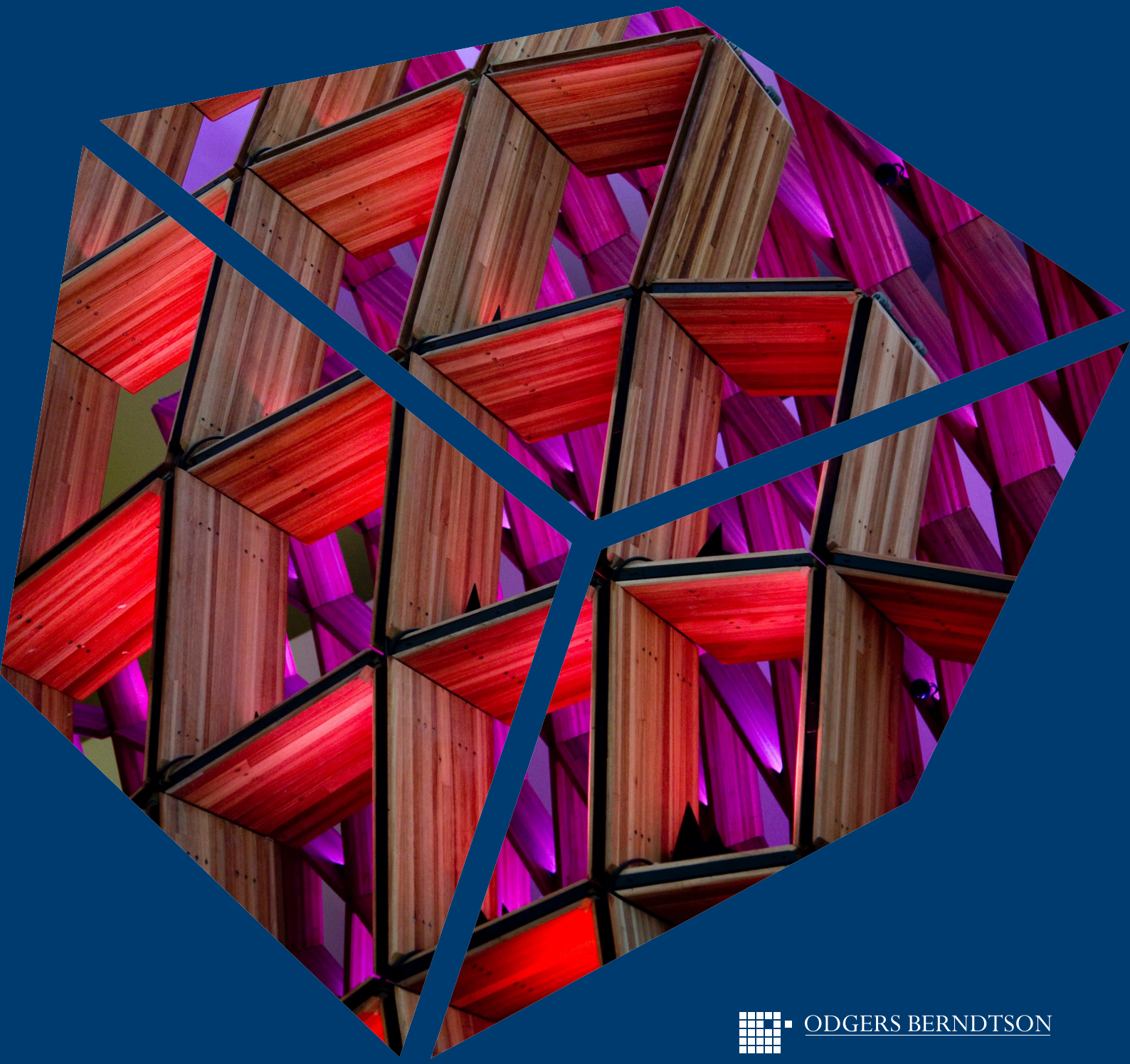
ODGERS BERNDTSON CHAIR AND BOARD PRACTICE

Board assessment, corporate governance and improving performance.



ODGERS BERNDTSON

‘The price of greatness is responsibility.’

These words spoken by Winston Churchill upon receiving his honorary degree at Harvard University can be equally applied to corporate leadership today.

This white paper explores the structure of boards and their responsibilities and makes the case for how regular independent board assessments can improve performance and ensure boards fulfil their potential.

BOARD STRUCTURE AND RESPONSIBILITIES.

Everyone is familiar with the concept of a corporate board, but they can vary in structure, size and function depending on corporate governance regulations and practice. Before discussing the utility of board assessments, let’s consider the different forms this oversight body can take.

