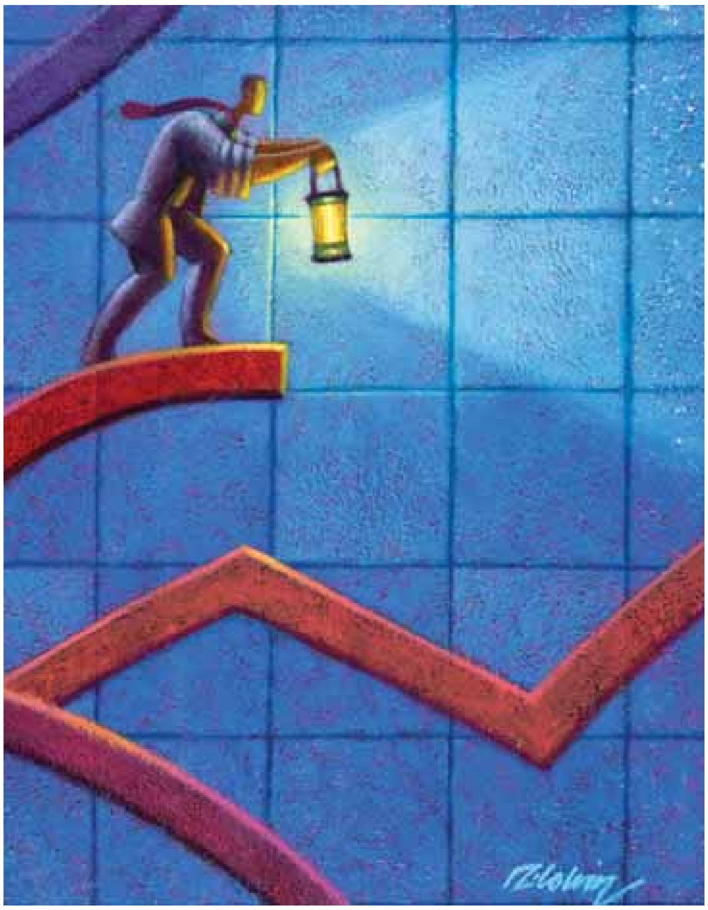
Troubleshooting In the Boardroom

A third-party assessment during a crisis can bring long-lasting improvements.

By Roger M. Kenny and Sarah K. Stewart



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Boards that engage a third party to assess how they function as a team and how they engage with management are often in crisis mode. Directors may be dealing with some wrenching change in the business or wrestling with dysfunctional relationships that have developed. They know they need partners who can sensitively help them navigate the change and deal with its impact on personal relationships and board effectiveness. We have guided 20 clients through this process and believe we can offer some useful insights.

Naturally, we believe that third-party help with a board assessment creates a discipline that elicits a higher degree of candor from directors. Indeed, many of our clients had performed their own self-assessments in the past with mixed results. They've often used a "tick the box" approach that couldn't and didn't lead to outcomes of any real substance.

As part of our assessment process, we ask each board member to complete a survey designed to address broad issues but also highlights the special questions facing that particular board. We follow up with one-on-one discussions with each director. It is also critical to speak with executives who regularly interact with the board. We are then able to present the collective views of directors and management and lay out an action plan for the board.

These assessments frequently reveal that management wants help from the board but doesn't always know how to get it. Executives often feel that directors haven't learned as much as they need to about their businesses. At times, this may be because directors aren't holding up their end of the bargain—but it also means management should be providing better opportunities for directors to learn about the company and its industry. Unfortunately, at most organizations, no one is assigned to help make this happen regularly.

While every board's situation is unique, we have found that most assessments include discussion and action plans for nine key areas:

Directing strategy. Getting strategy right is front and center for most boards. Directors want to make sure decisions are made with an approved and clear strategy in mind, and they want to be able to provide counsel that is helpful to management. Often, however, there is a sense that the board's contribution is superficial. Getting a board really engaged in strategy isn't always easy. It requires effort and patience on everyone's part.

