not participate in decisions that could affect their firms.

Conflicts can occur in public companies and with board members who are government employees. For example, the heads of the OTS and OCC are on the FDIC board. These two board members sometimes face decisions at FDIC that affect their parent organizations, since all three organizations regulate depository institutions.

At PBGC, board members sometimes balance tensions between the interests of PBGC and the cabinet departments over which they preside. For example, regulatory changes at PBGC may be in PBGC's interests while also highlighting shortcomings in regulations in the cabinet departments. Similarly, it is possible for PBGC's board to militate for PBGC to make budget expenditures that benefit the cabinet departments. While PBGC states that it abides by all laws governing appropriations and expenditures, PBGC has not articulated an explicit policy about how board members should handle such situations.

In summary, conflicts or potential conflicts occur on almost every board, whether it be a private or government corporation. Organizations manage these conflicts by promoting transparency and instituting formal governance rules, such as requiring each board member to act in the interest of the company on whose board they sit, rather than in the interest of any other organization with which they are affiliated. In practice, these methods allow the boards to function effectively in spite of the conflicts.

E. BOARD LEADERSHIP

The likelihood of the CEO also serving as board chair varies by geography. In the U.K., only five percent of CEOs serve as board chair, while in publicly traded companies in the U.S., 75 percent of CEOs serve as board chair. In the U.S. there has been a gradual decline in the number of companies that combine the roles and a substantial increase in the prevalence of the formalized appointment of a lead outside director. Of Fortune 1,000 U.S. companies that combine the CEO and board-chair roles, 80 percent have a lead outside director.[26]

In the U.S. public sector, it is less common to have the CEO also serve as board chair. Only 17 percent of U.S. government corporations do so, and none of the 67 large public pensions surveyed combined the roles.

The Council of Institutional Investors recommends that boards be chaired by an outside director. If the board decides to have the CEO also serve as board chair, they recommend that the board appoint a lead independent director and provide a written explanation of their reasons for combining the roles. James Darazsdi, author of *The Governance Committee: A Director's Handbook*, says, "Who leads the board in ensuring effective board governance? The answer should point to an independent director."[27]

F. BOARD COMMITTEES

All Fortune 1,000 companies have at least two board committees, due in part to NYSE rules requiring all listed companies to have an independent audit committee and a nominating or governance committee.[28] The SEC also requires an independent audit committee. In contrast, NASD merely requires independent oversight of nomination and compensation decisions, without identifying committees as the mechanism for guaranteeing independence. Sarbanes-Oxley prohibits company executives who are on the board from being part of certain committees, such as those covering governance and compensation. In private-sector companies, there do not seem to be any notable instances of board committees having members who are not also members of the overall board.

U.S. government corporations have 1.6 board committees on average, while large public pensions have 3.4 board committees. For government corporations, the most common committees are Audit/compliance and Advisory committees, each present in 25 percent of organizations. For large public pensions, the most common committees are Audit/compliance and Investment, present in 67 percent and 59 percent of organizations, respectively. See Figure 6.

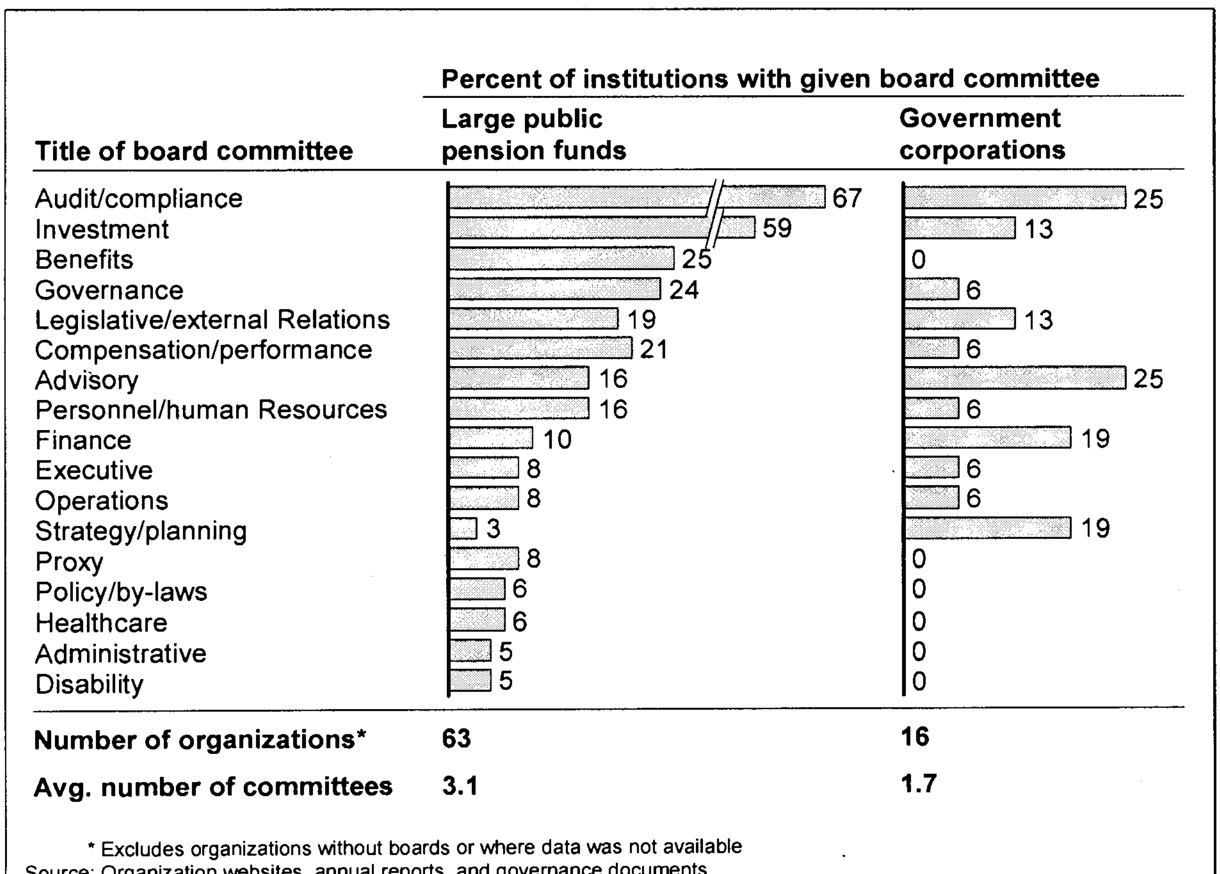


Figure 6: Nature of typical board committees

In the 11 in-depth cases studies, every organization with a board has at least one board committee, and some have as many as eight committees. Some of these organizations have detailed requirements for a board member to be on a given committee. For example, PPF requires that the Audit Committee be composed of at least three members who are not company executives and at least one member with professional finance experience, and PPF's Investment Committee must have a majority of members and a committee chair who are not company executives.

The Conference Board supports the use of committees and recommends establishing committees "that will enhance the overall effectiveness of the board by ensuring focus on and oversight of matters of particular concern."[29] The Business Roundtable does not recommend specific committees per se, but it does advise boards to involve independent board members issues related to audit, board-member nominations, governance, and compensation.[30]

G. TERM LENGTH OF BOARD MEMBERS

A 2002 survey of the NASDAQ-100 found that all have board member term lengths of one to three years, with 52 percent having one-year terms, and 47 percent having three-year terms.[31]

U.S. government corporations and large public pensions tend to have longer term lengths, averaging 3.9 years and 3.8 years, respectively.[32] Several organizations in the in-depth case studies have recently shortened term lengths of board members. For example, USPS board members now serve for seven years instead of nine, and TVA board members serve five years instead of nine.

Some organizations also have frequent election or selection cycles to regularly evaluate board performance with an opportunity for extended re-appointment. Freddie Mac has single-year terms, though board members can be reappointed and serve up to ten years. OTPP also has frequent re-elections with board members serving two-year terms up to a maximum of four terms.

The SEC, NYSE, NASD, and other financial regulators have neither formal requirements nor recommendations on the term length for board members. NYSE's own board members are elected to one-year terms, though they can be reelected indefinitely.

In a recent McKinsey global survey of company directors, managers, and executives, one third of respondents did not see a need for term limits; another third believed terms should be six years or more.[33] In contrast, the Council of Institutional Investors recommends that all directors be elected annually, in non-staggered terms.[34]

H. TERM LENGTH OF CHIEF EXECUTIVE

In the private sector, the chief executive seldom has a fixed term length, but in the public sector, this is more common. For example, the Federal Reserve Banks, GAO, the Export-Import Bank, and FDIC all have fixed terms for their chief executives.

I. RESPONSIBILITIES OF THE BOARD

Almost all large private sector corporations have written bylaws that specify how the board will function and on what areas the board will engage. For example, General Electric's statement of governance principles lists the five key functions of the board. For government corporations, board powers and responsibilities are often stated in broad terms by the enabling legislation, which are then usually further specified in corporate bylaws.

For example, FDIC's bylaws clearly assign roles and responsibilities to the board, the Director of Division of Supervision and Consumer Protection, the Deputy Director, Assistant Directors, and Field Supervisors. The board retains authority to accept or deny applications for federal deposit insurance or to rule on any enforcement matter. The board delegates the responsibility to approve, deny, and investigate deposit insurance applications and filings; to investigate and intervene in the activities of state banks; and to take corrective or enforcement actions.

Similarly, the PPF in the U.K. created a detailed and specific articulation of duties in its Statement of Operating Principles and Scheme of Delegations. This 12-page document outlines those duties that are delegated to board committees and to the chief executive. PPF's board chose "to make extensive delegation of its functions" to others within the organization."[35] Appendix IV contains a sample governance matrix specifying detailed roles and responsibilities of the board and various other company stakeholders, akin to the precise articulation in PPF's bylaws.

The Business Roundtable, the Conference Board, and the National Association of Corporate Directors recommend that boards develop a statement of corporate governance principles.[36] Business scholar David Nadler, writing in the *Harvard Business Review*, recommends that boards develop a charter that specifies the duties of the board and then translate those duties into specific activities, with a desired level of board engagement for each activity. Nadler explains that boards benefit from this exercise by gaining a useful measure for self assessment, creating a context for board alignment on roles and responsibilities, and prompting healthy questions about the kinds of expertise needed on the board.[37] Clear articulations of the kinds of actions boards will and will not undertake tend to improve board efficiency by helping the board to focus on essential issues.

J. BOARD MEMBER TIME COMMITMENT

In a 2005 survey, members of private-sector corporate boards reported spending an average of 22 hours per month on board matters.[38] Another 2005 survey found that 62 percent of board members in Fortune 1,000 companies allocated 16 or more hours a month to activities of the board.[39]

Some board guidelines have explicit requirements or expectations about member attendance and time commitment. For example, board members at CalPERS usually spend one or two days per month on board-related activities. The PPF expects its board members to commit to roughly 20 days of work a year. P&G's board guidelines state that attendance is expected at all meetings, and the chair of the board and P&G's Governance and Public Responsibility Committee initiate a review of Board member conduct if attendance falls below 75 percent.

