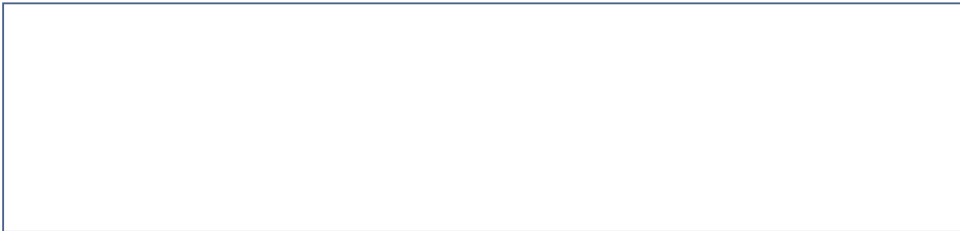




**29th Annual  
Board of Directors Study  
2002**

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**Emerging Companies**



## Executive Summary

It has been an extraordinarily turbulent year for American companies and their boards, marked by near-unprecedented volatility in investment markets, sharp erosion of investor confidence, heightened focus on the validity and credibility of financial reporting practices, and high-profile corporate failures such as Enron and Worldcom. In this environment, the board's critical role in overseeing fundamental corporate practices — how effectively that role is being executed and how it can be strengthened — has come under scrutiny as never before.

This publication, a supplement to Korn/Ferry International's *29th Annual Board of Directors Study*, presents responses and findings from survey participants on the boards of Emerging Companies — companies with revenues under \$200 million. The study indicates that these organizations are making long-term progress in efforts to implement board practices for stronger corporate governance — but that some significant gaps still remain..

This year:

- 70 percent of boards have written guidelines on corporate governance, compared with 71 percent of *Fortune* 1000 boards.
- 25 percent of boards formally evaluate the entire board's performance on a regular basis, compared with 37 percent of the *Fortune* 1000; and
- 45 percent of boards have a formal committee that reviews corporate governance processes and board operations, compared with 62 percent of *Fortune* 1000 boards.

While progress is being made regarding corporate governance processes and board evaluation, boards will have to do more — especially in light of new regulatory mandates designed to formalize these processes in the wake of the past year's notable failures of board oversight.

For example, corporate governance rule proposals adopted by the New York Stock Exchange Board of Directors in August state that listed companies must adopt and disclose corporate governance guidelines on management succession and other key processes. Yet our survey of Emerging Companies directors reveals that:

- only 46 percent of boards have a management succession committee or process.

Mandates such as those of the NYSE, with prescriptions for formal governance guidelines, could create issues for the significant percentage of companies that, according to our survey, do not have such guidelines or processes at this time.

The Korn/Ferry Emerging Companies survey also shows that evaluation of individual directors clearly has not yet taken hold as a board practice.

- 77 percent of respondents say that individual directors should be evaluated regularly regarding performance. However:
  - only 12 percent of boards currently conduct such evaluations, and
  - only 30 percent of directors on those boards think that the evaluations are effective.

Boards going forward can anticipate closer examination of how they measure the performance and, ultimately, the effectiveness of directors on behalf of shareholders, as part of the heightened concern over how well boards execute their oversight role.

Other key survey findings include:

- Independence is an essential concern of directors:
  - 77 percent of directors say the former CEO shouldn't sit on the board.
  - 71 percent of directors say the board should hold regular executive sessions without the CEO during board meetings, yet
    - ▲ only 41 percent of boards hold such sessions.
- Directors are spending slightly less time on board matters than their *Fortune* 1000 counterparts. – an average of 13.2 hours per month, or approximately 158 hours annually, compared with 183 hours annually for *Fortune* 1000 companies.
- Most directors (51 percent) say their company's CEO compensation program is effective.
- 50 percent of directors think the majority of a director's compensation should be in stock.
- 54 percent of boards have a requirement that directors own shares of company stock.
- 53 percent of directors would like to see their board become more diverse by increasing its minority representation.

Korn/Ferry's *29th Annual Board of Directors Study – Emerging Companies highlights* provides a comprehensive and illuminating look into the state of board practices at the nation's emerging companies – charting progress made, as well as progress still to be achieved. The publication represents Korn/Ferry's ongoing commitment to generating and sharing timely, practical information from the nation's corporate leaders regarding their efforts to maintain and extend "best practices" for corporate governance.

