

A Study on the Corporate Governance Structure for-Profit Hospital -Focusig specially on the outside Director in Commercial Code-

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Abstract

In this paper many discussions are raised regarding the outside director system in order to establish the position of the outside director within institutional organizations and to review ways to activate the outside director system in for-Profit Hospital.

it seems to be more desirable in Korea for each company to establish an efficient system by itself in accordance with suggested guidelines suitable for each for-Profit Hospital management circumstances rather than to apply a unilateral outside director system to for-Profit Hospital through legalization. In this regard, while keeping the current outside director system for the time being, it is necessary to review and improve the management status of companies and the usefulness of the system, and various recommendations from lawyer associations, Hospital business associations, and academia should be allowed rather than just for-Profit Hospital recommendation by the government.

▶ Keyword :for-Profit Hospital, outside director, for-Profit Hospital Policy

I . Introduction

The modern corporate system grants the operating rights of a company to the directors and a BOD in accordance with the principle of the division between ownership and management; accordingly, the functions of shareholders' meetings and auditors have disintegrated and dictatorial management by directors and controlling shareholders has intensified. Therefore the introduction of a systematic tool is urgent for requiring responsibilities by directors in the modern corporate institution system where the rights and responsibilities of directors are being emphasized.[1]

BOD of a corporation has the right to make decisions to execute and supervise the management of directors in accordance with the Commercial Code, the BOD has been downgraded to a subordinate organization under the company president, in reality receiving only directions

and orders since it is composed of executive managing directors and other directors who are controlled by the president. As a consequence, the BOD cannot perform its check function intended by the Corporate Law and has become an organization in name only. It has only increased despotism, misappropriation, dereliction, window dressing, unlawful dividends, and tax evasion by the owners, and the deteriorated financial status of the company, resulting in successive bankruptcies. Hence the outside director system was introduced in order to assure the completeness and activation of the BOD's functions. Thus the American-style outside director system was introduced to attempt to overcome the dissolution of the BOD's function by allowing the internal directors to properly perform their decision-making function and to properly exercise their right of supervision of management. Furthermore, the outside director system

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servers to coordinate the various views of the stakeholders through active and democratic discussion and to provide the management with special knowledge and experience.[2] In this paper many discussions are raised regarding the outside director system in order to establish the position of the outside director within institutional organizations and to review ways to activate the outside director system.

II. Theoretical Background

1. Definition of outside director

The term "outside director" is originally not a legal term but an English term used in American stock companies. Currently an outside director is also called "Independent director", emphasizing his independent status.

In general, outside directors only participate and make resolutions when a BOD meeting is held and are distinct from the inside directors who perform the internal work every day. the Committee for Improvement of Corporate Governance recommended the application of this system in its "Best Practices of Corporate Governance"[3]. Thus the term "outside director" has assumed an important place in the discussion of stock companies' organization and governance structure. In the case of securities companies and stock-listed companies according to the January 2000 revision of the Security Exchange Code, "outside director" was officially designated as a legal term such that the BOD and the audit committee have a certain proportion of outside directors as its component

2. Qualifications of outside directors [4]

The following cannot serve as outside director in accordance with the revised Security Exchange Code ① a minor or incompetent or quasi-incompetent person, ② one who has filed for bankruptcy and has not been reinstated, ③ one who has been sentenced to imprisonment of which less than two years have elapsed since the completion of the imprisonment or since the rendering of the decision not to execute such punishment, and ④ one who was discharged or dismissed under this act for whom less than two years have elapsed since the date of such discharge or dismissal; ii) a person who is the largest stockholder of the voting stocks; iii) a person

in a special relationship with the largest stockholder; iv) the major stockholder of the applicable securities company, his/her spouse, direct ascendant or descendant; v) a person who is an officer or employee of the applicable company or has been affiliated with the company within the past two years; vi) the spouse or lineal ascendant or descendant of an officer of the company; vii) an officer or employee of a corporation that is in an important business relationship with the applicable company according to presidential decree, a competitive relationship or a cooperative relationship with such company or a person who has worked as an officer or employee of such corporation within the preceding two years; viii) an officer or employee of an applicable company who is working as a non-standing director, and ix) a person who has difficulty in faithfully performing his duties as an outside director, or may affect adversely the management of his/her company as stipulated by President decree.

