



Improving board effectiveness

Dr Neville Bain, Chairman of the IoD and co-author of *The Effective Board*, outlines the key elements in creating better board performance

All organisations want to be successful and to improve performance. It doesn't matter whether that organisation is commercial, not-for-profit, or in the public sector.

And there are characteristics that define successful organisations. Such organisations have the right strategy and the right people with the right skills and motivation. They have clear values, well communicated and practised throughout. Leadership of the organisation comes from the board or equivalent body and it is the board that sets the organisation's vision, purpose and values.

A key question is whether the board can improve its performance. Addressing this question is a central task of the IoD's new book, *The Effective Board*. Co-authored by myself and Dr. Roger Barker, the IoD's Head of Corporate Governance, it sets out to build on an earlier publication, *The Effective Director*. The book provides a practical and up-to-date guide to boardroom success.

One of our concerns was to take account of the lessons of the credit crunch and the recession. These tumultuous events delivered a wake-up call to many boards, both inside and outside the financial sector.

Many of the official responses to the crisis, such as the Walker Report and the latest edition of the UK Corporate Governance Code (formerly the Combined Code), have recognised that legislation, regulation and codes of best practice only go so far in shaping boardroom behaviour. More important is the presence on boards of able and motivated directors with a detailed understanding of their role.

The Effective Board seeks to supply at least part of this understanding. It complements the IoD's other efforts to enhance the effectiveness of directors (such as the Chartered Director programme) and offers insights into the wide-ranging roles and responsibilities of directors. Underlying the book is the idea that good governance is a key source of added value and competitive advantage.

The challenge for all boards is to supply a governance framework that delivers long-term success for the organisation in terms of its mission and objectives. Governance should never be regarded as a mere compliance activity.

Key role of chairman

The tone and performance of any board is a reflection of its chairman. The

chairman is elected by the board and has the same legal duties as other directors. But given the importance of the role, in public companies a chairman will usually be appointed after a wide search overseen by the nomination committee. It is essential to match the candidate to the specific needs of the company based on its forward strategy and challenges.

A key task for any chairman is to ensure they have the right balance on the board. This balance is reflected in terms of the ratio of non-executive directors to executive directors, and in having the right skills and experience. Other elements of balance are becoming increasingly important. These include the ratio of female to male directors (see box, page 9) and different ethnic groups, although there are many dimensions of diversity that may be relevant in particular circumstances such as age, nationality, and professional background. This balance should help ensure there is enough challenge and debate, with better decision-making as a result.

Improving board performance

The board is always capable of improving its performance. No board has reached a state of perfection. Even near-perfection can never be taken for granted. The board constantly needs to fine-tune its performance if it is to be sure of being able to respond appropriately to changes in the wider environment. Two areas where boards

have been challenged to up their game are board effectiveness and risk management.

The UK Corporate Governance Code recommends that the effectiveness of the board be reviewed annually and that the senior non-executive director assesses the chairman's performance (based on discussions with the other directors). The wise chairman will hold one-to-one meetings with non-executives at least once a year, to find out how their strengths and weaknesses are perceived and where performance can be improved.

The board appraisal is a useful value-adding exercise and will yield opportunities for improving board performance. This applies to all organisations, not just the commercial ones. The process for making recommendations to improve board effectiveness need not be heavy. The aim should be to limit the process to the essential and devote time to searching for improvements. The new code requires an external appraisal at least once in every three years for FTSE-350 companies.

The board and risk management

A second area emphasised by the Walker Report is for the board to take a greater responsibility for defining the risk appetite and tolerance of the organisation. The board needs to have a good system of risk management and internal control to safeguard shareholders' interests and the company's assets.

This topic has moved higher up the boardroom agenda as the board needs to be satisfied that an appropriate process is in

place to identify, grade and manage risks. While many organisations will delegate the detail of this work to the audit and risk committee (or risk committee, where it is separate), the board will review this quarterly or half yearly. Assessing the risks of a company strategy is a well-defined procedure, most usefully tackled through risk workshops.

Risks are evaluated for impact and probability, and ranked accordingly. High-level risks need to be "owned" and there should be a person responsible for managing each one, although the board as a whole should never delegate overall responsibility. Risk management is not an annual or a financial exercise: it is integral to operational life.

External stakeholders want assurance that the organisation's leaders have the right systems, people and information to reduce exposure to risks and to realise value. Effective boards are not risk-averse, but they're not reckless either.

The need for constant improvement

All boards can lift their game, and *The Effective Board* is designed to support directors in this task. Getting the right balance on the board is an important first step. Two important areas that have received renewed focus in the UK Corporate Governance Code are the board evaluation and the process for identifying and managing risk.

An appropriate approach to these issues will add value to the organisation and enhance stakeholder confidence, including that of the wider community, in the long-term viability of the organisation.

Key elements of board performance

The board should choose the process that will best deliver cost-effective results for their organisation. There is no standard one-size-fits-all template. The main components in a board appraisal are:

- A review of documents including strategy, annual plan, 12 months' worth of board agendas and minutes. This will give clarity over how the board allocates its time
- A follow up of any previous appraisal and recommendations to ensure implementation
- One to one discussions with all board members and the board secretary
- A questionnaire that will enable numeric values to be ascribed to show the weight of feeling to any questions. This is best delivered and evaluated electronically
- A report to the board
- Presentation of the findings and discussion at the board meeting
- Although some appraisers sit in on board meetings to observe behaviours, this can be artificial as behaviour tends to change under observation.

The Effective Board



The Effective Board, by Dr Neville Bain and Roger Barker, is an invaluable guide to best boardroom practice which builds upon and updates *The Effective Director*.

The book reflects changes in the business environment over the past two years, including amendments to the UK Corporate Governance Code. It is based not just on statutory and voluntary codes of conduct, but also on close observation of effective boards in practice.

The Effective Board looks at the lessons to be learned from the 2008 credit crunch and the subsequent economic crisis, and focuses on the key issues no board today can ignore, such as the pensions crisis, sustainability and social responsibility and risk management. Other areas covered include the role of the board and its chairman; the duties

and liabilities of directors; governance and the key board committees; and how to build effectiveness and value through leadership.

"This is an outstanding book of guidance for directors. It is admirably comprehensive and pulls together the fruits of wisdom and experience from many sources. It is a book to be constantly consulted by those wishing to maintain high standards and a wide awareness of directorship in all its aspects," says Sir Christopher Hogg, Chairman of the Financial Reporting Council from 2006 – 2010.

The book is priced at £25 (plus £2 UK postage and packaging).

To order a copy of *The Effective Board* please contact:
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