We hope that you find the study informative and useful, and that it provides you with insight into the key steps that governance programs must take to address today's pressing concerns about the credibility and responsibility of corporate America.

# Survey Responses

The following responses are a supplement to Korn/Ferry International's *29th Annual Board of Director's Study*. The findings are based on responses from Directors of companies with revenues under \$200 million.

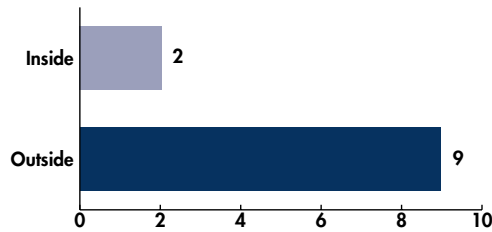
## Board Composition

The average board in our survey consists of two inside directors and nine outside directors. According to respondents, the optimal board size is two inside directors and eight outside.

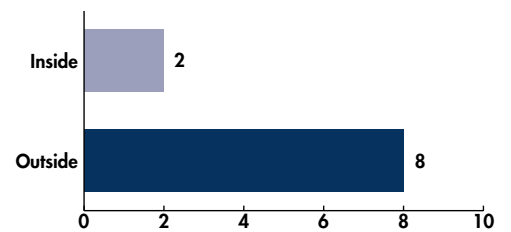
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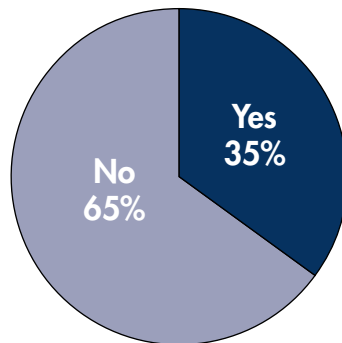
Current Board Size



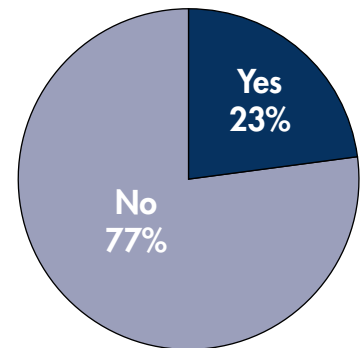
Optimal Board Size



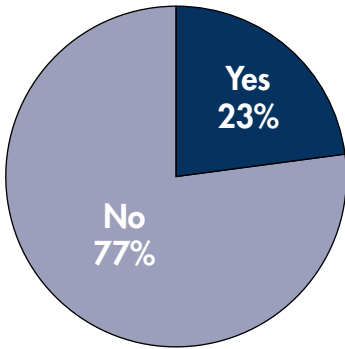
Does the former CEO sit on the board?



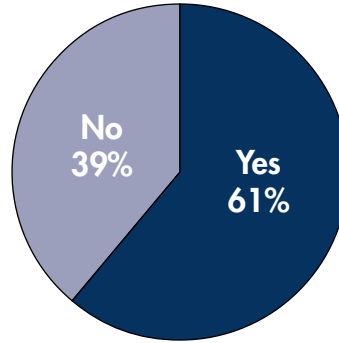
Should the former CEO sit on the board?



If your chairman is also the CEO, do you have an elected or appointed lead director?



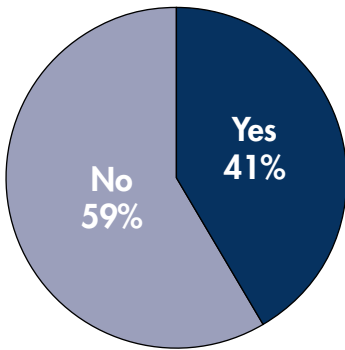
Should a board that has an inside director as chairman elect or appoint an outside director as the lead director?



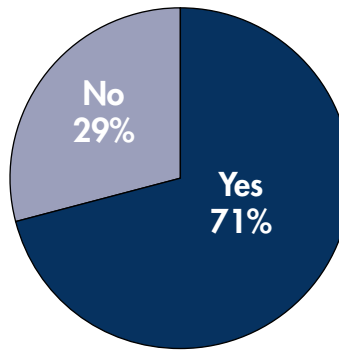
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Does the board typically hold regular executive sessions without the CEO during board meetings?



Should the board typically hold regular executive sessions without the CEO during board meetings?