Management presentations should be well-written and concise, so that they drive board discussion rather than cause mind-numbing weariness. Strategy is all about answering the fundamental questions that define what a company really wants to be. It's not always well articulated by the management team. When directors challenge executives to produce better strategic statements and then test management's plans and assumptions, they are asking the right questions.

Executives may get frustrated and defensive if they feel they are constantly being asked to explain their strategy, so directors should be sensitive to management's efforts. Because strategy is an evolving thing that needs continuing guidance, the board must find a way to be both supportive and challenging.

Succession planning and management development. The No. 1 objective of most boards is to select, encourage and support the management team. No board wants to have to replace a failing management team, because it is an admission of its own failure to select an effective leader and to build bench strength.

At the CEO level, many directors ask for succession choices and want to see active processes to empower those candidates. At many companies, however, the board is less engaged in the development of key executives below the CEO. This is a long-term process that should include getting to know the senior team through regular contact, both formal and informal.

Directors can add value to top management's thinking on future leadership, and it is the board's job to make sure the company has processes in place for rigorous self-evaluation; for hiring and identifying key talent; and for developing and mentoring those executives to prepare them for greater responsibility. Obviously, this is not something the board executes, but directors can drive it by keeping it high on the agenda.

Formalizing CEO evaluation. Almost every board wants to do a better job of CEO evaluation, using financial and nonfinancial performance metrics. Boards today are required to articulate in the proxy the reasoning behind CEO compensation, which is generally tied to performance. However, CEO evaluation is about much more than pay. When it's done well, most of the issues that directors are concerned with fall into place. Formalizing CEO evaluation can lead to better results. An effective process focuses on identifying areas for improvement and ensuring good communication. There should be a shared understanding of what constitutes success.

Empowering board leadership. Board leadership can add a lot of value, and having a nonexecutive chair or lead director in place can be especially helpful during a period of transition or turnaround. The role requires excellent interpersonal skills; a lead director must be a trusted communicator who has the respect of his or her fellow directors and that of senior management.

Just creating this position gives the CEO a new channel for help. And when the CEO and board empower the lead director to take on vital responsibilities—such as helping to set the tone of board discussions, keeping the board agenda focused on the right issues, ensuring that all board members' views get adequate time and attention or moving discussions along when bogged down—board meetings and effectiveness are improved. Clearly, a major role of the lead director or chair is to facilitate consensus and act as the board's spokesperson with management, especially in communicating feedback from executive sessions.

Directors want less presentation time from management and more time for discussion.

Improving board meetings. Traditionally, board meetings have tended to revolve around routine business reviews rather than issue-oriented discussions. Today's boards are moving to frame meetings more around strategy, focusing on subjects and businesses that are priorities for reasons of performance or timing.

Other suggestions for improvement include fine-tuning the agenda so that board meetings cover fewer topics. Highlighting just one or two management presentations results in deeper, more productive dialogue. Cumulatively, these sharper conversations result in board meetings that no longer feel like ad hoc events but connect with a long-term strategy.

"You're Fired": Getting a Problem Director Off the Board

Asking a director to leave is probably one of the most difficult jobs a board can face. After all, board members are generally highly accomplished and respected corporate leaders. Having to tell a director that he or she is "not working out" is extremely awkward. It's no wonder boards avoid such confrontations as often as possible and simply wait until the problem director decides voluntarily not to run for reelection.

In the days when boards were little more than ritual-driven clubs, such passivity didn't matter. Today, however, they are concerned about maximizing their effectiveness and adding real value for the organizations they govern. They also face more scrutiny than ever before. In this environment, ignoring a director performance issue is far less acceptable. Directors who *consistently* doze off at meetings, arrive unprepared, never take their eyes from their BlackBerries, or actively impede the board's functioning—either by wasting time on trivial issues or interacting aggressively with fellow board members—should not be allowed to retain their positions. Ignoring such behavior further impedes board performance. And it detracts from the credibility of board leadership, creating the wrong "tone at the top."