The American Bar Association Task Force on Corporate Responsibility suggests that boards establish clear expectations for board member time commitments.[40] Similarly, the Council of Institutional Investors urges companies to establish appropriate expectations and limit board member service to a maximum of two other corporate boards.[41]

K. BOARD MEMBER COMPENSATION

Because of the time commitment required, most private sector companies compensate board members for their time. In Fortune 1,000 companies in 2005, average annual cash compensation for outside board members averaged $76,707, which included both a yearly retainer and a fee for each meeting attended. Total cash compensation for board members of companies with more than $20 billion in revenues averaged $115,375. For board members of companies with less than $3 billion in revenues, it averaged $55,178. Cash compensation of board members has been increasing in recent years. These figures do not include non-cash compensation, such as stock options, which is often substantial.[42]

In the 11 in-depth case studies, compensation for board members varied widely. USPS pays board members a salary of $32,000 per year and $300 per day of service. The TVA pays board members a salary of $45,000, and an extra $5,000 per year for the chair of the board. The PPF compensates its board members £15,300 for their expected 20 days of work per year. Freddie Mac compensates board members annual cash compensation of $60,000 plus per-meeting fees and equity compensation.

Today, PBGC has an Advisory Committee that makes non-binding recommendations to PBGC's board on policy issues. ERISA states that compensation for members of the Advisory Committee shall be no more, pro rata by time served, than the rate paid to Government Schedule 18 employees.

Regulators and experts have increased their focus on compensation of board members in recent years, in line with the greater attention to corporate governance and growing responsibilities of board members. For example, the Council on Foundations explains why board-member compensation is important: "Responsible board service is time-consuming, legal requirements have become increasingly complex and potential liabilities have grown. In some cases, compensation can facilitate participation by persons with different skill levels and those with different economic circumstances."[43] The National Association of Corporate Directors agrees, stating that "maintaining an appropriate structure and level of director compensation is a critical element of good board governance."[44] The executive compensation consulting firm Watson Wyatt Worldwide expects that "the market for director talent will continue to be tight" and that as a result, board member pay will increase.

L. BOARD SUPPORT

Most large organizations in the private, public, and nonprofit sector have one to four full-time staff dedicated to administrative functions of the board, including managing the board's calendar, gathering and distributing materials to the board, and organizing board meetings. This staff usually includes a board secretary who sets the board's agenda, crafts minutes of board meetings, updates and applies the board's bylaws, and provides guidance to the board on governance issues, among other duties. This individual may be fully dedicated to the board but usually has other duties, such as being the general counsel of the company. Very few large organizations have dedicated substantive staff for the board. Instead, on substantive topics, the board relies on executives within the organization or outside consultants.

The organizations studied in the 11 in-depth case studies follow this pattern. The FDIC has a full-time support staff of at least six assistants who primarily serve the full-time board members. The USPS has a full-time Secretary that coordinates resources for and serves as the primary staff assistant to the Board. Freddie Mac has a Corporate Secretary that coordinates all communication and administration for the board. OPIC has a Corporate Secretary that maintains board records, resolutions, and publicly-accessible information. CalPERS has a full-time executive program manager and staff of three to five assistants who coordinate administrative issues for the board. None of these organizations seems to have a full-time substantive staff, and their staff size tends to be larger when the board is larger and when it meets more frequently.

Each member of PBGC's board uses his or her own staff to help with the oversight of PBGC, working through substantive issues and vetting proposals. There do not seem to be any examples of other boards using their outside staffs in this way.

M. BOARD MEMBER INDUCTION AND TRAINING

When board membership changes, the board's effectiveness can be hampered by the loss of institutional memory and knowledge. To counteract this effect, about two-thirds of boards now conduct formal orientation and training programs for new board members.[45] The programs usually focus on building both company-specific knowledge, such as how the companies products work, and functional skills, such as principles of risk management.

Many of the institutions in the 11 in-depth case studies have such board orientation and training programs. For example, Ontario Teachers' Pension Plan has an orientation program for new board members and sponsors ongoing seminars and technical workshops on financial topics. The board also regularly turns to external advisors for education on particular topics, such as investment management and compensation. As another example, Freddie Mac's board has a formal orientation program that is overseen by the board's chair. This program includes written materials and briefings by company management, on topics including business strategy, risk management, and corporate governance.

N. BOARD EVALUATION

Most boards periodically assess the effectiveness of the board and its members. Such assessments are usually based on (a) structured questioning of the board members themselves or (b) examination by outsiders, such as consultants. In a 2005 survey, 84 percent of board members in large private-sector corporations reported that their organization formally evaluated the board's performance on a regular basis. Only 37 percent reported that their organization evaluated individual board members, but 77 percent said that they thought it should.[46]

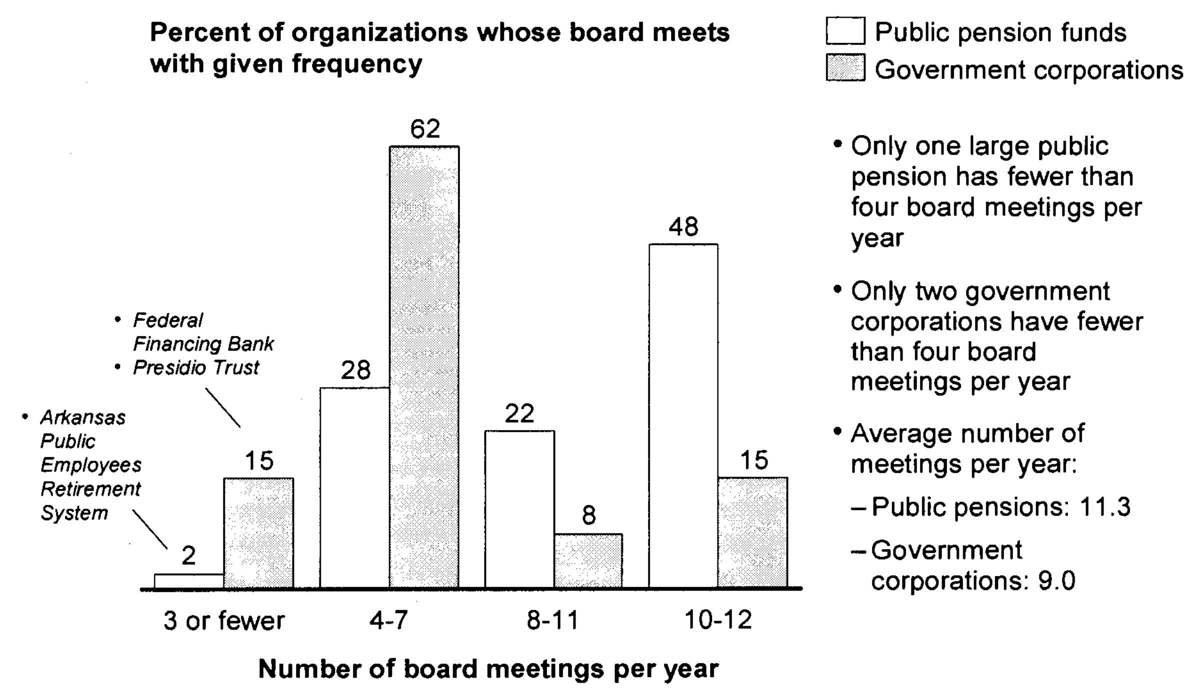
Many of the organizations in the 11 in-depth case studies have formalized processes for board evaluation. Ontario Teachers' Governance Committee reviews board performance through a self-evaluation survey of effectiveness of board, committees, and membership knowledge level. The chair of PPF's board formally reviews board performance and governance once per year. CalPERS' Governance Committee reviews the effectiveness of the board's internal governance procedures and recommends to the board any changes or additions. Freddie Mac's Governance, Nominating, and Risk Oversight Committee evaluates the policies, procedures, and information of the board overall, while each standing committee formally evaluates itself annually.

Experts such as the Conference Board and the NYSE are increasingly calling for meaningful board evaluation. For example, management consultants often advise their clients to institute a formal survey of board members to test their knowledge of the risks of the organization and how those risks are managed. The results of such surveys then guide selection of new board members, allocation of board members to committees, and ongoing education of board members.

O. BOARD MEETINGS AND COMMUNICATIONS

The boards of public companies meet frequently: Publicly-traded companies with more than $20 billion in annual revenues meet an average of eight times per year.[47] These meetings tend to be lengthy: In a recent survey, half of board members cited the average length of a board meeting to be five hours.[48] Sometimes board meetings last one or two full days, as with annual strategic offsites. Most board meetings are conducted in person: For NASDAQ-100 companies, only 17 percent of board meetings took place by exchanging written materials, and only one percent took place by phone.[49] During these broader board meetings, almost all boards break into committees for focused discussions, and almost all boards go into executive session to allow outside board members to speak candidly about the management team and direction of the company.[50]

The boards of large public pensions and U.S. government corporations also meet frequently. See Figure 7. The boards of large public pensions meet on average more than 11 times per year, and only one meets less than four times per year. The boards of government corporations meet nine times per year on average, and only 15 percent meet less than four times per year.



* Meeting frequency not available for 14 of 84 organizations surveyed

Source: Organization websites, annual reports, and governance documents

Figure 7: Frequency of board meetings

Of the 11 organizations in the in-depth case studies, half the boards meet at least monthly: CalPERS, FDIC, Ontario Teachers, PPF, and USPS. For example, the FDIC board meets at least once a month, and sometimes weekly, with seven to eight sessions per year that are open to the public. Of the nine organizations with boards, all of them meet at least four times per year.

Experts on governance do not spell out rigid rules for the frequency of board meetings, since the optimal frequency will depend on the nature of the organization and the agenda of the board. For example, the Business Roundtable encourages board meetings that are frequent enough to provide sufficient oversight, given the company's particular situation. Most experts suggest frequent executive sessions of the board, to maximize the oversight provided by outside members of the board. For example, NYSE rules recommend regular executive sessions.

6. Structural Options to Improve Governance

The framework of PBGC's governance structure is set by legislation: ERISA and PPA dictate the composition of PBGC's board and the role of PBGC's board and Director. Changes to that structure would open up new approaches to PBGC's governance.

This chapter identifies five options for the overall governance structure of PBGC and then discusses the pros and cons of those options in light of best practice and the ability of PBGC to fulfill its mission.

A. OPTIONS FOR PBGC'S GOVERNANCE STRUCTURE

There are many potential governance structures for PBGC. The key variables are whether or not to have a board and the size and composition of the board. The following five options span those variables:

Option A. Larger board, fully autonomous. PBGC's current board would be replaced with 7-11 individuals from the private sector. There would be explicit selection criteria that would ensure candidates had skills and experience that would be relevant to PBGC. The board would create two to four committees to oversee critical organizational issues, such as the audit function.

Option B. Larger board with some government members. This option would be a blend of Option A and Option C. PBGC's current board would be replaced with 3-5 private-sector individuals and 4-6 government executives, one of whom might be the PBGC Director. The board would create two to four committees to oversee critical organizational issues, such as the audit function.

Option C. Larger board with all government members. PBGC's current board would be replaced with 7-11 government executives, one of whom might be the PBGC Director. Board members would be at the Undersecretary and Assistant Secretary level, or their equivalent, drawn from throughout the federal government. Some of these board members might be career government executives, rather than political appointees. Some may serve ex officio, by nature of their offices. The board would create two to four committees to oversee critical organizational issues, such as the audit function.