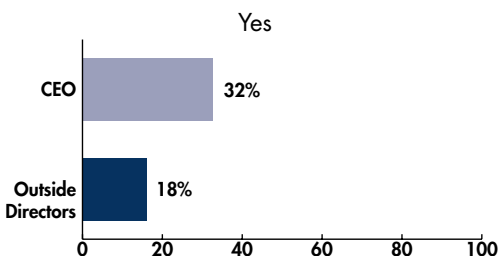


Diversity in the Boardroom

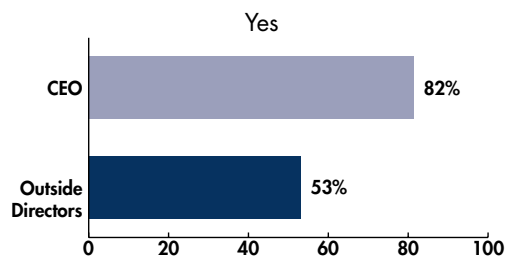
Do you have any of the following minorities currently represented on your board?

|                  |     |
|------------------|-----|
| Women            | 88% |
| African American | 39% |
| Hispanic         | 15% |
| Asian            | 12% |
| Other            | 3%  |

Is there a limit to the number of other boards on which the CEO and board members may serve as outside directors?



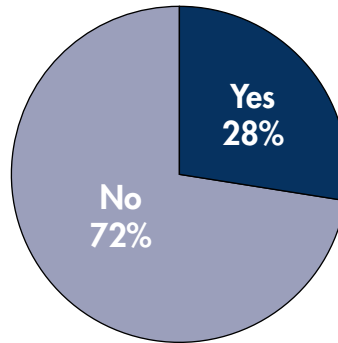
Should there be a limit to the number of other boards on which the CEO and board members may serve as outside directors?



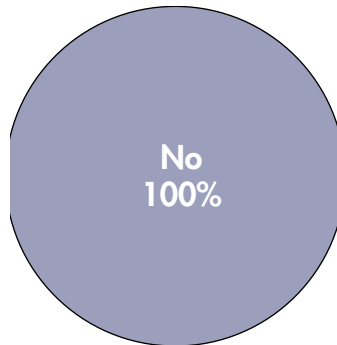
## Board Meetings

Board commitment and activity continues to intensify. The majority of Emerging Companies boards meet on a quarterly basis. With 46 percent of directors spending more time on board matters. Face to face meetings are still the way most boards continue to meet.

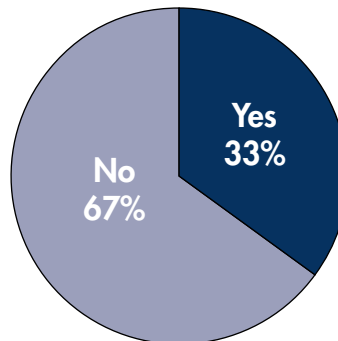
Does your board typically have board members who attend meetings electronically?



Has your board ever held a virtual board meeting via the Internet?



Would you feel comfortable holding a board meeting in a secure Internet environment?



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13.2

average hours per month  
spent on board matters.

Compared to last year how  
many hours are you  
spending per month on  
board matters?

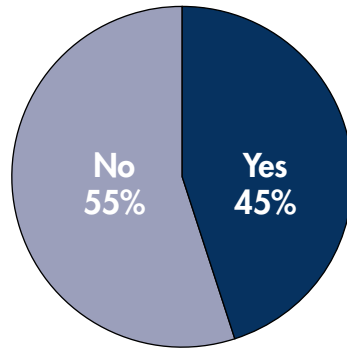
|                |     |
|----------------|-----|
| More           | 46% |
| Fewer          | 7%  |
| About the Same | 47% |

## Managing Corporate Governance

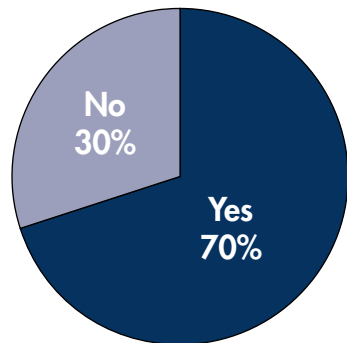
Contrary to the established trend in a formal committee that reviews corporate governance processes and board operations, emerging companies are somewhat behind the curve in this area.

However, 70% of these companies have written guidelines on corporate governance and 94% believe these guidelines are helpful to a board.