Of course, if a director engages in activities that could be illegal, his or her removal from the board must be handled with particular care. The board should proceed only with advice from corporate counsel and perhaps consult external legal experts as well. But for behavior that is clearly detrimental to good governance without breaking the law, a few best practices apply:

◆ **Let the lead director take the lead.** One of the greatest boons to boards in terms of dealing with personnel issues has been the surge in the appointment of lead directors, now found on more than 70 percent of U.S. boards. It is always easier for a board member to address performance issues with a peer than it is for the chairman or CEO to do so. Whether or not the CEO also carries the title of chairman, he or she "reports to" the board. That creates thorny dynamics when it comes to discussing board performance. As one lead director explained: "Micromanagement is frequently

Following the rules of engagement. Communications and relationships are often at the heart of improving board effectiveness. How individuals interact is as important as what they have to say. Directors who uphold the board's compliance function while contributing to and supporting management goals and activities don't have to like one another. But they must treat each other with respect.

Directors and management, through their intentions, tone and style, must define their way of working together. Trust and camaraderie always facilitate difficult decisions. We have sometimes seen boards take too long to acknowledge signs of nonperformance or dysfunction at a company, and then must take precipitous corrective action. We attribute this to what we call the "politeness syndrome" on the part of too many boards. But we have also seen boards capable of stepping up and dealing with tough issues with the right amount of conviction and sensitivity.

Improving the information architecture. Most directors we talk with want less presentation time from management and more time for discussion. At the same time, as boards have stepped up their level of engagement, management teams feel pressured to provide more information. We believe that the right balance can be found if boards agree to spend some time in executive session talking about the kinds and amount of information they would most like to have, so that management can streamline the board books. It makes sense to provide more detail in writing and expect directors to review it fully. That way, management presentations at meetings need only hit the high points to drive discussion.

Breaking in new directors. Many boards sense that their process for assimilating new directors could be much better. It is not enough to leave orientation to the directors themselves. Helping new directors learn about the business in detail should be a priority for the management team. Specific managers, such as the chief human resources officer, should be assigned this task.

We also believe that good director education programs should be ongoing and revolve around deepening directors' understanding of the business, the industry and its challenges. In addition, boards have a wealth of knowledge and talent around their own tables that can be called upon to create programs that add value for the company and everyone on the board.

Finding the best composition. Most boards see an urgent need to upgrade themselves with new skills that are relevant and useful to management and aligned with the company's strategic direction. Whereas in the past, directors were selected for name recognition or reasons of personal friendship, boards today are defining the skills they need. Most are also trying to bring on members who can contribute to discussions while enhancing the board's diversity profile, including professional and personal backgrounds.

Obviously, any third party conducting such an assessment must be a trusted, confidential adviser. We're told the results are well worth it. D

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an issue in director performance. It's a lot easier for a lead director to raise this issue with the person who is doing it. If the CEO raises it, he or she sounds defensive."

◆ **Consider a peer review.** Although individual director performance assessments are still undertaken by fewer than half of S&P 500 companies, they are on the increase. Unfortunately, self-assessments are typically little more than consciousness-raising exercises. All too frequently, problem directors give themselves outstanding scores.

Peer reviews, on the other hand, can have significant impact on director performance. Most directors take the views of their fellow board members very seriously. Moreover, collecting feedback from all board members can ensure that there is consensus on the problem. Using a third party rather than an insider to collect the evaluations makes it difficult for a problem director to accuse one or more colleagues—or the CEO—of animosity or some other personal agenda.

◆ **Give notice and preserve dignity.** It is imperative to be fair and respectful in handling a director's removal. The problem should be drawn to the director's attention in a constructive way, and he or she should be given ample opportunity to address it. Directors who suddenly find out that they are not being renominated, with no idea what was coming, can create a host of political difficulties for the board.

Sometimes, feeling unable or unwilling to address a serious issue drawn to his or her attention, a problem director may decide to resign. If this occurs, it is important that the resignation be treated with the utmost respect—for it represents a decision to put the board's interests ahead of one's own. But regardless of the way in which a problem director leaves, it is critical to let the individual leave with dignity. The field day the press had with Hewlett-Packard provides an almost unparalleled illustration of the importance of this point. The key is to have the courage to address performance issues and approach them in a way that is both fair and respectful to the individual concerned. — *Beverly Behan*

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