Option D. Small board, all government members. This is the status quo. The board would continue to consist of the Secretaries of Commerce, Labor, and Treasury.

Option E. Departmental rollup. PBGC's current board would be eliminated. PBGC would remain a separate U.S. government corporation, but it would report to the Secretary in one of the federal departments.

The following sections assess each of these options, first against best practices, and then against PBGC's mission.

B. ASSESSMENT OF STRUCTURAL OPTIONS VERSUS BEST PRACTICE

The review of governance in private sector corporations, government corporations, large public pensions, and the 11 in-depth case studies collectively point to four best practices in governance structure:

1. **Get the right people involved in oversight.** Effective governance hinges on having a board with appropriate skills and experiences to know how to guide the organization and challenge the management team. The required skills and experience will vary from one organization to another. Each board member need not have the full range of necessary skills and experience. Rather, it is the composition of the board overall that leads to effective governance. TVA, USPS, PPF, OTPP, and many best practice organizations use explicit selection criteria and formal nominating committees to ensure optimal board composition. In addition to appropriate skills and experience, well functioning boards minimize the potential conflicts of board members by carefully selecting board members with minimal conflicts.

2. **Ensure that enough time is spent on oversight.** Good governance takes time, to understand the issues and deliberate on the organization's options. Boards that are stretched for time tend to take what they are given, not having time to ponder deeper issues and ask probing questions. In most well-functioning boards, each board members spend 16 or more hours per month on board-related issues. Some of this time is spent in board meetings, but even more is typically spent reading and digesting thoughtful materials that are distributed to the board on a regular basis.

3. **Create a high degree of continuity of oversight.** Boards are more effective when they have institutional memory. The organization can learn from its successes or failures only if there are mechanisms to recall past experiences. The leading mechanism is to have board members with longstanding involvement with the organization. That is why high-performing organizations tend to have total board terms of more than four years and deliberately stagger the appointment of new board members. This is particularly challenging in government organizations, especially when board members are political appointees serving ex officio. This is likely why only 20 percent of board members of U.S. government corporations serve in an ex-officio capacity.

4. **Focus oversight on particular areas.** Governance requires careful attention to particular areas, like investment strategy and the audit function. Given the many demands on boards today, they tend to be more effective if (a) they focus on big-picture issues, like long-run strategy, and (b) the various areas of inquiry are delegated to specific subsets of the board, usually through board committees. Of the organizations studied in the in-depth cases, almost all made extensive use of committees as a way to achieve focus. Oversight is further focused by clearly assigning roles and responsibilities, so the board avoids wasting time on issues of secondary importance.

Figure 8 explores how the five structural governance options would perform against these four best-practice governance principles

Effect of option, relative to Option D: Positive / Neutral / Negative

✓ Good
× Bad

Governance option		Best practices: 1. Right people involved in oversight	2. Enough time on oversight	3. High degree of continuity of oversight	4. Focused oversight (e.g., committees)
Option A **Larger board, fully autonomous**	• Board consists of 6-10 members from private sector, plus PGCC Director • 2-4 board committees	✓ Fully selectable skills and knowledge × Chance of biases and less gov't experience	✓ More outside board members, able to commit to increased hrs ✓ More total board member hours	✓ Staggered and longer terms × Potential delay in confirming board members	✓ Many issues handled in committee
Option B **Larger board with some gov't. members**	• Board consists of 3-5 members from private sector, 3-5 members from government, plus PGCC Director • 2-4 board committees	✓ Mostly selectable skills and knowledge ✓ Some gov't. experience × Chance of biases	✓ More outside board members, able to commit to increased hrs ✓ More total board member hours	✓ Staggered and longer terms, some filled automatically, others requiring longer process	✓ Many issues handled in committee
Option C **Larger board with all gov't. members**	• Board consists of 6-10 members from government, plus PGCC Director • 2-4 board committees	✓ Strong gov't. expertise; some breadth of experience × Some biases across gov't.	✓ More board members ✓ More time relative to Dep't Secretaries	✓ Some members brought on quickly, ex officio × Board terms still mostly short and not staggered	✓ Many issues handled in committee
Option D **Small board, all gov't. members**	• Status quo, with enhancements	Defined to be neutral Skills balance dependent on experience of Secretaries and will vary over time; can draw on dep't staffs	Low level of engagement, given small Board and many outside commitments	No board continuity; some staff continuity; board appointed quickly as ex officio	Proposed bylaws delegate many decisions; board committees not possible Defined to be neutral
Option E **Departmental rollup**	• Integrate PBGC into one of the federal departments • No board	× Dept staff rarely have the skills and experience to oversee large investment portfolios	✓ Uses department's governance infrastructure	Dept. staff give some continuity, as today	✓ Clear operating principles and limits within department

Figure 8: Assessment of governance options versus best practices

C. ASSESSMENT OF STRUCTURAL OPTIONS VERSUS PBGC'S MISSION

ERISA laid out the three-part mission of PBGC[51]:

1. Provide timely and uninterrupted payment of pension benefits
2. Keep pension insurance premiums at a minimum
3. Encourage the continuation and maintenance of private-sector pension plans

These mission objectives are supported implicitly by five root objectives against which PBGC's governance should deliver:

a. **Optimize operations to pay beneficiaries promptly.** PBGC has complex operations, directly administering benefits to over 600,000 pensioners. In order to pay benefits promptly (objective 1), PBGC needs to have well-engineered operations. For example, there are sometimes delays in benefit payments while

PBGC works through the arithmetic of how much to pay beneficiaries of newly terminated plans.

b. **Make prompt policy decisions.** Some policy decisions affect PBGC's timely payment of benefits (objective 1), while others affect long-run insurance premiums (objective 2). For example, PBGC occasionally decides to terminate a pension plan in an orchestrated fashion, prior to bankruptcy of the plan sponsor. This can allow for timely payments (objective 1) and can reduce total PBGC obligations (objective 2), by preventing the moral hazard of newly promised but never-funded shut-down benefits.

c. **Use PBGC resources efficiently.** PBGC is a major business enterprise. Effectively managing general and administrative costs is an important way to keep long-run insurance premiums down (objective 2).

d. **Invest PBGC assets effectively.** PBGC's investment portfolio is valued at $63 billion, of which $48 billion is in the Trust Fund, where PBGC has discretion on the investment strategy. Improving risk-adjusted returns on this portfolio is an important lever for improving the solvency of PBGC and reducing the need for increases in insurance premiums (objective 2). If federal government decides in practice to guarantee PBGC obligations, taxpayers could be at risk or stand to benefit from PBGC's investment results.

e. **Advise Congress on premiums.** Congress sets the insurance premiums that private-sector corporations must pay for PBGC's pension insurance. Congress can and should rely on PBGC to explain what premiums will be required to maintain the solvency of the enterprise (objective 2).

Figure 9 explores the ability of each structural governance option to deliver against these five root objectives of PBGC.

Effect of option, relative to Option D: Positive / Neutral / Negative

✓ Good
× Bad

Governance option	Mission criteria*: 1. Provide timely payments — a. Improve ops, cut checks on time	b. Make prompt policy decisions (1. Provide timely payments; 2. Minimize pension premiums)	2. Minimize pension premiums — c. Use PBGC resources efficiently	d. Invest PBGC assets effectively	e. Advise Congress on premiums
Option A Larger board, fully autonomous	✓ Substantial private-sector expertise in operations	✓ Staggered board terms allow for institutional memory × Potentially less policy experience	✓ Substantial private-sector expertise in cost management	✓ Substantial expertise in investment management	✓ Expertise on risk-based pricing ✓ Seen as independent
Option B Larger board with some gov't. members	✓ Some private sector best practices in ops; some expertise in government operations	✓ Partially staggered terms allow memory; some policy experience	✓ Balance of private and public expertise in cost management	✓ Improved expertise in investment management	✓ Some expertise on risk-based pricing, and some degree of independence
Option C Larger board with all gov't. members	✓ Substantial expertise in effective operations in government context	✓ Substantial policy experience × Few staggered terms so less institutional memory	✓ Substantial expertise in efficiency in government	Skills balance dependent on experience of board members and will vary over time	✓ Broad stakeholders but each of only moderately high status
Option D Small board, all gov't. members (Defined to be neutral)	Skills balance dependent on experience of Secretaries and will vary over time	Substantial policy experience; little institutional memory; need clearance from many depts.	Skills balance dependent on experience of Secretaries and will vary over time	Skills balance dependent on experience of Secretaries and will vary over time	Each stakeholder has high status; small group with clearly vested interests (Defined to be neutral)
Option E Departmental rollup	✓ Might leverage operations of department × May be subject to gov't closure	✓ Dept. staff provide continuity and policy experience × Dept's often slow to decide	✓ Some economies of scale using departmental overhead and systems	× Dept staff rarely have the skills and experience to oversee large investment portfolios	× Very narrow base of support × Low visibility to those outside department

* Mission elements drawn from ERISA legislation; mission element "encourage continuation and maintenance of private pensions" not included because not affected substantially by governance options

Figure 9: Assessment of governance options versus PBGC's mission

7. Governance Choices Stemming from Structural Change

Many governance design elements are independent of formal governance structure. For example, however a board is composed, clarifying roles and responsibilities confers governance benefits. This chapter considers five design elements that are linked to the structural decisions in the previous chapter. In particular, each of these five elements clarifies the design and operation of the PBGC board.

1. **Board leadership (i.e., Chair).** Today, the Secretary of Labor is the chair of PBGC's board. If PBGC continues to have a board, the board chair would need to be determined. Figure 10 lists the various options and their pros and cons. Having the PBGC Director also serve as chair of the board would ensure that the chair would have substantial engagement on PBGC issues, but it would also be contrary to emerging best practices in corporate governance, which tends to favor a separation of the roles of board chair and CEO. Having a cabinet secretary serve as board chair may not be a desirable option, because (a) such high-level officials may not have sufficient time to be fully engaged on PBGC issues, (b) cabinet secretaries do not generally stay in office for a long time, (c) that could favor the interests of one department over others, and (d) there may be conflicts between the interests of PBGC and of the department the Secretary oversees. Having an outsider serve as chair would address these potential issues, especially that of ensuring good governance via the separation of the roles of board chair and CEO. There are two other options, not considered in Figure 10: The board could vote on who would be chair from amongst its own non-executive members, or the President could designate the board chair from the existing board members whenever that position became vacant. These options would have the benefit of considering all the criteria in light of the particular individuals on the board, but both these options would decrease the predictability of board leadership.