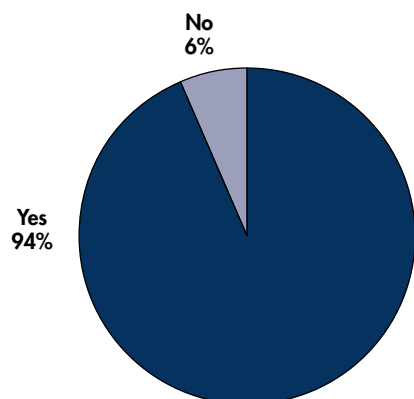
Does your board have a formal committee that reviews corporate governance processes and board operations?



Does the board have written guidelines on corporate governance?



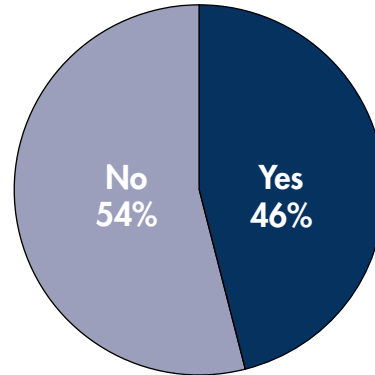
Do you believe written governance guidelines are helpful to a board?



## Management Succession

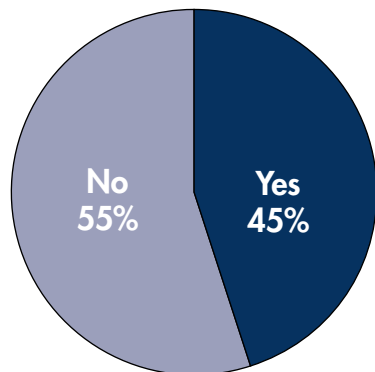
Data reveals that in the last three years only 45% of these emerging companies has undergone a management succession process. In spite of the frequency of change at the top, 54% of these companies do not have a management succession committee or process, despite strong public and regulatory support for creation and disclosure of such.

Does the board have a management succession committee or process?



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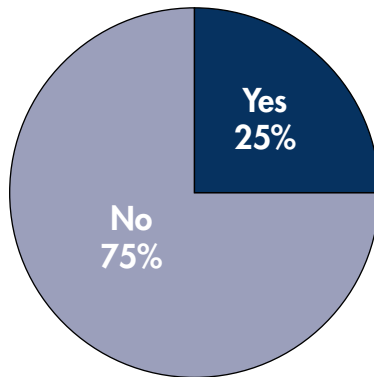
In the last three years, has your company undergone a management succession process?



## Evaluating Performance

One-quarter of the companies responding evaluate the full board’s performance on a regular basis and only 12% of those individual directors are evaluated.

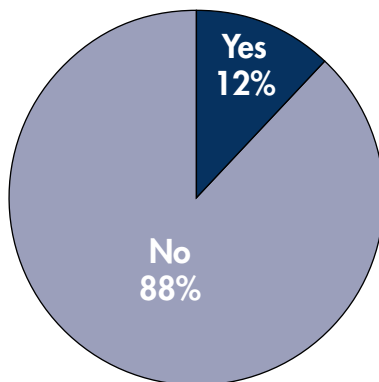
Is the entire board’s performance formally evaluated on a regular basis?



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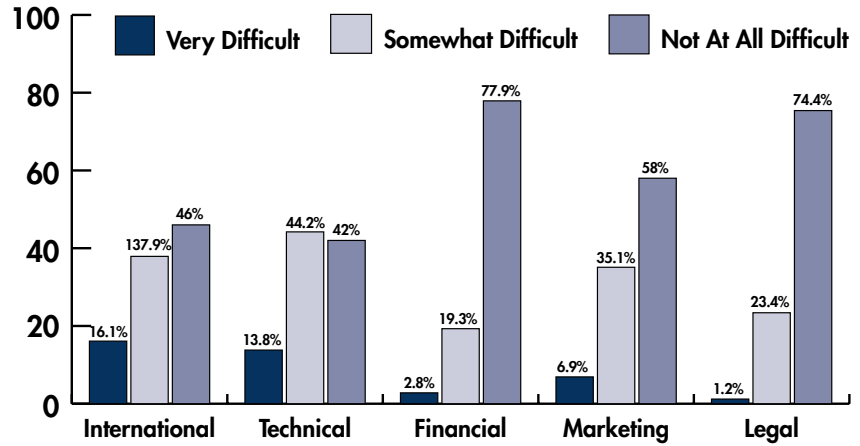
Does your board evaluate individual directors on a regular basis?