BOARD TYPES

Unitary

A ‘unitary’ board, or one-tier board, is a single board of directors comprising executive directors and independent non-executive directors. The latter typically are not involved in the day-to-day management of the business, but do take part in board-level policy and strategy discussions. Non-executive directors may be responsible for monitoring the company’s executive directors and they generally act in the best interests of the wider stakeholder population. This is sometimes referred to as the Anglo-American board model.

On a unitary board, each member, whether she is an executive or non-executive director, has similar responsibilities. Each board member is there to promote the company’s best interests and ensure its success. The board works together to shape the corporate strategy and hold company executives accountable for meeting targets and delivering on that strategy.

Two-tier

In Germany and other countries that follow the Rhineland example, a ‘two-tier’ board is preferred. The first tier is a management or operating board led by the CEO that is responsible for the day-to-day running of the business. The company’s chairman runs a separate supervisory or corporate board, which has a wider membership and is responsible for strategic oversight of the organisation.

The supervisory board typically includes representatives of major shareholders, environmental groups, employees (possibly trade union representatives) and lenders. In contrast to the INEDs (Independent Non-executive Directors) on a unitary board, these individuals are not considered to be ‘independent’ as they act in the interests of the groups they represent.

Two-tier boards meet separately so the supervisory board is not privy to executive discussions about running the business and the management board is not involved in discussions of corporate strategy in the first instance. Members of one board cannot sit on the other and managerial functions cannot be delegated to the supervisory board. Ultimately, the supervisory board has the power to sack all or part of the management board if it does not think the latter is meeting expectations.

BOARD RESPONSIBILITIES

Regardless of a board’s structure, it must take the employee perspective into account. Boards may do so either through the participation of a human resources executive at board-level or by inviting union or employee council representatives to give board presentations.

In addition, good leadership sets the tone and performance standard of a unitary board or supervisory board, as the case may be. It is important to have an effective chair who can run meetings well, establish the trust of her fellow board members and lead a constructive discourse. An effective chair is generally willing to invest in training and development and can deliver appropriate feedback.

Finally, the chair should have sufficient experience and capacity such that she could take over the role of the CEO on an interim basis if the need arose.

BOARD SIZE

While there is no universal consensus on the optimum size of a board of directors, a board that is too large may not be able to work together efficiently or allow for meaningful participation from all directors. On the other hand, a small board can be very effective and, with the right leadership, can become a very collegiate and close-knit team. According to a 2014 study by governance researchers GMI Ratings for The Wall Street Journal, smaller boards engage in deeper debate and are capable of more nimble decision-making.

A unitary board (or supervisory board in a two-tier structure) of about seven members can encompass a diversity of views and have enough members to sit on important board subcommittees overseeing remuneration and audit. However, one challenge for a small board is that as the organisation grows and evolves, it may need to add members with a particular skillset or to staff additional subcommittees.

At fifteen members, board meetings become more staged and formal, but not necessarily less effective. A skilled chair will set an appropriate agenda, solicit contributions from all members and keep meetings moving at a good pace. Defining the scope of a meeting is important in this respect, whether that be the delivery of statutory duties, approving a new corporate policy or debating a business proposal.

Ultimately, the number of board members is less important than how the board is managed.

SELECTING BOARD MEMBERS

Although the unique needs and requirements of every company differ, broadly speaking, a non-executive director will have a breadth of leadership experience, a commercial mind-set, and the financial acumen to add value at a senior level.

The requisite experience and expertise should be coupled with an understanding of what boards do and the right temperament to be a cooperative, but forthright independent director. An independent director should possess good communication skills: they should be a good listener, but also be confident enough to speak up in front of executives and fellow directors when discussions become highly-detailed and even heated.

Ideally, a prospective board member will be a strategic thinker with a breadth of experience in organisations that have matured through different stages of development. Those with a background in change management will be able to hold stakeholders to account on critical proposals and follow through on strategic initiatives. Having served previously on a divisional board or as a trustee is also useful relevant experience.

Finally, whatever form a board takes, it must be filled with people who have the requisite ability and experience to guide the future direction of the business. Board members must be given sufficient information and authority to contribute to the discussion and should be empowered to challenge management decisions when necessary.

BOARD ASSESSMENTS.
WHY THEY ARE NECESSARY?

As companies confront fluctuating economic conditions, digital disruption, globalisation and increased regulatory pressure, the role of the board and its performance have come under greater scrutiny. Companies cannot afford to have boards that aren't performing up to their full potential.

