Operational Efficiency and Corporate Structure

Nick Jacobi[1]

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[1] Mr. Jacobi is an FSA, CERA with two years' experience as an actuary in the disability finance unit of Metropolitan Life Insurance Company. Nick began his career as the senior mathematician at Gaming Laboratories Intl. and also has three years of experience as an actuary with Guardian Life Insurance. He is a graduate of Lafayette College in Easton, Pa.

Abstract

Operational risk is the risk of loss due to people, process or technology. It does not carry a higher potential reward as more risk is taken, and this makes it unique among traditional risk classifications. It never pays; it only costs. This risk is also unique in that it tends to hedge itself. As more management levels are added to an organization, fewer errors should occur due to greater supervision. In this study I will review some correlations between the operating income per employee and some elements of company structure for the S&P 500 that are proxies for management control and supervision. An analysis yielded the following general observations: 1) companies in which the chairman and CEO roles are combined generate more income per employee than those in which the roles are separate; 2) companies with a lead director and the chairman and CEO combined typically do better still; 3) the more executive officers a company has, the higher operating income is generated per employee although this decreases marginally; and 4) companies tend to gravitate toward a structure with 10 executive officers and 10 directors; this is a fixed point of an iterative decision function.