**77%**  
of respondents felt that individual directors should be evaluated regularly as to their performance.

## Board Experience

How difficult has it been for your board to add directors with the following skill sets?



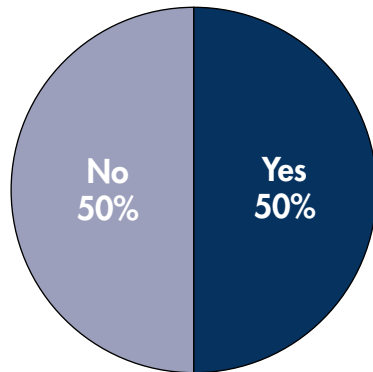
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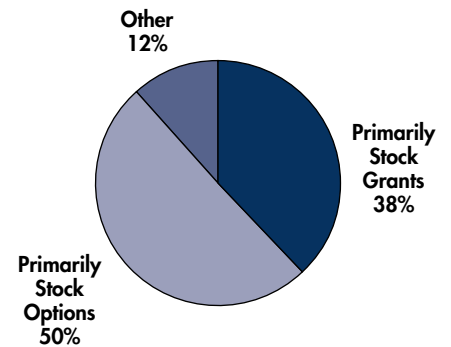
## Compensation

There is an even split on the topic of director's compensation being paid primarily in stock options.

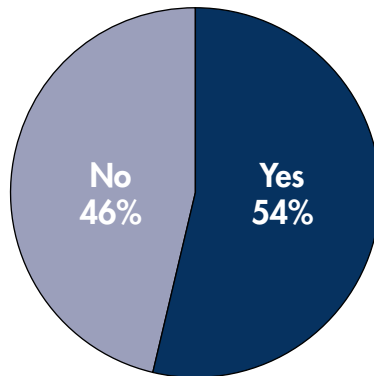
Do you think the majority of a director's compensation should be in stock?



If YES: What form of stock?



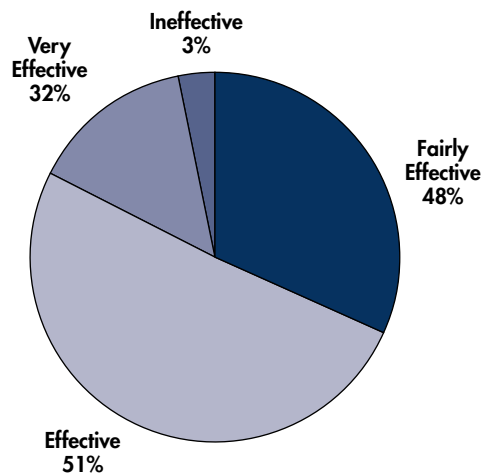
Is there a requirement that directors own shares of company stock?



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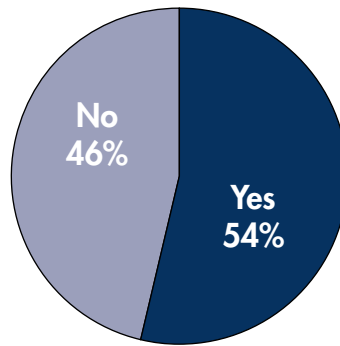
How do you feel about your company's CEO compensation program?



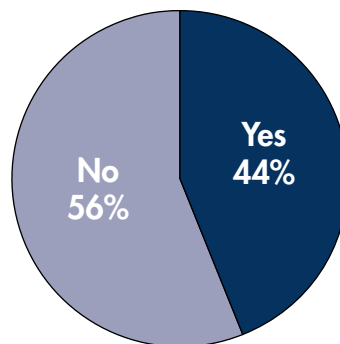
## Risk & Crisis

Emerging Companies are ahead of the pack with regards to crisis management-planning. Over 54% of companies surveyed have had a crisis management plan in place prior to 9/11/01.