Boards perform better when they receive feedback about what they are doing well and what they could do better. In addition, individual members perform better when they are held accountable for improving their contribution. Board members should be periodically assessed to ensure they are performing well in their roles and that they are living up to their goals and objectives, as well as best-in-class benchmarks.

As this consensus has emerged, board assessments or evaluations have become more widely utilised internationally in both common law and civil law jurisdictions. Evaluations are now recognised as a critical structural tool for assessing the effectiveness and efficiency of both unitary boards and supervisory boards in a two-tier structure.



BOARD ASSESSMENTS.
WHAT CAN THEY ACHIEVE?

> “It is surprising how little most companies spend in terms of time and resources to make sure their supervisory body is functioning properly.”

For both unitary and two-tier board models, the same assessment principles apply. The questions that need to be asked to keep the board running at its peak performance are the same. Namely, is there a common understanding of the board’s objectives? Are all members of the unitary board or the supervisory board aligned as to what they and the organisation are trying to achieve? Are all board members clear about how to fulfil their particular role in trying to meet that objective?

Based on a common understanding of the board’s goals and objectives, board members may then be asked whether they have the adequate information, resources and capacity to tackle the challenges presented by the business and to optimise the effectiveness of their decision-making.

For example, an assessment may be able to identify if the board is spending too much time on the wrong issues. If the objective of the company is to expand into new markets overseas, but 80% of the board’s time is spent talking about issues related to the company’s domestic environment, this is clearly a problem. Board assessments ensure proper alignment between the organisation’s goals and what the board is spending its time on to ensure that appropriate governance and oversight are being provided.

When you consider how important a board of directors is to the functioning of a company, it is surprising how little most companies spend in terms of time and resources to make sure their supervisory body is functioning properly. Indeed, companies tend to spend significantly more on graduate recruitment and management development programmes than they do on assessing the effectiveness of the body overseeing their business. Creating a feedback and assessment loop at the board level is just as important as it is at any other level of an organisation.

Furthermore, board assessments undertaken by an external party can provide a more detailed, objective and impartial evaluation of how a board is functioning and enable transparent, fresh thinking. External assessments provide boards with an opportunity to understand how their performance compares to that of relevant, high-performing benchmarks.

For board members, external assessments provide a good check on whether their current skillset aligns with the company’s strategy and goals and whether their leadership and supervisory performance are optimising company value. External assessments also provide a valuable opportunity for board members to share their views confidentially and to suggest improvements to the management and functioning of the board so that the efficiency and performance of the overall board can be improved.

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BOARD ASSESSMENTS.
HOW SHOULD THEY BE IMPLEMENTED?

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While there are overarching principles and common questions that apply to all board assessments, they can vary significantly in terms of their rigour. Assessments range from an informal board survey to a more formal ‘audit’ that may include one-on-one meetings with directors, observation of board meetings, and a review of operational procedures. For example, how the board’s meeting agenda and other board documents are structured and disseminated and how often the board meets.

Good board evaluations contain quantitative and qualitative findings. Usually the latter infuse the evaluations with rich insights that enhance the usefulness of the quantitative data.

Effective evaluations generally commence with the chair exploring and agreeing the extent of the evaluation of the board and its committees. Depending on the needs of the company, the exercise may be conducted in-house or by an independent external expert. Either way, the right evaluator will be able to absorb relevant sector-specific information, explore sensitive issues and ask the right questions.

For ease and efficiency, an initial assessment can be conducted through an online survey. Typical questions for board members might include: Is the board spending the right amount of time on important topics? Is the balance between determining strategy and overseeing compliance sufficient? Does the board have the right mix of skills and competencies? How effective is the chair at facilitating the delivery of board responsibilities? Is the relationship between the chair and company executives productive and collaborative?

The external facilitator can then conduct one-on-one interviews with each board member to explore their survey responses in more detail. At this stage, specific examples of what could be changed or improved in order to enhance the board’s performance can be elicited. The findings from these interviews can then be presented back to the chair or to the entire board, as appropriate.

Some evaluators also insist upon sitting in on a board meeting. The purpose of this would be to observe the meeting dynamics and the contributions of individual board members as well as the overall quality of the debate and the board’s decision making processes. Observing the board in action can add valuable insight to a board assessment and triangulates with other data gathered through the survey and interviews.

In terms of evaluating the skills and qualities of individual board directors, many different parameters can be considered. Data on a director’s performance can be gathered, either through anonymised peer surveys or by an independent expert. The parameters considered could include their contribution to leadership, financial analysis skills, personal commitment and availability, the value they have added on specific topics, and their interpersonal skills. The breadth of this list reflects the fact that a director’s performance depends on their behaviour as well as their skills and experience.