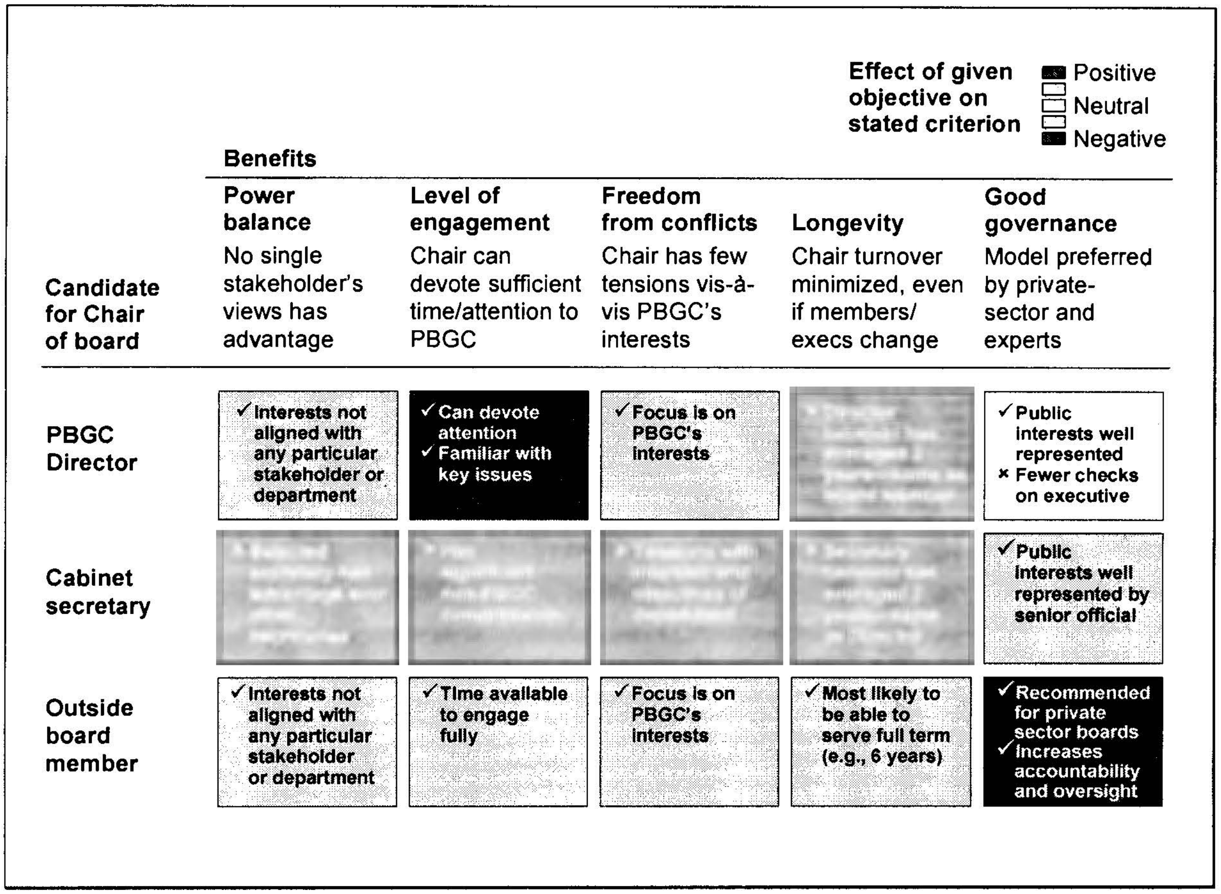


Figure 10: Options for chair of PBGC's board

2. **Selection of board members**. If PBGC is to have a larger board, it will need to determine how to select those members. For U.S. government corporations, the President selects almost all board members, and in most instances the Senate must confirm these selections. The main benefits of this approach are that it ensures board members have solid public-policy credentials and increases the prestige of board membership, thus increasing the pool of desirable candidates. The main drawback of this approach is that it can be time consuming. If the President selects board members, there could be a restriction requiring a balance of affiliations to particular political parties. For example, the FDIC's board cannot have more than three members any one political party.

3. **Term length of board members**. Today, PBGC's board members are determined ex officio, by nature of the cabinet office they hold. As such, their stay on the PBGC board is equal to their tenure in the cabinet. Under the structural options in which PBGC's board is enlarged, many or all of the board members would not serve ex officio, so their stays on the board could be set by deliberate decision. As described in earlier chapters, in private-sector and public corporations, the term length of board members varies widely, with terms of 1-14 years. Typically,

organizations with shorter term lengths re-select board members for repeated terms, leading to a typical total tenure of six years or more. For the effectiveness of governance, total term on the board matters more than the amount of time between board selections. Total term lengths of less than four years tend to decrease board effectiveness because board members are not fully conversant in the specifics of the organization. On the other hand, total term lengths longer than ten years run the risk of board-member complacency and missing out on fresh thinking. The term length of board members also affects the amount of board continuity. For example, the Federal Reserve Board fosters continuity by appointing governors to long and staggered terms, appointing one of its seven members every two years, for a 14-year term.

4. **Board-member time commitment**. The smaller PBGC's board, the greater the requisite time commitment of any individual member. For example, the FDIC has a small board, with only five members, but three of them serve FDIC full time. The time commitment required of individual board members will depend on the size of the board. As described above, board members of large private-sector corporations, which tend to have boards of nine members or more, typically spend more than 16 hours per month on board-related activities. Having a larger time commitment of each board member would tend to improve governance, but placing large demands on board members might shrink the pool of talented individuals who would be willing to invest that much time.

5. **Board-member compensation**. Today, PBGC does not compensate its board members, because they serve ex officio, by nature of their cabinet positions. If PBGC were to enlarge its board to include private-sector individuals, financial compensation might be necessary, especially if desired time commitments were large. As described above, in public and private organizations of PBGC's size and complexity, board members typically receive $30,000-$60,000 per year, plus additional compensation for meetings and for holding leadership positions. In the private sector, board members also typically receive equity compensation, such as stock options, but this would not be possible for PBGC. Board members of public organizations do typically receive financial compensation, but at below-market rates, since many talented individuals are willing to serve out of public interest and for the prestige of the position. The same is likely to be true of potential members of PBGC's board. If PBGC were to enlarge its board to include non-government employees, PBGC could likely compensate these new board members just like PBGC compensates members of its Advisory Committee today.[52]

All these governance design options must be considered jointly, to establish a well-orchestrated governance system. For example, board-member compensation is inextricably linked to board-member time commitment, and the optimal term on the board will depend on the size of the board and how time-consuming the selection process is.

8. Conclusion

PBGC is an institution whose importance, size, and complexity will increase in the coming years. In this context, it is increasingly important to ensure strong governance at PBGC, to give the President, Congress, and the public confidence that PBGC is being managed effectively.

There are several viable alternatives for PBGC's governance structure and practices. In terms of formal governance structure, the most-important design decision is the size of PBGC's board: PBGC could have a large board, no board at all, or anything in between. There are strengths and weaknesses of each alternative.

Once the overall governance structure is settled, there will remain several design choices, such as whether to include PBGC executives on the board and who should be chair of the board. There are several reasonable options for each of these design choices.

PBGC's governance has improved in recent years, with heavy engagement by the current board, passage of the PPA, expanded and improved board bylaws, and the creation of a permanent Deputy Director position that will not change from one administration to another. It will be worthwhile to continue to invest time and energy to ensure strong governance at PBGC, because better governance leads to higher performance and better decision-making, which will enable PBGC reliably to fulfill its important mission in the coming decades.

Appendix I. Statement of Work

The contractor shall review the PBGC's current board structure and governance practices in order to understand its unique structure.

The contractor shall prepare a detailed report that shall:

1. Describe the board structure and governance practices of government corporations, including those identified in the GAO recommendation to Congress and selected private sector corporations and identify the advantages and disadvantages of each as they relate to the unique mission of the PBGC. In particular, the report should describe for each:

    a. The mission, structure, and authorities of each corporation along with how it is similar to or different from the PBGC.

    b. The formal governance structure including, as applicable, number of members, terms, expertise represented, number of subcommittees, and bylaws.

    c. The formal and informal governance operation including the number, length and focus of formal meetings; and extent of informal contact between corporate officials and governing officials and their staffs.

    d. Whether there is a dedicated staff, independent of corporate management, that supports the governing body's oversight and policy functions and how that operates, if there is no such dedicated staff, how interaction between the Board members (and their staffs) and the corporation works.

2. Review pertinent best practices in corporate governance in the public and private sectors, including both for-profit and not-for-profit corporations that the Board might wish to consider in its review of the PBGC structure.

PBGC will provide the contractor with PBGC's corporate governance documents, its compendium of applicable laws and regulations, and recent annual reports.

The contractor shall meet at the commencement of the contract and periodically thereafter with PBGC and Board staff to discuss the progress of the report, and, when the report is issued, shall present a briefing to PBGC and Board staff at PBGC headquarters in Washington, D.C. The contractor also may be directed to make special presentations to the Board Members or their staffs.

Appendix II. Organizations Studied

Many of the facts cited in the body of this report were gathered from a broad-based review of all known U.S. government corporations and all known U.S. public pensions with assets of $1 billion or more. Table 1 and Table 2 list all these organizations.

For each organization, the broad-based review collected data on: the number of board members; whether each board members was a government-sector or private-sector employee; whether the CEO was the chair of the board; who nominated or selected the board members; the term length of board members; the names of any board committees; and the frequency of board meetings. This information was gathered from the organizations' annual reports, websites, and press releases, as well as from third-party sources such as press articles and academic research on governance.

Organization name
Commodity Credit Corporation
Export-Import Bank of the United States
Federal Crop Insurance Corporation
Federal Deposit Insurance Corporation
Federal Financing Bank
Federal Prison Industries
Financing Corporation
Government National Mortgage Association
National Railroad Passenger Corporation (AMTRAK)
Overseas Private Investment Corporation
Presidio Trust of San Francisco
Resolution Funding Corporation
Rural Telephone Bank
Saint Lawrence Seaway Development Corporation
Tennessee Valley Authority
United States Postal Service
Valles Caldera Trust

Table 1: U.S. government corporations included in broad-based review

Organization name	Organization name
Alameda County Employees' Retirement Association	Minnesota State Board of Investment
Arkansas Public Employees Retirement System	Missouri Public School & Non-Teacher School ERS
Arkansas Teacher Retirement System	Missouri State Employees' Retirement System
California Public Employees' Retirement System	Montgomery County Employees' Retirement System
California State Teachers' Retirement System	New Hampshire Retirement System
Colorado Fire and Police Pension Association	New Jersey Division of Investment
Colorado Public Employees' Retirement Association	New York City Board of Education Retirement System
Connecticut Retirement Plans and Trust Funds	New York City Employees' Retirement System
Contra Costa County Employees' Retirement Association	New York City Police Pension Fund
Dallas Employees' Retirement Fund	New York City Teachers' Retirement System
Delaware Public Employees Retirement System	New York State and Local Retirement Systems
Detroit General Retirement System	New York State Teachers' Retirement System
District of Columbia Retirement Board	North Carolina Teachers' and State Employees' Ret. System
Fairfax County Educational Employees' Ret. System	Ohio Police & Fire Pension Fund
Florida State Board of Administration	Ohio Public Employees Retirement System
Houston Firefighters' Relief & Retirement Fund	Ohio School Employees Retirement System
Idaho Public Employee Retirement System	Ohio State Teachers' Retirement System
Illinois State Board of Investment	Orange County Employees Retirement System
Illinois State Universities Retirement System	Pennsylvania Public School Employees' Retirement System
Illinois Teachers' Retirement System	Pennsylvania State Employees' Retirement System
Iowa Municipal Fire & Police Retirement System	Sacramento County Employees' Retirement System
Iowa Public Employees Retirement System	San Diego City Employees' Retirement System
Jacksonville Police and Fire Pension Fund	San Francisco City & County Employees' Ret. System
Kentucky Retirement Systems	San Jose City Employees Retirement System
Kern County Employees' Retirement Association	Santa Barbara County Employees' Retirement System
Los Angeles City Employees' Retirement System	South Carolina Retirement System
Los Angeles County Employees Retirement Association	Tennessee Consolidated Retirement System
Los Angeles Fire and Police Pension System	Texas Municipal Retirement System
Los Angeles Water and Power Employees' Ret. Plan	Texas Teacher Retirement System
Marin County Employees' Retirement Association	Vermont Pension Investment Committee
Maryland, State Retirement Agency	Washington State Investment Board
Massachusetts Bay Transportation Authority Ret. Fund	West Virginia Investment Management Board
Massachusetts PRIM	Wisconsin State Investment Board
Milwaukee Employees' Retirement System	

Table 2: U.S. public pensions included in broad-based review

Appendix III. In-Depth Case Studies

This appendix contains 11 in-depth case studies providing more-integrated, coherent examples of how these governance design features come together in actual organizations, and reflect how these attributes contribute or hinder the effectiveness of governance in practice.