3. Election of outside directors[5]

How to elect the outside directors is an important matter as it affects the independence of the BOD. The methods of electing outside directors can be divided into election by the company management or controlling shareholders, election by nominating committee, and election by institutional investors.

The first method is the nomination of candidates for outside directorship by the company management or controlling shareholders and election of the outside directors in a shareholders' meeting among these candidates. This method poses problems for the independence and objectivity of the BOD and outside directors because both the company management and controlling shareholders tend to nominate persons who have academic, regional or blood ties or persons who are otherwise in a substantial relationship with the company. Korean companies currently utilize this method of election so that the effectiveness of outside directors is questionable[6].

The second method is the search and nomination of outside directors by a nomination committee of the BOD. This method can be effective for securing the independence of the outside directors since many outside directors can be involved in the nomination committee [7]. On the other hand, it might be difficult to expect the independence of the outside directors who are included in

the nomination committee because both the executive management and the controlling shareholders can influence the nomination committee.

4. Merits of the outside director system

4.1 Monitoring and supervision of management

Traditionally BOD and auditors have not been able to perform their roles since they have not been provided with independence from the controlling shareholders, so that outside directors who are guaranteed independence are effective in monitoring and supervising management[8]. While it has been the majority opinion that outside directors can perform preemptive monitoring activities by participating in the decision-making processes of the BOD while traditional auditors can audit only the legitimacy of the management activities, outside directors are different from traditional auditors since they can also audit the appropriateness of management activities. Additionally, the focus on outside directors lies in pursuing long-term and social interests as their views can be objective since they are outside the company, in contrast to the company management and controlling shareholders[9].

4.2 Prewarning and advice from specialists

Outside directors can prewarn or advise in an appropriate way as a tool of management control, since they are specialists such as professors, lawyers, technical specialists, and managers of other companies. For example, those who are executive managers of other companies or have similar past experiences can provide useful and highly sophisticated advice, if necessary, knowing as they do the complex nature of business management, and can perform roles as members of various committees.

While inside directors cannot perform these functions because of their execution responsibilities, rightful judgement of the prevailing issues of the BOD can be expected from outside directors as they do not bear the burden of the daily work. Outside directors also supply special knowledge, experience, and technology in the establishment of the company's long-term business strategies, and can propose unbiased independent opinions regarding matters from which potential conflict of interest could occur[10].

5. Demerits of outside directors

5.1 Influence from management

Outside directors can perform their functions only when they are independent of management and controlling shareholders. However, in most stock-listed companies, outside directors are elected by shareholders' simple voting from a list proposed by the BOD or a nominating committee. Even though the utilization ratio of a nominating committee where the chairman is one of the outside directors has increased, the executive management of the company holds practical authority as far as the nomination of directors is concerned. Outside directors are not only practically dependent on executive management during their tenure but also have a sense of integration by nature, and a social solidarity is formed between officers and directors. Lawyers of investment banks may actually have an important financial interest relationship with the company and their own companies in many cases[11]. Accordingly, outside directors evaluate the executive management positively and have a tendency not to participate in the company policies and decision-making of the management in an open and critical way. There are also many cases in which the outside director accepts the company management's policies or decisions passively rather than challenges them actively[12].

5.2 Lack of information

Outside directors must gather enough information to smoothly perform their monitoring and supervisory functions and form their opinions regarding management execution. Nevertheless, outside directors can only access the information that is chosen to fit the intention of the management because, in the case where the chairman of the BOD is the executive manager, the agendas of meetings and volume of supportive information are controlled by the executive management. Accordingly, the functions that are expected from outside directors cannot be carried out because there is a limitation upon outside directors in their access to information[13].

5.3 Lack of sufficient time

Frequently outside directors have many issues that need to be reviewed and studied over a broad range that goes beyond their specialized professions as professors, lawyers, CPAs, or managers of other companies, yet BOD meetings tend to be called infrequently and last for a

short time.

Furthermore, because outside directors wish to maintain good relationships with the chaebol groups without any unreasonable behavior while maintaining their director position, they do not actively perform their supervisory functions[14].

5.4 Lack of speciality in supervision

Often outside directors do not have any speciality for making a sophisticated company decision despite being provided with enough information. In particular, outside directors who do not have a business background often lack professional knowledge of the BOD agenda, attend BOD meetings in a stereotypical manner, and serve on committees while being remunerated little in return. Outside directors' active roles in company management and risk prevention can hardly be expected under these circumstances[15].

