

2nd Edition

# ***Board Effectiveness***

## ***What Works Best***



## *Executive Summary*



The economic crisis that began in 2008 increased the focus on both the role of the board and its effectiveness in executing its responsibilities. Boards are under intense scrutiny — from shareholders, regulators, politicians, the media, company employees, and other stakeholders. Directors know that, since their work happens behind closed board-room doors, they rarely receive accolades for helping their companies succeed and avoid problems. But they are in the line of fire when things go wrong.

Given this scrutiny and that they face an ever-evolving landscape, directors should focus on understanding the scope of their key responsibilities and engaging in a considered process to discharge those responsibilities thoughtfully and thoroughly.

### ***What the chapters cover***

#### ***1. Strategy and Implementation***

***Interview insights***  
Boards need to have a longer-term view than their shareholders may have.

— Director

Strategy sets the direction for a company and impacts virtually everything the company does. The right strategy is the starting point for success. The board has a vital role to play in overseeing management's development of the strategy and its implementation. But this is a challenging area because it requires directors to thoroughly understand the company, the industry, emerging trends and risks, and management's assumptions. Equipped with the right information and time, directors can engage in robust discussion that allows them to contribute to management's proposed strategic plan. Ideally, their involvement will help the company adopt the plan most likely to enhance shareholder value. This chapter highlights leading practices for effective board oversight of strategy development and implementation.

#### ***2. Risk and Crisis Management***

Today's companies face a vast array of risks — both known and unexpected. Some risks turn into crises that have significant implications for operations or even a company's future. Given this setting, it's a challenge for boards to get comfortable that risk is addressed appropriately — but it's a critical responsibility. Boards frequently delegate elements of risk oversight to committees — most commonly to the audit committee. But ultimately the responsibility for risk oversight

resides with the full board, and each director should understand the key risks facing the company. This chapter helps boards better understand the changing landscape of risk oversight, management's role in managing risk, and effective ways to oversee the process. It also includes insights on how boards can most effectively discharge their responsibilities when a crisis strikes.

### **3. Corporate Ethics**

Compliance with laws and regulations is critical. But directors recognize it is only the starting point in creating a culture of ethical behavior. The right tone at the top, reinforced by business unit managers throughout the company, is vital to ensure these values cascade to all employees. This chapter provides insights that can help boards understand how tone at the top is set and the role they can play in overseeing company culture, especially in times of change or crisis. The chapter also emphasizes the importance of directors demonstrating ethical behavior.

### **4. Monitoring Company Performance**

Boards use many data points to monitor company performance — including traditional financial metrics and nonfinancial metrics, along with peer and industry information. Knowing what metrics are most effective in helping directors to understand performance and see early indicators of trouble is challenging. Astute directors also know it is important to raise concerns based on a gut feeling — even if their concerns prove to be unfounded. This chapter shares insights on selecting the right metrics, setting and monitoring targets, and effectively sifting through information sources.

### **5. Transformational Transactions**

At some stage, a company will go through a potentially transformative transaction. This could be an acquisition, divestiture, or other business alliance such as a joint venture. The stakes for the company are high in terms of investment, reputation, and whether the deal ultimately contributes to the success of the company's overall strategy. Given the significant potential impact of a deal on shareholder value, boards have a key role in working with company executives to set the stage for successful transactions and maximize their value. This chapter provides insight as to how boards can do this effectively, and outlines key considerations for the different stages and different types of transactions.

#### ***Interview insights***

Directors are committed to doing a good job. Unfortunately, investors and the media tend to focus on the outliers.

— Thought Leader

#### ***Interview insights***

Boards in [our country] may be too polite. We need to push more and think of shareholder value.

— Director

*Interview insights*

One of the biggest challenges for a director is being courageous — being willing to ask difficult or uncomfortable questions.

— Director

## **6. Management Evaluation, Compensation, and Succession**

Executive compensation may be the board responsibility most scrutinized by investors, the media, and other stakeholders. Stakeholders have extensive visibility into executive remuneration levels, but perhaps more limited understanding of the complexity directors face as they try to get it “right.” Boards must balance many factors in reaching compensation decisions — attracting and retaining top talent while incenting behaviors that will achieve long-term shareholder value. This chapter provides insights on effective evaluation and compensation processes and the importance of director independence in making these sensitive decisions. It also deals with the issue of CEO succession — whether planned or unplanned — and offers advice for boards to consider as they deal with this important issue.

## **7. Communicating with Stakeholders**

Disclosure requirements — for financial statements, proxy filings, and other regulatory filings — have become more voluminous and complex and are under greater scrutiny. Stakeholders have also been asking for more information, beyond what companies are required to provide, to really help them understand performance and risks. These factors alone make the board’s role more challenging. In addition, new technologies are changing how companies communicate with stakeholders and how stakeholders and company critics exchange information. This chapter describes how boards can best discharge their oversight responsibilities to ensure that communications are transparent, accurate, and reliable, while balancing stakeholders’ demands for more information.

*Interview insights*

There is a gap between what shareholders and regulators expect boards to do and what boards can realistically deliver.

— Thought Leader

## **8. Board Dynamics**

Composition and leadership are critical in supporting a board’s ability to carry out its responsibilities effectively. Boards need the right combination of skills and experience — and to be alert to the fact that the “right” combination changes over time. They also need a leader who will ensure the board effectively discharges its responsibilities and a process that engages directors most productively. This chapter discusses considerations for board composition and leadership, effective board processes, and training and education.