These case studies draw on all the data appearing in the broad review, as well as specific details and attributes on:

- Structure: Qualifications of board members; rules on party affiliation; board member compensation; independence from executive and government affiliations; committee membership
- Roles and responsibilities: Delegation of duties to relevant authorities between board, committees and executives, time commitment levels, and degree of board support through staff
- Processes: Board member induction and training, board evaluation, and communication channels

This data was gathered from publicly accessible online information, including organization websites and annual reports. This data was supplemented with interviews with employees and representatives of these selected organizations.

A. CALIFORNIA PUBLIC EMPLOYEES RETIREMENT SYSTEM

Background

The California Public Employees Retirement System (CalPERS) is the largest pension fund in the U.S., managing defined benefit pension and health benefits for approximately 1.5 million state, county, and local public employees and retirees.

CalPERS is relatively analogous to the PBGC in terms of organization type as a state-sponsored independent corporation, and in its primary business function of managing and paying defined benefit pension compensation. Its status as the largest U.S. pension plan (with a current total market value of $252 billion) certainly warrants inclusion. CalPERS also has a record of very competitive performance in terms of investment returns, with

11.8 percent in 2006; 9 percent ten-year annual average. Despite criticism about its political, shareholder-activist nature, CalPERS is arguably the most prominent pension institution in the U.S., with a highly developed organizational and governance model.

Summary of governance features

Governance structure

CalPERS is primarily governed by a Board of Administration, composed of 13 members. Six members are elected by active and retired public employees (pensioners), three members are appointed by California state public officials (Governor and State Legislature), and four members serve in an ex-officio through other California state public offices (State Treasurer, State Controller, Director of the Department of Personnel Administration, and a designee of the State Personnel Board). Six of 13 members of the Board either have significance professional commercial experience in finance, insurance, or law, or formal graduate education in business administration. Board members serve for a term length of four years, with the possibility of re-election.

General board meetings and standing committee meetings each occur monthly. The board has established a committee system to review and report on specific programs, projects, and issues, and to make recommendations to the board. The board is organized into five standing committees: Benefits and Program Administration, Finance, Health Benefits, Performance and Compensation, and Investments. There are also subcommittees for Investment Policy and the R Street project and two ad-hoc committees on Board Elections and Board Governance.

Governance roles and responsibilities

The CalPERS board has a legally bound fiduciary responsibility for asset management and plan administration. "Board of Administration is responsible for the management and control of CalPERS, including the exclusive control of the administration and investment of the Retirement Fund." Specific board responsibilities also include setting employer contribution rates, determining investment asset allocations, and providing actuarial allocations.

The board does not have the authority to add, change, or delete benefits without the concurrence of the California state legislature. However, the board has the power to designate any of its decisions on interpretation of retirement law as a "precedential decision" which the CEO is delegated authority to implement, and is not subject to rulemaking or judicial review. Because CalPERS is responsible for administering California state retirement law and other government benefit codes, the Board of Administration is responsible for resolving disputes over the interpretation of these laws.

Responsibility is delegated to CEO for operational management and overseeing implementation of Board's decisions. Professionals in the Investments Office are responsible for implementation of the overall investment strategy and making specific investment transactions.

Governance processes

CalPERS has a history of governance challenges with highly political decision-making, especially with regard to shareholder activism, as well as ethical and economic development-targeted investment screens. However, various control mechanisms have been pre-established to restrict board members from interfering with investment staff in influencing decisions on specific investment transactions: Board communication with investment officers is buffered through the Chief Investment Officer, there is transparency in investment criteria and decision-making, and CalPERS uses fund-of-fund managers. In addition, the state of California oversees an annual external audit of fund management, including a validation of CalPERS' capacity to cover benefit liabilities.

Key Observations

CalPERS' governance model is notable for its clear and fully developed organizational structure. Separation of executive, operational, and control functions occurs through formalized processes for authority delegation (including committees, and separation of board from individual investment transactions, etc.), and transparency and regular reporting, auditing, and controls. Although board composition has a high level of political appointees and politically-affiliated ex-officio representatives, solid governance processes provide checks against conflicts of interest and moral hazard.

Another distinct feature of CalPERS' governance has been its clear aspiration for high performing and cutting-edge investment processes. Strategic goals are clear and ambitious, to reach competitive market returns, and employ/develop best practices in asset management. CalPERS has become "stamp of approval" in capital fundraising and has built a reputation in private external manager selection.

Another distinct governance feature has been in creating a compelling value proposition to attract talent in investment management. As a public corporation with a restrictive government pay scale, CalPERS struggled to attract and retain top talent, but it got a legislative exemption in recent years to ensure more competitive compensation package for investment professionals and fund managers overseeing large pools of assets. In addition, CalPERS is known to offer high responsibility for mid-tenure talented individuals, offering springboard to more lucrative positions.

B. ONTARIO TEACHERS' PENSION PLAN

Background

Ontario Teacher's Pension Plan (OTPP) is an independent Canadian corporation co-sponsored by the Government of Ontario Ministry of Education and Ontario Teachers' Federation, who are jointly responsible for fully funding the plan and setting plan benefits and contribution levels. OTPP is responsible for investing the assets and administering the pensions of Ontario's 271,000 teachers and retired teachers. OTPP was created as it currently stands by the Teachers' Pension Act of 1990.

OTPP is analogous to the PBGC as an independent government corporation and has a similar primary business function of managing and paying defined benefit pension compensation. OTPP is of comparably large size, with $106 billion net assets as of 2006. OTPP is also a particularly high-performing organization, largely in terms of fulfilling its mission of obtaining high investment returns (16 percent in 2006, 15.7 percent four-year average). In addition, industry experts recognize OTPP as a leader within the Canadian pension system in demonstrating best practices in organizational governance.

Summary of governance features

Governance structure

OTPP is primarily governed by a board of nine members. The Government of Ontario and Ontario Teachers' Federation each select four members and then jointly select the board chair. All board members are independent: they are non-executive and are not employed by nor are formal representatives of the Ontario government. The board is composed of individuals with a high concentration of commercial experience and skills, with eight of nine current members possess significant management expertise in finance, investments, business, and accounting. Board member term length is two years, and members can serve a maximum of four consecutive terms.

The board holds ten scheduled meetings and several special meetings a year. The board is organized into five committees: Investment, Audit and Actuarial, Benefits Adjudication, Governance, and Human Resources and Compensation.

Governance roles and responsibilities

The board has stated responsibility to "administer the pension plan, manage the pension fund, and pay members and their survivors the benefits promised" and has the obligation to exercise "the same prudence expected of a person dealing with another's property." Specific investment responsibilities include annually reviewing investment strategy and long-term asset-mix policy and rewarding investment managers for achieving periodic performance targets However, the board delegates day-to-day administration and investment management to executive staff, including the responsibilities of setting annual corporate objectives and long-term business strategies.

Governance processes

To ensure that the board is fully engaged, informed, and capable to provide quality oversight, board members periodically consult with external advisors and experts on investment management, compensation management, or other general topics. New board members participate in an orientation, including seminars or specific technical workshops for education on financial topics, such as actuarial valuation of liabilities and the use of derivative contracts.

To ensure accountability, the Audit and Actuarial Committee consults directly with the internal and external auditors and the independent actuary and reviews auditors' assessments of internal controls. The Governance Committee reviews board performance through self-evaluation surveys and written questionnaires of board and committee effectiveness. Compliance is enforced with a Code of Business Conduct to manage conflicts of interest.

Key Observations

OTPP's governance model is notable for its board member selection process that ensures independence and alignment of interests in oversight. Government and labor interests are represented through the board appointment process, without having officially affiliated representatives that provide direct organizational oversight as actual board members. In fact, board members have the fiduciary responsibility to act independently of the interests of the respective plan sponsors that appointed them. In place of special interests, selection guidelines focus on creating board composition that reflects relevant and complementary professional and commercial expertise.

In addition, the OTPP governance model is notable for its formalized processes that support good governance in practice. Orientation, training, and frequent briefings ensure an adequate level of board-member engagement and knowledge for proper oversight. Board processes create expectation and measurement for board accountability and performance.

C. FEDERAL DEPOSIT INSURANCE CORPORATION

Background

The FDIC is a U.S. government corporation that insures deposits in banks and thrift institutions up to $100,000, currently insuring more than $3 trillion in deposits. The FDIC is the primary regulator of state-chartered banks not under the Federal Reserve System and currently examines and supervises about 5,250 banks and savings banks, which are more than half of the institutions in the entire banking system. The FDIC receives no Congressional appropriations: It is wholly funded by risk-based insurance premiums paid by banks and thrift institutions, as well as earnings on investments.

FDIC is analogous to PBGC because FDIC is a U.S. government corporation, it is an insurer of financial institutions, it has experienced a governance transition with board expansion occurring with FIRREA legislative changes in 1989, and it is large (with $50.7 billion in assets and nearly $49 billion in its insurance fund as of 2006).

The FDIC is also an ideal case study as a relatively high performing organization in fulfilling its mission of maintaining stability and insuring confidence in the nation's banking system. In its latest 2006 financial report, the FDIC reported that under its supervision, it has gone 31 months without the failure of an FDIC-insured institution, the longest period in its 73-year history.

Summary of governance features

Governance structure

The FDIC is primarily governed by a Board of Directors, composed of five members[53], including three full-time members and two ex-officio members who serve as Comptroller of the Currency and Director of the Office of Thrift Supervision in the Treasury Department. All board members are appointed by the President and confirmed by the Senate. A maximum of three board members may be of the same political party. A professional requirement exists that at least one member must have state bank supervisory experience. The three full-time board members serve a term length of six years, while the Chairman serves a term length of five years (ex-officio term lengths depend on tenure of the other position). The three full-time board members are compensated according to the Government Schedule (GS) pay scale.

The board typically meets at least once a month, with an average of seven to eight open meetings a year. Governance and board oversight is organized through three standing committees: Audit, Assessment Appeals, and Supervision Appeals Review. Board members serve as chairs of these committees, with full-time staff for activity oversight and issue coverage. The FDIC Chairman and board can establish advisory committees, covering such topics as Banking Policy and Economic Inclusion.