> “Observing the board in action can add valuable insight to a board assessment.”

How often should board assessments be carried out?

For many companies, board assessments are becoming either an annual or biannual exercise. Some companies do this as a matter of practice; others include board assessments as a requirement in their charter. In any case, they should be undertaken regularly with an independent review every two or three years, or when there have been substantial changes in the composition of the board or a radical re-shaping of the business. This does not mean every company needs to undertake a full board assessment annually, but an annual pulse-taking exercise is advisable.

In the UK, FTSE 350 companies must conduct an externally-facilitated, detailed board assessment at least every three years and more often if there has been a change in the chair or CEO, or a substantial change in the business mix. This requirement imposed by the UK Financial Reporting Council underlines how valuable such assessments can be to shareholders.

Conclusions

In the eyes of regulators and shareholders, the role of the board in safeguarding and increasing corporate value is taking on ever-greater importance. There is thus a growing need to continually assess how effectively board members are performing in their roles and how the board as a whole is helping the company to achieve its objectives.

Board members perform better when they are held accountable by their peers and external parties and when they receive feedback about what they are doing well and what they could be doing better.

Furthermore, regular board assessments ensure proper alignment between the organisation's goals and how the board is spending its time. Setting time aside to consider how the board is performing in its supervisory role and to ensure that it is taking into account the interests of all stakeholders is no longer just a good idea, it's essential to good governance.

MORE INFORMATION

Odgers Berndtson is a leading global executive search firm with a long history of sourcing outstanding chairs and independent directors for a wide range of public and commercial boards, and supporting companies to maximise board effectiveness. Our clients include companies large and small, with many quoted on stock markets from London to New York, Frankfurt to Amsterdam. In addition, our senior leadership services include succession planning, assessment and benchmarking, coaching, and the analysis of skills gaps.

An increasing focus on corporate governance and the need to ensure boards are appropriately-skilled has brought the importance of regularly assessing board skills to the fore. In turn, the knowledge gained from regular board assessments helps those companies to better focus and execute searches for new board members when the need arises.

> "Board members perform better when they are held accountable by their peers and external parties."

About the Authors



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Michaël Mellink is a Senior Partner in the Amsterdam office and Head of the Life Sciences Practice. He specialises in advising clients on board and senior level appointments for Pharma, Biotech, Medtech and Service companies. He works across international markets and a broad range of companies in Life Sciences.

Prior to joining Odgers Berndtson, he worked for Cephalon, a U.S. biopharmaceutical company, where he was General Manager for Benelux operations and European Business Development. He has worked for Eli Lilly and Company in senior commercial and management positions. Michaël holds a Bachelor's degree in Physiotherapy and has studied Orthopaedic Medicine.

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Susanne advises on Board composition and succession of Chairmen, independent Directors and CEOs. Her international client base encompasses Fortune500 and CAC40, to start-ups, multi-generational family-businesses and state-owned enterprises.

Susanne has been helping Boards develop and explore their leadership options since 2003, bringing breadth of insights from multiple sectors to her engagements. Mirroring her early engagements with Odgers in Technology and e-commerce, Susanne maintains a consumer, technology as well as life science and biotech orientation.

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Elizabeth (Liz) has over 30 years as a business consultant, working for global professional services firms, and in the last 15 years focused on advising on Boards, CEOs, the C-Suite and their pipeline of successors. She has worked with organisations across a breadth of private and public sectors on strategic, business, talent management and leadership issues, including Strategic Leadership Capability and Risks, CEO & C-Suite Benchmarking & Succession Strategies, Board Reviews and Top Team Performance, and Realising Leadership Potential through Development.

Liz brings a depth and breadth of expertise to support her passion for optimising organisations strategic performance through releasing the potential of their leadership.

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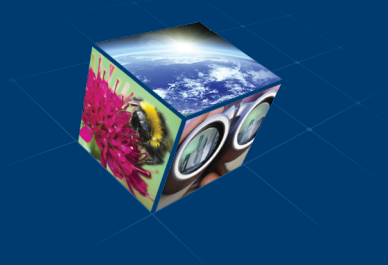
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Kit Bingham is a Partner in the Board Practice at Odgers Berndtson, and Head of the Chair & Non-Executive Director Practice. Kit joined after a career in financial journalism and financial public relations. He was Senior Writer at Financial News, a Dow Jones publication, covering both corporates and the capital markets, with a particular focus on corporate governance reform. In 2007, he joined The Communication Group as a Director of the Financial Practice, with a mix of professional services and financial services clients. He developed and tutored an MBA in board effectiveness at Henley Management College, and graduated from Balliol College, Oxford University, in 1991.

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