III. Activation of outside director system for-Profit Hospital

1. Strengthening the independence of outside directors

Currently, outside directors who are friendly to management are elected so that it is difficult to expect them to exercise their supervision role because the regulation regarding the independence of outside directors is not strict enough[16]. Recently, as the appropriateness of economic incentives including rewards should indicate, economic independence is even more important than human independence[17].

In most cases, however, either the controlling shareholders or the company executives recommend the outside directors[18], and the election method of outside directors is not transparent, as in the blocked election of outside directors suitable for management control, since it is impossible for ordinary shareholders to identify the candidates for outside directorship. Therefore, not only should the independence of the outside directors be secured through enforcement of the qualifications of outside directors, but the selection of candidates and the election process should also be improved. For example, it is necessary to guide the shareholders to make

reasonable decisions when they elect the outside directors by pre-announcing the information regarding the candidates' profiles and recommendations either on the Stock Exchange or in the written agenda of the shareholders' meeting[19].

Korea's Security Exchange Code states the necessary qualifications for outside directors in order for independent outside directors to be elected. However, notwithstanding these regulations, outside directors' independence evokes suspicions because ex-executives and employees, ex-executives of subsidiaries, ex-non-standing directors, or non-independent people connected by region or school tend to be elected as outside directors. Therefore it is necessary to strengthen the qualifications of outside directors by studying ways to improve the election procedure from the root, this will require the thought conversion of the business management[20].

2. Enhancing the functions of outside directors

manage their activities except in such ways as counting the number who participate in BOD meetings or who vote for or against the important issues of company management. Also, as explained above, outside directors as professionals in most cases cannot spend enough time and effort in their outside director work when they share concurrent positions. According to a survey, fifty-three percent of listed companies want to reduce the percentage of those in concurrent positions[21]. Accordingly, it is necessary to improve the effectiveness of the outside director system by announcing outside directors' activity results to the public in order for the shareholders to be able to determine whether the elected outside directors are performing their proper role [22].

According to Enforcement Order 37-2-3 of the Security Exchange Code, an outside director of more than one listed company other than the company in question is disqualified. This regulation applies to outside directors of share-listed companies ③ of the Security Exchange Code). The regulation on the limitation of concurrent positions is to be further researched and complemented. On the other hand, outside directors should have sufficient information of the company's management plans and management status in order perform their function efficiently. Therefore a company should supply whatever information an outside director needs.

3. Improvement of operating conditions of outside directors

The government's and related institutions' active support is required for institutions that educate outside directors while being established as new businesses. Currently the Korean Listed Companies Association, the KDI, and the Korean Efficiency Association are in the process or preparing for the development of outside director training programs as well as a human resource bank for outside directors. However, not many candidates who have been trained in these programs have been invited to be outside director in companies because of executives' fixed ideas of inviting their own aides to these positions[23].

For the number of outside directors to increase and the election process to improve in the future, the government needs to support the activation of training facilities fully so that they can fulfill their role as human resource pools

4. Limitations on the responsibilities of outside directors

Even though there is a view that Articles 399, 401 and 401-2 of the Commercial Code should be revised to set a limitation on the responsibilities of outside directors, such responsibilities cannot be relaxed when the related laws and articles of incorporation are violated, and they outside directors cannot be limited when companies damage third parties out of malice or unintended mistake[24].

Therefore, as reviewed previously, it is desirable to relax the responsibilities of outside directors through such methods as liability insurance and interpretational acceptance of business judgement rules

IV. Conclusion

Lately, government considered that the telemedicine has high economic value as a new growth engine of the Korea and preceded the national tasks that future creative economy activation. So, they are pushing the legislation for telemedicine. However, healthcare sector is closely related to health of the people[25].

finally, it seems to be more desirable in Korea for each company to establish an efficient system by itself in

accordance with suggested guidelines suitable for each for-Profit Hospital management circumstances rather than to apply a unilateral outside director system to for-Profit Hospital through legalization. In this regard, while keeping the current outside director system for the time being, it is necessary to review and improve the management status of companies and the usefulness of the system, and various recommendations from lawyer associations, Hospital business associations, and academia should be allowed rather than just for-Profit Hospital recommendation by the government.

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