Governance roles and responsibilities

The board is primarily responsible for administering the Federal Deposit Insurance Act and numerous other laws related to insurance, regulation, and supervision of depository institutions. The Chairman assumes the general role and responsibilities of Chief

Executive Officer. The Chairman "shall manage and direct the daily executive and administrative functions and operations of the Corporation, and shall otherwise have the general powers and duties usually vested in the office of the chief executive officer of a corporation." Along with the two other full-time board members, the Chairman works closely with the executive team to monitor organizational performance and guide strategy.

FDIC's bylaws explicitly outline strict delegation of authority between the board, Director of Division of Supervision and Consumer Protection, Deputy Director, Assistant Directors, and Field Supervisors (Risk Management). These responsibilities include the ability to: approve, deny, and investigate deposit insurance applications and filings; investigate and intervene in the activities of state banks; and take corrective or enforcement actions. The board retains authority to act or issue final orders (including denial) on applications for federal deposit insurance or any filing or enforcement matter. Otherwise, the board delegates authority to committees or other FDIC officials. With the Federal Deposit Insurance Act of 2006, the board has more flexibility to manage the Deposit Insurance Fund and is permitted to price deposit insurance according to risk.

Governance processes

The Inspector General is responsible for audit and investigative activities, reports to the Chairman, and keeps the board informed on issues or problems related to administration, operations, or fraud.

Key observations

FDIC's governance model is distinct in the board's level of balance and independence. The three primary members are full-time, such that they are not employed or formally affiliated with another federal body. Their majority non-governmental independence counterbalances the ex-officio representation of the two Treasury officials, who notably are Bureau heads (not cabinet-level positions), dedicate due attention to FDIC oversight through frequent board meeting attendance, and they are expected to act in interest of FDIC, not their respective organizations. To further promote independence and manage conflicts of interest, no board member may be an officer or director of any insured depository institution or holding company, the Federal Reserve Bank, or Federal Home Loan Bank. Also, there is an effort to balance partisanship by the requirement that no more than three members be of the same political party.

Another notable aspect of FDIC governance is the emphasis on continuity, played in large part by the role of career executives and support staff. Six board staff members are dedicated to supporting the three full-time board members. In addition, the staggered six-year and five-year term length of board members and Chairman, respectively, promotes continuity by not perfectly coinciding with changes from one presidential administration to the next. The lead career executive, the Chief Operating Officer, plays a large role in maintaining strategic and operational direction, and managing a strong governance process to support continuity and institutional knowledge transfer when board member turnover does occur. Competitive compensation for executive and middle management, outside of the Government Schedule (GS) pay scale also helps to attract and retain talent in staff.

D. PENSION PROTECTION FUND

Background

The Pension Protection Fund (PPF) in the United Kingdom is an independent government corporation created by the Pensions Act of 2004. PPF serves as a guarantor of private pension schemes. Its main function is to provide compensation for beneficiaries of defined benefit pension plans that have become insolvent, or when an employer's assets are insufficient to cover pension liabilities. Its strategic objectives are to "pay the right people the right compensation at the right time", to promote confidence in pensions while maintaining the financial solvency of the organization, and to invest assets effectively. The PPF is financially self-sufficient; it is wholly-funded by risk-based levies (premiums) it charges to plan sponsors. The PPF currently insures 7,800 pension schemes with approximately 12.5 million members.

PPF is essentially the British equivalent of the PBGC. It is highly analogous in terms of its organizational type as an independent government corporation and has the exact same primary business function as a guarantor of private defined benefit pensions plans. Admittedly, it operates somewhat differently under the U.K. system, is a relatively new organization, having been created in 2004, and is significantly smaller in size (£4.4 billion assets under management, as of 2006). The PPF has a strategy and mission that is explicitly focused on achieving high performance and adhering to good governance practices.

Summary of governance features

Governance structure

The PPF is primarily governed by the Board of the Pension Protection Fund, composed of 11 members. The Board includes a chair, seven independent (non-executive) members, the Chief Executive Officer, and two additional executives. The Secretary of State for Work and Pensions selects the chair, who then with the assistance of professional executive search consultants selects the rest of the board members through an open, public selection process. Board members serve for terms of three years and can serve a maximum of two terms. Consistent with its strategy of creating a high-performing and well-managed independent corporation, the PPF board has a high composition of individuals with professional management and commercial experience. Nine of 11 current members of individuals possess professional finance experience and expertise as asset management, pension consultants, and attorneys. The board is composed of no government officials or affiliates; in addition, the organization is structured entirely separate from the Pension Regulator (tPR), which externally maintains all regulatory authority over pension schemes.

The board meets at least once a month. Non-executive members receive annual compensation £15,300 based on estimated time commitment 20 days of work.

Board oversight is organized through a system of six committees: Audit, Decision, Investment, Non-Executive, Reconsideration, and Renumeration. Some committees have specific requirements about level of (non-executive) independence or financial expertise of membership. The most active committee is the Investment Committee, which develops investment principles and a strategic approach to investments, risk management, and asset liability matching.

Governance roles and responsibilities

The board is responsible for overseeing payment of pension compensation, calculating annual levies, and setting investment strategy of the fund. Notably, PPF's founding statute grants the board underwriting flexibility to set risk-based levies, with the purpose of ensuring the financial solvency of the organization. Its Statement of Operating Principles notes clear delegation of board authority to set strategic direction and organize its oversight through committee roles, but it has a formal Schedule of Delegated Powers that delegates all operational decisions and general powers to executive management.

Processes

For evaluative purposes, the board's chair annually reviews board performance and governance. PFF is also accountable and must submit annual reports to Parliament, through the Secretary of State for the Department for Work and Pensions. Audits are conducted by governmental and external private bodies. Full disclosure is made of board member meeting attendance and voting record, as well as external affiliations and mitigated conflicts of interests. Board and management both focus on a high level of transparency and communication. For instance, PPF actively and frequently engages with both industry and labor stakeholders to gain feedback, build consensus, and foster public-policy debate when setting pension protection policies.

Key observations/notable governance attributes

The PPF governance model is distinct for its clarity and direct alignment between the organization's mission and strategic objectives, the board's responsibilities and duties, and the composition and qualification of board members. Specifically, nine of 11 board members have professional expertise in pension benefits, insurance, underwriting, finance, and investments. This background enables them to successfully fulfill the board's duties of overseeing pension payment, calculating levies, and managing investments, with the purpose of ensuring that the PPF successfully achieves its mission and strategic goals of operational efficiency of pension payment, being financially solvent, and investing assets effectively. In particular, the board's ability to set risk-based levies (premiums) ensures the organization's financial solvency and ability to respond appropriately to changes in market trends and increased risk profiles of defined benefit pension plans.

Another distinct feature of PPF governance is the large, independent board. Given that seven of the Board members are non-executive, and all members have no governmental employment or affiliation, PPF operates at arm's length from political or special interests. Furthermore, government only selects the chair of the board, who then selects the rest of the board through a highly professional, transparent, relatively apolitical process using executive search consultants. In addition, the role of the Pension Regulator (tPR) is entirely separate, so as to further promote independence, and mitigate conflicts of interest or moral hazard.

E. NATIONAL RAILROAD RETIREMENT INVESTMENT TRUST

The National Railroad Retirement Investment Trust (NRRIT) is an independent U.S. government entity formed in 2001 to manage the retirement assets of U.S. railroad workers. By year-end 2006, those assets were $29 billion. A separate U.S. agency, the Railroad Retirement Board (RRB) determines who is eligible for benefits and the levels of those benefit payments.

The NNRIT has a board of trustees composed of seven members. Three of these members are appointed by major labor unions, and three are appointed by major railroad companies. These six members then choose a seventh, who is typically an executive with substantial experience in pensions. These seven members are not U.S. government employees, since NNRIT is fully independent of the government. Board members serve for staggered three-year terms.

Members of the Board of Trustees shall be appointed only from among persons who have experience and expertise in the management of financial investments and pension plans. No member of the Railroad Retirement Board shall be eligible to be a member of the Board of Trustees.

The legislation that established the NNRIT was explicit about the duties of the board members: "The Trust and each member of the Board of Trustees shall discharge their duties (including the voting of proxies) with respect to the assets of the Trust solely in the interest of the Railroad Retirement Board and through it, the participants and beneficiaries of the programs funded under this Act."[54]

The board has an Audit Committee and an Administrative Committee. The Audit Committee meets four times per year, to cover perennial issues like reviewing the financial position of the trust and performing one-off investigations, like an taking an inventory of risks faced by the NNRIT.

F. OVERSEAS PRIVATE INVESTMENT CORPORATION

Background

The Overseas Private Investment Corporation (OPIC) is a U.S. government corporation that supports international business investment and economic development through financing (direct loans and loan guarantees), political risk insurance, and investment funds (including private equity capital), particularly in emerging markets without established financial institutions.

OPIC is analogous to the PBGC in organizational type as a government corporation and guarantor of private sector enterprises. Relative to PBGC, OPIC has a different regional and business focus and is smaller (with only $6.3 billion in assets as of 2006).

Summary of governance features

Governance structure

OPIC is primarily governed by a board of directors composed of 15 members. All members are appointed by the U.S. President and confirmed by the Senate. The chair of the board is also the President and CEO. Seven board members serve in an ex-officio capacity through other departmental positions: the Deputy U.S. Trade Representative; Deputy Secretary of Commerce; Deputy Secretary of Labor; Under Secretary of State for Economic, Business, and Agricultural Affairs; Under Secretary of Treasury for International Affairs; and U.S. Director of Foreign Assistance for USAID. Eight board members are from the private sector and are wholly independent (non-executive and non-governmental officials), two of which must be experienced in small business, one of which must represent organized labor, and another must have experience in cooperatives. Board member term length is three years. The board meets four times a year. The OPIC board has one standing Audit Committee, but it may establish additional committees as needed.

Governance roles and responsibilities

Board is responsible for providing policy guidance to the corporation and approves all major insurance, project financing, and investment-fund projects.

Key Observations

The OPIC governance model is notable for having a relatively large board that has balance of both governmental and non-governmental members who represent a diverse set of stakeholders and experience, in trade, business, labor, and international development policy. A minority of members are ex-officio representatives, and the Chairman and CEO is the only executive member on the board. Therefore, there is a relatively moderate level of independence, combined with the fact that government representation is split equally between six agencies.

G. TENNESSEE VALLEY AUTHORITY

Background

The Tennessee Valley Authority (TVA) is a U.S. government corporation and the nation's largest public power company. Through 158 locally owned distributors, TVA supplies power to about 8.7 million residents of the Tennessee Valley, including sections of Alabama, Georgia, Kentucky, Mississippi, North Carolina, Tennessee, and Virginia. TVA was created in 1933, and now fulfills a three-pronged mission, focusing on "improving the quality of life in the Tennessee Valley through the interrelated parts of its mission: energy, environment, and economic development." More specifically, its strategic goals are to provide reliable and affordable source of power, promote environmental stewardship in land and water use, and support local economic development through employment, investment, and tax revenue.