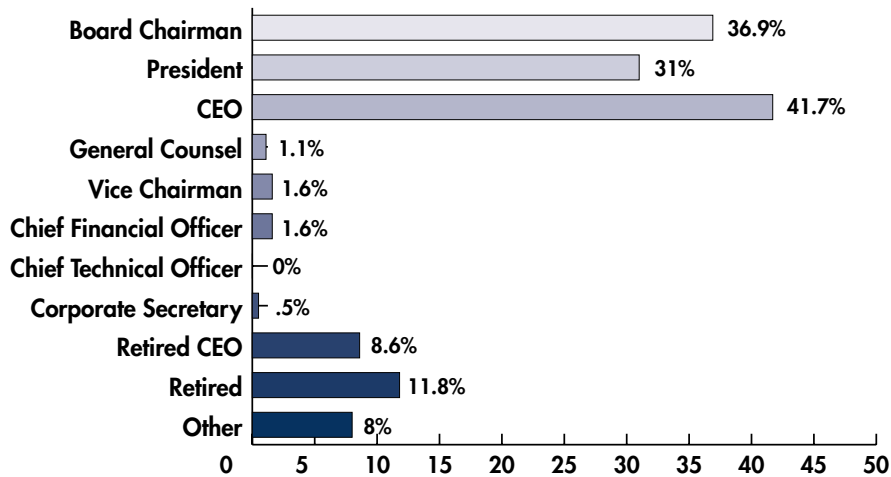
Had your board and management team developed or discussed a crisis management plan prior to September 11th?



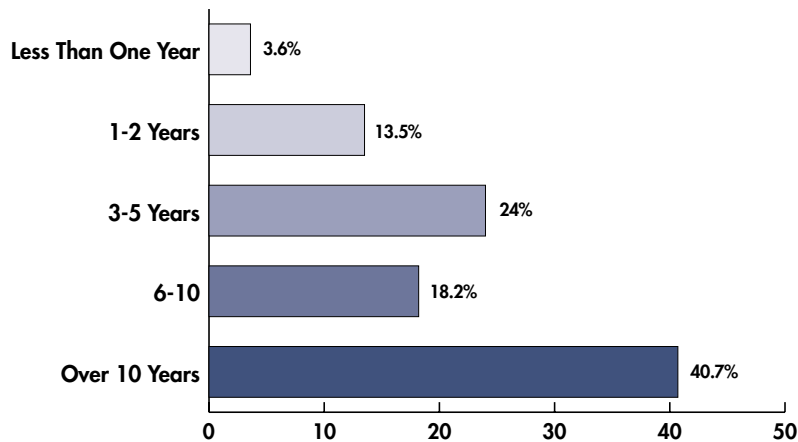
Has your board taken any action to address crisis management since the tragedy of September 11th?



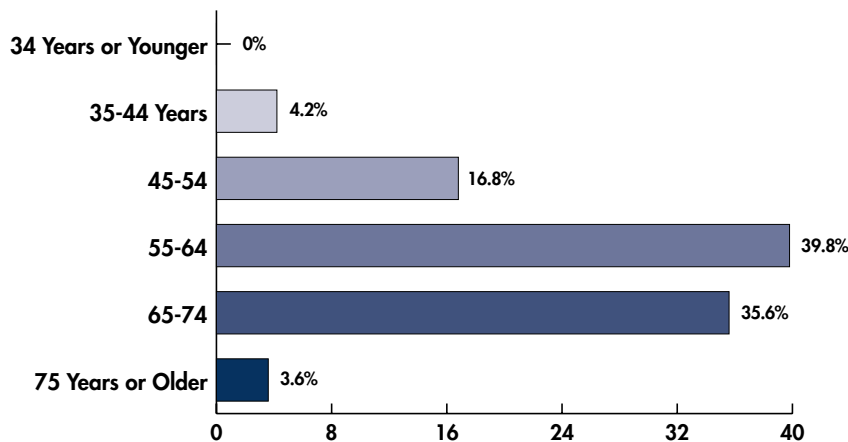
What is your title or status with your primary company?



How long have you served on this board?



Your age:



