

Warren Buffett: Annual Letter Comments Regarding the Selection of Corporate Directors

Berkshire Hathaway 2003 Annual Report: Pages 9-10: (bold not italics added)

True independence – meaning the willingness to challenge a forceful CEO when something is wrong or foolish – is an enormously valuable trait in a director. It is also rare. **The place to look for it is among high-grade people whose interests are in line with those of rank-and-file shareholders – and are in line in a very big way.**

We've made that search at Berkshire. We now have eleven directors and *each* of them, combined with members of their families, owns more than \$4 million of Berkshire stock. Moreover, all have held major stakes in Berkshire for many years. In the case of six of the eleven, family ownership amounts to at least hundreds of millions and dates back at least three decades. **All eleven directors purchased their holdings in the market just as you did; we've never passed out options or restricted shares. Charlie and I love such honest-to-God ownership. After all, who ever washes a rental car?**

In addition, director fees at Berkshire are nominal (as my son, Howard, periodically reminds me). Thus, the upside from Berkshire for all eleven is proportionately the same as the upside for any Berkshire shareholder. And it always will be...

The bottom line for our directors: You win, they win big; you lose, they lose big. **Our approach might be called owner-capitalism. We know of no better way to engender true independence.** (This structure does not guarantee perfect behavior, however: I've sat on boards of companies in which Berkshire had huge stakes and remained silent as questionable proposals were rubber-stamped.)

In addition to being independent, directors should have business savvy, a shareholder orientation and a genuine interest in the company. The rarest of these qualities is business savvy – and if it is lacking, the other two are of little help. Many people who are smart, articulate and admired have no real understanding of business. That's no sin; they may shine elsewhere. But they don't belong on corporate boards.

Berkshire Hathaway 2006 Annual Report: Page 18: (bold not italics added)

In selecting a new director, **we were guided by our long-standing criteria, which are that board members be owner-oriented, business-savvy, interested and truly independent.** I say "truly" because many directors who are now deemed independent by various authorities and observers are far from that, relying heavily as they do on directors' fees to maintain their standard of living. These payments, which come in many forms, often range between \$150,000 and \$250,000 annually, compensation that may approach or even exceed all other income of the "independent" director. And – surprise, surprise – director compensation has soared in recent years, pushed up by recommendations from corporate America's favorite consultant, Ratchet, Ratchet and Bingo. (The name may be phony, but the action it conveys is not.)

Charlie and I believe our four criteria are essential if directors are to do their job – which, by law, is to faithfully represent owners. Yet these criteria are usually ignored. Instead, consultants and CEOs seeking board candidates will often say, "We're looking for a woman," or "a Hispanic," or "someone from abroad," or what have you. **It sometimes sounds as if the mission is to stock Noah's ark.** Over the years I've been queried many times about potential directors and have yet to hear *anyone* ask, "Does he think like an intelligent owner?"

The questions I instead get would sound ridiculous to someone seeking candidates for, say, a football team, or an arbitration panel or a military command. In those cases, the selectors would look for people who had the specific talents and attitudes that were required for a specialized job. **At Berkshire, we are in the specialized activity of running a business well, and therefore we seek *business* judgment.**