TVA is analogous to the PBGC in organization type as a government corporation and of comparably large size, with $34.5 billion in assets as of 2006. TVA was a particularly compelling case study given that it experienced its own dramatic governance transformation in 2005. This transformation included a restructuring of the board and modifications to the board's role.

Summary of governance features

Governance structure

TVA is primarily governed by a board of directors composed of nine members.[55] All members are appointed by the U.S. President and confirmed by the Senate. The board elects the Chairman among its own appointed membership and also selects the TVA's President and Chief Executive Officer. All members must be independent: They cannot be TVA employees or executives or governmental representatives. At least seven must be legal residents of the TVA service area. TVA has explicit qualification requirements for members: They must have management expertise within a large for-profit or nonprofit corporate, government, or academic structure. There is a high level of professional and commercial composition on board: Five of the nine current board members have had careers in business, finance, or energy.

Members serve for five-year terms. Board members are compensated $45,000 for time commitment. The board chair gets an additional $5,000. The board is organized into seven committees: Audit and Ethics; Community Relations; Corporate Governance; Environment and Safety; Finance; Operations; and Strategy and Rates.

Governance roles and responsibilities

Board members are responsible for upholding TVA corporate objectives to be a "national leader in technological innovation, low-cost power, and environmental stewardship." The board provides general strategic guidance and independent oversight, sets corporate policies, and approves annual budget. The board delegates ongoing operational management and strategic implementation to executive management.

Governance processes

TVA's Inspector General (IG) conducts ongoing audits of TVA's operational and financial matters in accordance with government auditing standards, including SEC, IRS, and state commission filings. The board has established a Disclosure Control Committee to develop, maintain, and amend as necessary a Disclosure Control Policy and an Information Certification Policy. For instance, board members must disclose any investment or financial interest in the energy industry if it might create a conflict of interest in their position.

Key Observations

TVA's governance model is notable for its emphasis on independence and performance, largely due to the significant governance transformation it underwent in 2005-2006. The change from three executive members to nine non-executive members largely was an effort to make the board more independent from management and to formalize the professionalism of the board. In addition, TVA moved off government pay scales, giving

TVA more flexibility to attract talent, particularly utilities executives from the private sector. This infusion of talent helped TVA to become more competitive in the highly privatized utilities market.

H. UNITED STATES POSTAL SERVICE (USPS)

Background

The United States Postal Service (USPS) is a U.S. government corporation that delivers more than 213 billion pieces of mail every year, to more than 300 million people in 146 million homes in every state, city, and town in U.S. and its territories. USPS is a largely self-sustaining independent agency that funds itself from revenue from the sale of postage and mail delivery products.

USPS is analogous to the PBGC because USPS is a U.S. government corporation, has large-scale retail operations, and is large, with annual total revenue of $73 billion. In addition, the USPS experienced its own governance transition with a re-structuring of its board in 2006 after the Postal Accountability and Enhancement Act.

Summary of governance features

Governance structure

USPS is primarily governed by a Board of Governors, composed of 11 members. Nine independent (non-executive, non-government employed) board members are appointed by the President and approved by the Senate. Those nine members select the Postmaster General, who serves as the Chief Executive Officer, and those ten members then select the Deputy Postmaster General, who serves as the Chief Operating Officer.

Statutory requirements mandate that not more than five of the nine board members may serve from the same political party. Professional requirements were added to board selection in the Postal Accountability and Enhancement Act of 2006, which stated that board members must be selected solely on basis of experience in the field of public service, law, or accounting, or management in large private or public corporations. At least four members must have management experience in corporations with more than 50,000 employees. Seven of eleven current board members have significant private sector.

The nine independent board members serve seven-year staggered terms and cannot serve more than two terms. The two executive members serve indefinite terms, at the pleasure of the board. Each board member receives an annual salary of $30,000 and $300 per day of service, with a maximum of 42 days per year.

The board meets on a "regular basis." All board meetings are open unless the board votes otherwise. A full-time secretary serves as the primary assistant assigned to the board. The board is organized into four committees: Audit and Finance, Capital Projects, Compensation and Management Resources, and Governance and Strategic Planning.

Governance roles and responsibilities

The board is responsible for directing and controlling the budget, monitoring operations, conducting long-term strategic planning, setting policy, overseeing capital projects, and approving executive compensation.

Governance processes

The USPS Office of the Inspector General (OIG) is an independent agency that employs and oversees auditors and reports directly to the USPS board.

Key observations

The USPS governance model is notable for its focus on professional management. Because of large operational challenges and complexities of the organization, the 2006 legislation required that board members have demonstrated ability in managing organizations or corporations of substantial size. Compensation for board members enables USPS to attract talent to the board, while also solidifying the expectation of a significant time commitment by board members.

Another distinct feature is the high level of independence of the board. Non-executive board members comprise the majority of the board and together select the CEO and COO, ensuring a high level of independent oversight of executive management. Furthermore, board members are not federal government employees. The partisan cap on appointed Governors also ensures a balance of interests.

I. GOVERNMENT NATIONAL MORTGAGE ASSOCIATION

Background

The Government National Mortgage Association (GNMA) or "Ginnie Mae" is a U.S. government corporation created within the Department of Housing and Urban Development. Ginnie Mae serves as a "full faith and credit" guarantor of investments in mortgage-backed securities (MBS) backed by federally insured or guaranteed loans, including loans issued by the Federal Housing Administration, Department of Veterans Affairs, Rural Housing Service, and the Office of Public and Indian Housing targeted at low- and moderate-income borrowers. Ginnie Mae seeks to increase the liquidity of mortgage investments and to support affordable mortgage pricing in the secondary market. Its mission is "to expand affordable housing in America by linking global capital markets to the nation's housing markets." To meet these objectives, Ginnie Mae works closely with mortgage issuers and investors.

Like PBGC, Ginnie Mae is a government corporation, is a guarantor of financial products, and works closely with industry stakeholders. Although Ginnie Mae is significantly smaller than PBGC ($13.7 billion in total assets as of 2007), it presents a unique governance model as a government corporation that is closely connected with a departmental agency.

Summary of governance features

Governance structure

Ginnie Mae is primarily governed under Secretary of Housing and Urban Development (HUD) but is managed by a President. Ginnie Mae has no board. The President of Ginnie Mae is appointed by the U.S. President and approved by the Senate. The entire executive team, including Senior Vice Presidents of Management Operations, Finance, Mortgage Backed Securities, and Capital Markets, are all selected by the HUD Secretary.

Governance roles and responsibilities

The Secretary of HUD is primarily responsible for the general supervision and direction of Ginnie Mae, including the determination of all general policies. "All powers and duties shall be vested in the HUD Secretary and the Association shall be administered under the direction of the Secretary."

Governance processes

An external party conducts an annual audit and the auditor's report is submitted to Congress. In 2007 the external audit identified that Ginnie Mae had significant deficiencies in compliance and control in monitoring of issuers, risk management, and independent management control processes.

Key Observations

Ginnie Mae's governance model is notable for the high level of dependence on the Department of Housing and Urban Development. The HUD Secretary provides supervision and guidance, which is then carried out by executive team. With no board, there is minimal administrative or policy independence, and recent external audit reports reveal that risk management and governance control processes might be inadequate to meet economic volatility, particularly in the subprime mortgage market.

J. FEDERAL HOME LOAN MORTGAGE CORPORATION

Background

The Federal Home Loan Mortgage Corporation (Freddie Mac) is a government-sponsored enterprise (GSE) and stockholder-owned corporation that provides stability in the secondary mortgage market by increasing liquidity of mortgage investments and distributing investment capital for residential mortgage financing.

As a GSE, Freddie Mac is relatively a private corporation with ties to the government, like PBGC. Both organizations are also guarantors of financial obligations of other companies, and both are very large.

Summary of governance features

Governance Structure

Freddie Mac has a board of directors composed of up to 18 members. Thirteen members are elected by shareholders. Five members may be appointed by the U.S. President, but the current President has opted not to appoint any board members. A "substantial majority" must be external and independent. Board members elect the board chair, which has historically been the Chief Executive Officer. If the CEO is board chair, there is a lead independent director to provide non-executive oversight. Freddie Mac's board is committed to separating the roles of board chair and CEO "within a reasonable period of time." Any stockholder can nominate a candidate for selection to the board. These nominees are vetted by the Governance Committee of the board.

The current board has a high level of professional expertise and experience, including finance (investment and banking), law, finance, accounting, economics, and academia. Of the five board members available for Presidential appointment, candidates must include experience in homebuilding, mortgage lending, or real estate.

Members serve for a term length of only one year and can be re-elected up to ten years total service. Board members are compensated with an annual cash retainer of $60,000. They also receive equity in the company and additional compensation for each meeting they attend.

The board is organized into five committees: Audit; Compensation and Human Resources; Finance and Capital Deployment; Governance, Nominating, and Risk Oversight; and Mission, Sourcing and Technology. Each committee must be chaired by an independent (non-executive) board member.

Governance roles and responsibilities

Board members are asked "to promote the fulfillment of Freddie Mac's public mission, the Company's safety and soundness, and the interests of the Company's stockholders, through their oversight of Freddie Mac's business."

Governance processes

Freddie Mac has processes for supporting board member knowledge, including orientation and trainings. Freddie Mac has a director orientation and continuing education program that is overseen by the chair of the board. This includes individual briefings by management and written materials on such issues as business strategy, risk management, and corporate governance. Board members are frequently briefed by experts on relevant topics. In addition, there are processes to evaluate and measure board performance. The Governance, Nominating, and Risk Oversight Committee evaluates Board policies, procedures, and level of information. Standing committees also evaluate themselves on an annual basis.

Key Observations

Board members are specifically instructed to act in interest of Freddie Mac. The board achieves both accountability and continuity by having short terms lengths for its board members, with re-election for up to ten years.

K. PROCTER AND GAMBLE

Background

Procter and Gamble (P&G) is a Fortune 100 multinational public corporation and producer of wide variety of consumer goods. Its revenue is the 25th largest amongst U.S. companies.

P&G is a traditional private sector organization. P&G is a compelling case study because of its size, prominence, and reputation for strong corporate governance.

Summary of governance features

Governance Structure

P&G is governed by a board composed of 10-15 members. The majority of board members must be independent, i.e., not executives and without any material relationship to the company. The chair is elected by the non-executive board members. If the chair is the Chief Executive Officer, then there must be a non-executive member who serves as presiding director and who leads executive sessions and oversees executive performance.

Board members are selected based on (a) their ability to represent the interests of shareholders, (b) expertise in strategy, policy-setting, and management; (c) ability to meet time commitment; and (d) lack of conflicts of interests. Board members must remove themselves from discussions and votes that affect their personal or business interests.

Board member term length is three years, with a maximum of six terms. The board meets seven times a year. It focuses on frequent and substantive oversight of critical business issues, including annual review of executive performance and succession planning. Attendance is expected at all meetings. If a board member attends less than 75 percent, that board member will be reviewed by board chair and the Governance & Public Responsibility Committee. Board members are compensated for their time commitment.

The board has five committees: Audit; Compensation & Leadership Development; Finance; Governance & Public Responsibility; Innovation & Technology. Committees have specific participation requirements about number of independent, non-executive membership.