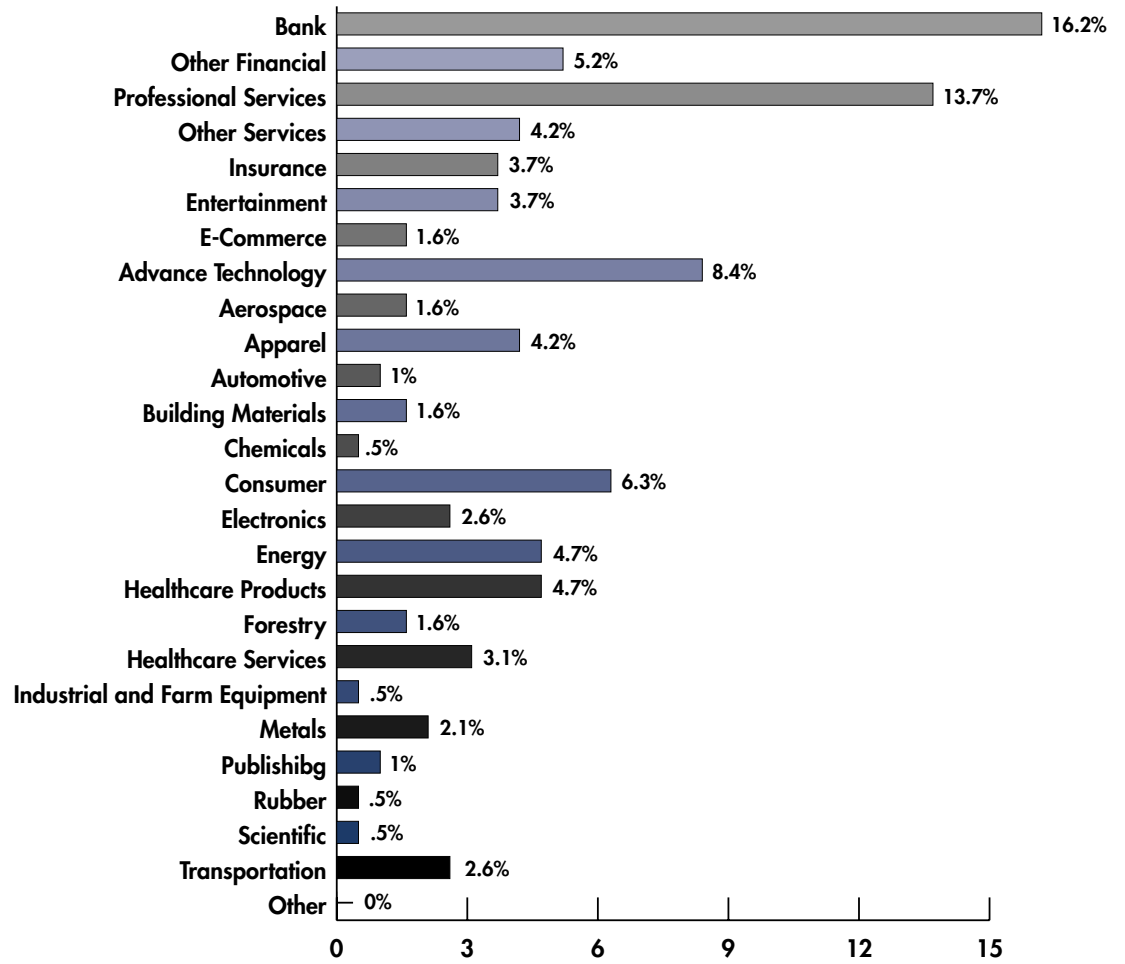
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Are you responding as an  
Inside or outside director?

|         |     |
|---------|-----|
| Inside  | 25% |
| Outside | 75% |

Which of the following best describes your company:



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## Korn/Ferry International North American Board Services Practice

- Korn/Ferry is the only executive search firm with a dedicated team of professionals 100% devoted to conducting Board of Director searches on a global basis. The North American team focuses its efforts on companies located throughout the United States and Canada.
- We tailor our approach to the specific governance needs of each client. As governance issues continue to change, we are very sensitive to the impact these have on our client base.
- We have developed the “Next Generation Director” product, which identifies the best and brightest young executives who will fill tomorrow's boardroom ranks. This is a proprietary product established through a joint venture with *Corporate Board Member* magazine.
- Korn/Ferry has one of the most recognizable brands in the world. At the senior-level, successful executives want to be known to us.
- We conduct over 200 Board searches each year with a significant percentage of those resulting in diversity placements.
- We have the highest success rate in the industry and are with you every step of the way throughout the search process.

## About Korn/Ferry International

Korn/Ferry International (NYSE:KFY), with over 70 offices in 36 countries, is the world's leading provider of executive human capital solutions. Based in Los Angeles, the firm works closely with clients worldwide to deliver customized executive search, management assessment and mid-level search services, including the identification of CEOs, COOs, CFOs, board members and other senior-level executives; the formal evaluation of senior management teams; and the recruitment of middle managers through its Futurestep subsidiary.

For more information, visit the Korn/Ferry International web site at [www.kornferry.com](http://www.kornferry.com) or the Futurestep web site at [www.futurestep.com](http://www.futurestep.com).

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