Has Your Board Hit Its Use-By Date?

by Iain McCormick

THE demands by stakeholders for boards to ensure that effective business strategy is implemented are growing rapidly. Boards of directors must maximise their effectiveness in strategy development and implementation and so ensure they are not in danger of outlasting their use-by dates.

The recent controversy over Hanover Finance has placed those directors in the brightest of spotlights. In December 2008 hundreds of investors expressed their displeasure at the board of the failed finance company. Emotion levels were high with one investor suggesting investors may not live long enough to see the results of the proposed rescue plan.

The *Herald* recently reported that Prime Minister John Key had expressed his displeasure at the price hikes by Genesis Energy and called on the company to reconsider these.

These examples illustrate the critically important role of any board in contributing to effective business strategy that is in line with the reasonable expectations of shareholders.

The way in which boards contribute to strategy development is highly varied. Some boards work with management to jointly develop strategic direction, other boards review and challenge the strategy that management has developed, while some merely rubber-stamp management's strategy.

Brauer and Schmidt, two European researchers, in their 2008 article in *Corporate Strategy* suggest a distinction can be made between two broad schools of thought on board involvement in strategy: the 'active' and the 'passive' school. The 'active' school means that board members act as independent thinkers who actively shape the strategic development of their organisations. While the 'passive' school views the role of a board as to review and challenge strategy.

Studies of corporate governance in the 1970s and 1980s suggested that many boards at that time had little involvement in strategy. In the 1971 book *Directors: myth and reality*, Myles Mace suggested that many boards of directors did not establish objectives, strategies and policies, did not ask discerning questions and did not select the CEO. A frightening situation.

This situation may not be quite as strange as it may seem with management writers such as Henry Mintzberg suggesting planned strategies, the types that are developed in planning retreats, may become irrelevant when new unforeseen opportunities emerge in the life of the organisation. This emergent strategy therefore consists of the sum of the important management decisions made over time. It may be totally different to output of the planned strategy the board was involved in.

KEY STEPS FOR GREATER BOARD EFFECTIVENESS

1. Greater participation of boards in corporate strategy.
2. Shifting from periodic to ongoing board involvement.
3. Striving to improve board communications.
4. Reviewing the information needs of the board.
5. Meeting regularly without the CEO.
6. Considering the skill composition of the board.
7. Providing more coaching and feedback to the CEO.
8. Using more regular board reviews.
9. Updating strategic planning processes.

While in practice effective business strategy is almost always an unpredictable mix of planned and emergent strategy, this in no way justifies a passive approach by the board. Not only is strategy development a requirement of effective board leadership but it is typically hungered for by the CEO.

My own experience from many board reviews in New Zealand and internationally is that most CEOs see the board as having a critical role in strategy but the reality of the board's input into strategy sessions is often disappointing to the CEO. This hunch of mine is confirmed by David Nader in a paper entitled "What's the board's role in strategy development?: Engaging the board in corporate strategy", in *Strategy & Leadership*, 2004. Nader suggests that while CEOs believe that participating in corporate strategy is the second most important activity that their boards undertake; CEOs rate boards as poor and give them only 11th highest ranking for their performance in this area.

If the board's role in strategy is important in more normal times, it is vital in the current global economic climate.

Andrew Tuch, co-editor, Harvard Law School corporate governance blog, suggests the following to help the board maintain its utility in these troubled times:

1. Greater participation of boards in corporate strategy Tuch suggests that boards have become significantly more involved in corporate strategy in recent years. This is a result of a number of reasons including: boards striving to be more proactive, the increased importance of activist investors, and directors' own desires to be more engaged in corporate strategy, especially when their companies are undergoing rapid changes or facing turbulent events. The active school of board involvement in strategy development is seen as critical.

2. Shifting from periodic to ongoing involvement Boards are becoming much more involved in assessing the effectiveness of the strategy as it is implemented over time. This ongoing, real-time engagement enables both the CEO and the board to learn the lessons of the moment and adjust direction as, or before, the environment changes.

3. Striving to improve board communications Boards are carefully focusing on the level of discussion of corporate strategy and on keeping these at the appropriate level. This means ensuring that high-level issues are tackled in a way that has direct practical implications for the organisation. It also involves the chair assertively telling directors if the discussion is becoming too tactical. Robust discussion and effective challenge of communication styles is critical but it needs to be done in a supportive and future-focused manner.

4. Reviewing the information needs of the board The quality, layout, structure and timeliness of board papers are frequently topics of discussion for many boards. Directors are increasingly concerned that the board is getting the critical information it needs to have effective input into strategy decisions. The board not only requires up-to-date financial and market data but also important information about assumptions that lie beneath the strategies, the alternative strategies that may have been considered and risks that are associated with each alternative.

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5. Meeting regularly without the CEO Meetings of the independent directors without the CEO allow for full and candid discussions about both strategic options and decisions. Even directors with frank and open attitudes often find it easier to discuss some strategic matters without the CEO. These meetings enable the biases and predilections of the CEO and management to be clarified and if need be plans made for rectification.

6. Considering the skill composition of the board The chair should assess the skill mix and level of the board on an annual basis and ensure the requisite strategy skills are available. These include not only innovative thinking skills but also the ability to develop alternatives to proposed strategies, the capacity to assess alignment between organisational capability and strategy, the fortitude to relentlessly track strategy even when the temptation may be to move onto other matters, the ability to develop measures which monitor strategy implementation effectively.

7. Providing coaching and feedback to the CEO Chairs and CEOs I have worked with increasingly find it useful to have a session together shortly before the board meeting. This enables the chair to help the CEO better prepare for board discussions of strategy. Together they can talk though likely questions and challenges that may be raised in the board meeting. Their collaboration becomes even more critical in an economic crisis when poor company performance can be misconstrued as unacceptable CEO performance.

To this list I would add the following:

8. Using more regular board reviews I have found a consistently increasing demand for board review, especially with specific peer assessment of the effectiveness of the board in the strategy area. These reviews help to highlight strengths and weaknesses allowing boards to craft professional development plans to ensure ongoing development.

9. Updating strategy planning processes, including:

- Frequent market updates. These consist of the routine information that is contained in board papers such as sales levels, gross margins, market share and order sizes. However boards increasingly want market updates on competitors' pricing, competitor staff turnover, advertising levels and so on.
- Strategic thinking updates. The world of strategic thinking and strategic planning is one of the most lively and vigorous discussed in business journals and newspapers. There is a constant stream of fascinating in-depth new approaches to strategy for directors to read with one recent example being the *Harvard Business Review* on green business strategy.
- Strategic planning methodologies. There are many new approaches to keeping strategic planning fresh and stimulating for boards. An example is the New Zealand developed strategic planning software BizVision (*www.bisvision.com*) which allows organisations to scan the environment, assess their capability, develop a vision, build a business plan and plan strategy execution using a set of simple question cards and a fun computer interface.

The demands that the global economic crisis is making on strategic input from the board are even more important than these have been in the past. There are a wide range of practical actions boards can take to improve their utility in these troubled times. At the heart of improvements is the ability of the board to reflect on its own performance in a critical but constructive manner. Every director should challenge themselves at the end of each board meeting with the question – "Did the board meeting add value to the strategic direction of the organisation?" If members are courageous enough they can also ask – "What is the use-by date of this board?"

Iain McCormick is the managing director of www.directorevaluation.com. He undertakes board reviews in New Zealand and internationally. His analysis for this article is based on a review of the business journals and newspapers on governance and boardroom dynamics and on interviews with directors, CEOs and senior executives.