Governance roles and responsibilities

According to P&G policies, the "board represents and acts on behalf of all shareholders of the Company. The board is responsible for establishing, and helping the Company achieve, business and organizational objectives through oversight, review and counsel." Other board responsibilities include approving and monitoring corporate strategy; monitoring and managing risks; selecting, evaluating, and determining compensation for the Chief Executive Officer and executive management.

Governance processes

P&G has formalized processes for orientation and continuing education for Board members on relevant topics.

Key Observations

The P&G governance model is notable for having a highly balanced, professional, and high-performing board. The board achieves balance and alignment of interest through rigorous shareholder election, which includes screening for conflicts of interest. The shareholder election process specifically seeks a high caliber of talent, management experience, and integrity and ethics. P&G conducts frequent elections to ensure continued performance. Independent oversight of executive management and operational performance is ensured through position of Presiding Director in the event that board chair is the CEO. A majority of board members are not company executives, so the board is well-equipped to independently fulfill its primary responsibility of selecting, evaluating, and determining compensation for executive officers.

Appendix IV. A Governance Matrix

Table 3 depicts a sample of a governance matrix that would show, for each major activity or decision, who ultimately Decides (D), Approves (A), is responsible (R), and (S) supports the execution. The first two rows are completed as an example.

	Chair	Board	Committee	CEO	Dep. Director	Chief Ins. Off.	CFO	General Counsel	Inspector General	Staff
Shape mission and strategic direction		D		S						S
Set board meeting agenda	D			S						S
Call for board meeting										
Set corporate strategy										
Check management plans										
Plan for response to changing contexts										
Set targets for the enterprise										
Change board bylaws										
Change regulations										
Change governance process										
Decide policy in major plan terminations										
Take action impacting >x% of beneficiaries										
Suggest legislative changes										
Set benefits and coverage levels										
Appoint senior management										
Set budget										
Craft Investment Policy Statement										
Set premium levels										
Authorize issuance of debt										
Review management performance										
Appoint Advisory Committee members										
Delegate board-member responsibilities										
Select asset managers										
Determine board-level communications										
Oversee financial statements										
Plan sufficiency										
Ensure timeliness of benefit distribution										

	Chair	Board	Committee	CEO	Dep. Director	Chief Ins. Off.	CFO	General Counsel	Inspector General	Staff
Send plan termination notices										
Manage risks										
Draft annual management reports										
Create and monitor performance metrics										
Assess executive performance										
Assess board performance										
Ensure ethical standards										
Review reports from Inspector General										
Manage conflicts of interest										

Table 3: Sample governance matrix

---

[1] GAO-07-808: Pension Benefit Guaranty Corporation, Governance Structure Needs Improvements to Ensure Policy and Direction Oversight.

[2] Title 29, Chapter 18, Subchapter III, Subtitle A. Section 1302.

[3] ERISA specifically states that the U.S. government is not obligated to pay PBGC obligations.

[4] 2007 PBGC Annual Management Report; http://www.pbgc.gov/about/annreports.html

[5] Title IV, Section 411 of the PPA, which amends Title IV of the Employee Retirement Income Security Act of 1974 (29 U.S.C. 1301 et seq.)

[6] GAO-07-808: Pension Benefit Guaranty Corporation, Governance Structure Needs Improvements to Ensure Policy and Direction Oversight.

[7] http://www.otpp.com/web/website.nsf/web/planoverview

[8] http://www.otpp.com/web/website.nsf/web/code_1/$FILE/Code_1.pdf

[9] Railroad Retirement and Survivors' Improvement Act, section 105.

[10] These are the Deputy U.S. Trade Representative; Deputy Secretary of Commerce; Deputy Secretary of Labor; Under Secretary of State for Economic, Business, and Agricultural Affairs; Under Secretary of Treasury for International Affairs; and U.S. Director of Foreign Assistance for USAID.

[11] http://www.freddiemac.com/governance/pdf/gov_guidelines.pdf

[12] PriceWaterhouseCoopers, "What Directors Think?" 2005 ; Korn/Ferry International, *31st Annual Board of Directors Survey.* 2005.

[13] Korn/Ferry International, *32nd Annual Board of Directors Survey.* 2006.

[14] Delbecq, Andre "Role Conflict in Administered Systems," Proceedings of the 9th Annual Midwest Academy of Management Conference, Bureau of Business Research, Southern Illinois University, 1968.

[15] Yermack, David, Higher market valuation of companies with a small board of directors. *Journal of Financial Economics*, Vol 40, Issue 2, Feb 1996, pp. 185-211.

[16] Korn/Ferry International, *31st Annual Board of Directors Survey.* 2005.

[17] The Business Roundtable, "Principles of Corporate Governance." November 2005.

[18] The Conference Board, *Corporate Governance Handbook.* 2007, p. 23.

[19] National Association of Corporate Directors ("NACD"), *Report of The National Association of Corporate Directors Blue Ribbon Commission on Director Professionalism.* 2005.

[20] Korn/Ferry International, *32nd Annual Board of Directors Survey.* 2006.

21 Korn/Ferry International, 32nd Annual Board of Directors Survey. 2006.

[22] The Business Roundtable, *Principles of Corporate Governance.* November 2005.

[23] Deweiler, Donald J. and Sandra G. Selzer, "Scope of Directors' Fiduciary Duties to Creditors." *American Bankruptcy Institute Journal*, Jul/Aug 2007.

[24] The Conference Board, *Corporate Governance Handbook.* 2007.

[25] NYSE/Euronext Corporate Governance Guidelines. 2007.

[26] Korn/Ferry International, *32nd Annual Board of Directors Survey.* 2006.

[27] Felton, Bob, and Wong, Simon, "How to Separate the Roles of Chairman and CEO" *McKinsey Quarterly,* 2004, Number 4.

[28] Korn/Ferry International, *31st Annual Board of Directors Survey.* 2005.

[29] The Conference Board, *Corporate Governance Handbook.* 2007.

[30] The Business Roundtable, *Principles of Corporate Governance.* November 2005.

[31] Frederic W. Cook & Co., Inc., *2002 Board of Directors Profile And Compensation At NASDAQ-100 Companies.*

[32] For organizations where term length data was available.

[33] McKinsey & Company, "The State of the Corporate Board, 2007." *McKinsey Quarterly*, June 2007.

[34] Council of Institutional Investors, *Corporate Governance Policies.* December 18, 2006.

[35] http://www.pensionprotectionfund.org.uk/statement_of_operating_principles.pdf

[36] The Business Roundtable, *Principles of Corporate Governance.* November 2005; The Conference Board, *Corporate Governance Handbook.* 2007; National Association of Corporate Directors ("NACD"), *Report of The National Association of Corporate Directors Blue Ribbon Commission on Director Professionalism.* 2005.

[37] Nadler, David A., "Building Better Boards." *Harvard Business Review,* May 2004.

[38] PriceWaterhouseCoopers, "What Directors Think?" 2005; Korn/Ferry International, *31st Annual Board of Directors Survey.* 2005.

[39] Korn/Ferry International, *31st Annual Board of Directors Survey.* 2005.

[40] American Bar Association, Report of the American Bar Association Task Force on Corporate Responsibility. March 31, 2003, pp. 71.

[41] Council of Institutional Investors, *Corporate Governance Policies.* December 18, 2006.

[42] Korn/Ferry International, *31st Annual Board of Directors Survey.* 2005.

[43] Council on Foundations, "Recommended Best Practices in Determining Reasonable Executive Compensation: A Guidance Memorandum from the Board of Directors of the Council on Foundations." December 6, 2002.

[44] http://www.nacdonline.org/

[45] PriceWaterhouseCoopers, "What Directors Think?" 2005; The Business Roundtable, Corporate Governance Survey Key Findings—October 2007. October 22, 2007; University of Southern California, Heidrick & Struggles, 10th Annual Corporate Board Effectiveness Study, 2006-2007.

[46] PriceWaterhouseCoopers, "What Directors Think?" 2005.

[47] Korn/Ferry International, *32nd Annual Board of Directors Survey.* 2006.

[48] PriceWaterhouseCoopers, "What Directors Think?" 2005.

[49] Frederic W. Cook & Co., Inc., *2002 Board of Directors Profile And Compensation At NASDAQ-100 Companies.*

[50] University of Southern California, Heidrick & Struggles, 10th Annual Corporate Board Effectiveness Study, 2006-2007.

[51] ERISA, 29 USC 18 § 1302(a)(1-3).

[52] See page 27.

[53] The FDIC Board used to be composed of three members, but with the FIRREA legislation of 1989 following the savings and loans crisis, the FDIC assumed additional responsibility, and the board was expanded to five members.

[54] Railroad Retirement and Survivors' Improvement Act, section 105.

[55] Previously the board of TVA was composed of three board members, each appointed for a nine-year term, and who also served as the Chief Executive Officer and executive team. However, the Consolidated Appropriations Act of 2005 restructured the board to its current expanded form, with nine part-time members. This legislation also separated the role of Chairman and CEO, added professional qualifications and TVA residency requirement, and removed statutory government scale salary cap for employees. The effort was spearheaded by the Tennessee delegation of the U.S. Congress.

Presidential Documents

Memorandum of February 1, 2013

Designation of Officers of the Pension Benefit Guaranty Corporation To Act as Director of the Pension Benefit Guaranty Corporation

Memorandum for the Director of the Pension Benefit Guaranty Corporation

By the authority vested in me as President by the Constitution and the laws of the United States of America, including the Federal Vacancies Reform Act of 1998, 5 U.S.C. 3345 *et seq.* (the "Act"), it is hereby ordered that:

Section 1. *Order of Succession.* Subject to the provisions of section 2 of this memorandum, and to the limitations set forth in the Act, the following officials of the Pension Benefit Guaranty Corporation, in the order listed, shall act as and perform the functions and duties of the office of Director of the Pension Benefit Guaranty Corporation (Director) during any period in which the Director has died, resigned, or is otherwise unable to perform the functions and duties of the office of Director:

(a) Chief Management Officer;

(b) Chief Operating Officer;

(c) Chief Financial Officer; and

(d) General Counsel.

Sec. 2. *Exceptions.* (a) No individual who is serving in an office listed in section 1 of this memorandum in an acting capacity, by virtue of so serving, shall act as the Director pursuant to this memorandum.

(b) No individual listed in section 1 of this memorandum shall act as Director unless that individual is otherwise eligible to so serve under the Act.

(c) Notwithstanding the provisions of this memorandum, the President retains discretion, to the extent permitted by law, to depart from this memorandum in designating an acting Director.

Sec. 3. *Prior Memorandum Superseded.* This memorandum supersedes the President's Memorandum of December 9, 2008 (Designation of Officers of the Pension Benefit Guaranty Corporation to Act as Director of the Pension Benefit Guaranty Corporation).

Sec. 4. *Judicial Review.* This memorandum is not intended to, and does not, create any right or benefit, substantive or procedural, enforceable at law or in equity by any party against the United States, its departments, agencies, or entities, its officers, employees, or agents, or any other person.

Sec. 5. *Publication.* You are authorized and directed to publish this memorandum in the *Federal Register.*

THE WHITE HOUSE,
Washington, February 1, 2013.

[FR Doc. 2013–02855
Filed 2–5–13; 11:15 am]
Billing code 7709–01