

Corporate Governance

Governance is a continuing focus at JPMorgan Chase, starting with the board of directors and continuing throughout the Firm. There are three pillars of good governance:

- An independent board, accountable to shareholders
- Strong internal governance
- Alignment with shareholders

Board governance

JPMorgan Chase's board is experienced, independent and accountable to shareholders. The board's structure and practices include *the following*, and more information on board governance can be found on the Firm's website (www.jpmorganchase.com):

- *effective size*: The board's preference is to maintain a smaller size for efficiency and to encourage active dialogue. As retirements occur, the board will actively seek to increase diversity among its membership.
- *a super-majority of non-management directors*: There are only two full-time management members on the board, Bill Harrison and Jamie Dimon. During 2005, Bob Lipp became a part-time member of management to share his special skills in developing talent within the firm. All other members of the board are non-management directors that the board has determined to be independent.

- *director independence*:

independent directors – Each of the non-management directors of JPMorgan Chase was determined by the board to be independent in accordance with board standards that consider past and current employment relationships; any business relationships with or charitable contributions to entities at which a director serves as an officer; and personal banking and other financial relationships, which must be on an arm's-length basis.

executive sessions of directors – In 2005, the board adopted the practice of meeting without management at each regularly scheduled board meeting.

access to outside resources – Although the main responsibility for providing assistance to the board rests with management, the board and board committees can engage outside expert advice from sources independent of management at the expense of the Firm.

- *director accountability*: majority voting for directors – In 2005 the board adopted a policy providing that in uncontested elections, any director nominee who receives more withheld than for votes will tender his or her resignation. Absent a compelling reason, the board will accept the resignation.
- *director compensation*: The board believes it is desirable that a significant portion of overall director compensation be linked to JPMorgan Chase stock, and the board's total compensation includes approximately one-third cash and two-thirds stock-based compensation in the form of share equivalents that must be held until a director's termination of service.

Internal governance

While governance begins with the board of directors, managing the enterprise requires effective governance structures and practices throughout the organization. The firm as a whole manages by line of business, supported by global policies and standards that typically apply to all relevant units regardless of geography or legal structure. The strength of these global control processes is the foundation of regional and individual subsidiary governance. Three examples of the Firm's global processes and standards are its risk management structure, policy review process and codes of conduct.

Defined risk governance is a principle of risk management at JPMorgan Chase. The board of directors exercises oversight of risk management through the board as a whole and through the board's Audit and Risk Policy committees. The charters of these and other board committees are available at the Firm's website. The board delegates the formulation of policy and day-to-day risk oversight to management. The Firm's risk governance structure is built upon the premise that each line of business is responsible for managing the risks inherent in its business activity, including liquidity risk, credit risk, market risk, interest rate risk, operational risk, legal and reputation risk, fiduciary risk and private equity risk. Each line of business has a risk committee responsible for decisions relating to risk strategy, policies and control. Where appropriate, risk committees escalate risk issues to the Firm's Operating Committee, comprised of senior officers of the Firm, or to the Risk Working Group, a subgroup of the Operating Committee. Overlaying risk management within the lines of business are three corporate functions: Treasury, Risk Management and Office of the General Counsel. Treasury is responsible for managing the interest rate and liquidity profile of the Firm. Risk Management provides an independent firmwide function of control and management of risk. The Office of the General Counsel has oversight of legal, reputation and fiduciary risk. A discussion of risk management begins at page 60 of this Annual Report.

The policy review process is based on the recognition that a firm's success requires maintenance of a reputation for business practices of the highest quality. The Firm has a specific structure to address transactions with clients that have the potential to adversely affect the Firm's reputation. Primary responsibility for adherence to the policies and procedures designed to address reputation risk lies with business units, which are also required to submit to regional Reputation Risk Committees proposed transactions that may heighten reputation risk. The committees may approve, reject or require further clarification on or changes to the transaction, or they may escalate the review to the most senior level of review, the Policy Review Office. The objective of the policy review process is to reinforce a culture that ensures that all employees understand the basic principles of reputation risk control and can recognize and address issues as they arise. For a further description of the policy review process, see the discussion of reputation and fiduciary risk starting at page 80 of this Annual Report.

The Firm has two codes of conduct, one applying to all employees and a supplementary code that applies to senior executive and senior financial officers. The Code of Conduct is applicable to all employees and the Firm requires each employee to certify annually his or her compliance with the Code. The Firm also has a Code of Ethics for Finance Professionals to underscore the importance of ethical conduct and compliance with law, particularly as it relates to the maintenance of the Firm's financial books and records and the preparation of its financial statements. Both codes are available at the Firm's website.

Alignment with shareholders

Good corporate governance requires that compensation policies align with shareholder interests. JPMorgan Chase's compensation policy for executive officers emphasizes performance-based, variable compensation over fixed salary and uses equity-based awards to align the interests of executive officers with shareholders. Members of the Firm's Operating Committee are required to retain 75% of the net shares received from equity-based awards, after deduction for taxes and exercise costs.