The art & science of creating an effective board

A directors’ guide to the essential attributes of high performing boards

Whitepaper produced by Board Agenda in association with Brainloop
BOARDS ARE COMING under more scrutiny and pressure than ever before from regulators, investors and the public to be effective and to continually raise their performance in the wake of the financial crisis, scandals and incompetence.

More accountability is called for, which brings further complexity to the responsibilities of the corporate board. It is a challenging time for directors, especially those who work hard and put in long hours but are still not getting the successful outcomes they seek. An effective board is only as good as the parts and processes that go into it, but it also takes strong leadership to pull together the different elements in a cohesive and insightful way in order to become truly effective.

Against this background, Board Agenda has brought out a directors’ guide, *The art & science of creating an effective board*, as a useful steer towards high performance. The guide focuses on the processes, structure, behaviour, values and dynamics that make up an effective board and how directors can strive to raise their game. It is designed for corporate boards—from large to small-caps—and not-for-profit companies.

Governance experts agree that boards that are willing to go beyond the basics, guard against complacency, and are unafraid to change behaviour are the ones that become best performers.

### Key insights at a glance

<table>
<thead>
<tr>
<th>Best board composition</th>
<th>Find the optimum mix of skills, experience, behaviour and diversity to create a truly effective board. Recognise that the process is continual and transparent as new challenges arise</th>
</tr>
</thead>
<tbody>
<tr>
<td>Board structure clarity</td>
<td>Clearly define roles to avoid any overlap of responsibility and make sure the board and committees understand how they relate to each other. Getting the balance right is a powerful contributor to a well-calibrated board</td>
</tr>
<tr>
<td>Good information flow</td>
<td>Collect, share and store accurate, transparent and timely information, which is crucial for good decision-making on high-performing boards</td>
</tr>
<tr>
<td>Culture matters</td>
<td>Effective board members must be company ambassadors who shape, follow and spread the company culture and fully understand the values and behaviour that drive it. A clear, shared vision of the company and its purpose is essential</td>
</tr>
<tr>
<td>Forward-looking boards</td>
<td>Plan a future agenda, as well as a current one, and strike a balance between creating and protecting value, while including sustainable long-term strategy</td>
</tr>
<tr>
<td>Engagement and dynamics</td>
<td>Be fully engaged and well prepared to ensure productive meetings and the best use of time. High performers know that mutual respectful and professional behaviour are critical to a healthy working environment and to resolving conflict</td>
</tr>
<tr>
<td>Regular reviews</td>
<td>Carry out constructive evaluation of individuals, the board and committees through the use of periodic, internal and external reviews for best practice. Boards that learn from review feedback are the ones that become high performing</td>
</tr>
</tbody>
</table>
Creating an effective board is the bedrock of a healthy, well-run business. It is an ever-evolving process that needs fine-tuning and adjusting to achieve a balance of members who can make good, insightful decisions and work well together.

This sounds easy but to build a successful, high-performing board takes a lot of hard work. It requires the best mix of skills and expertise, and carefully selected executive and non-executive directors who are diverse in background.

Board composition and size vary across European member states, says ecoDa, the European Confederation of Directors’ Associations, and the IFC, in their Guide to Corporate Governance Practice. Taking this into account, they recommend boards should not be “so large as to be unwieldy” and that the balance of skills and experience are “appropriate for the requirements of the business”.

How board members are appointed is an important part of the process. Nomination committees, which are responsible for board recruitment, must identify the gaps in the skills and expertise of the existing board and recruit members who will deliver. Ensuring there is a good technical skill set and keeping up with current trends and challenges, especially in cybersecurity, is vital.

A good chairman will add his or her views to create the best-performing board. The nomination committee must also plan ahead for new appointees when people reach the end of their service term, including detailed succession planning for chief executives and chairmen. Contingency planning for unforeseen departures is also vital.

A well-planned recruitment approach should be agreed with management for senior appointments and the recruitment process should be thorough and transparent at all stages. Good groundwork providing a clear description of duties and personal characteristics required, and an outline of the values and challenges facing the company, are useful for everyone involved.

The UK Corporate Governance Code requires FTSE 350 companies to publicly advertise roles or use a search consultancy, and also to disclose the information in the annual report. Choosing a recruitment firm with a diverse talent pool is a savvy step towards selecting a wide range of potential candidates, including at executive level.

Diversity in the broadest sense – gender, age, ethnicity, outlook and social background – plays an important part in the mix. This holds good for large, mid and small-cap companies, as well as charities. In its 2018 Guidance on Board Effectiveness, the Financial Reporting Council states that “diversity in the board room can have a positive effect on the quality of decision-making by reducing the risk of group think”. This can be challenging to achieve, especially if the chairman feels more comfortable recruiting a member who shares similar views and background. Effective boards put in place a good gender mix at executive as well as non-executive level.
**Personal qualities** Industry knowledge and executive board experience are essential to a high-performing unit but other personal attributes are equally important. Directors need to be capable of clear, strategic thinking, have the ability to debate key issues constructively in the boardroom and ask challenging questions. They also need to listen to other members when they present their views, a personal skill that is sometimes lacking around the table. High-performing boards achieve a fine balance between thinking independently and being culturally sensitive to other members.

## Board structure

Governance experts agree that the **chairman** is the pivot of an effective board. Regardless of the skills and expertise of other members, the board will be unable to function well if the chairman is weak, lacking vision or unable to tackle new challenges and trends that the company faces in a rapidly changing external environment. The role of the chair is to set the board agenda and tone of discussions, and make sure each member understands and carries out their responsibilities. Tapping into the views of all stakeholders, including customers and shareholders, is important. A good chairman fosters trust with the board, knows how to be consensus-seeking and authoritative, and encourages a participatory environment.

A good relationship between the chair and the **CEO** is vital. The FRC’s board effectiveness guidance states that it is “a key influence on board effectiveness”. Clearly defined roles, avoiding responsibility overlap, contribute to an effective working rapport. It is the chief executive who proposes strategy, and establishes the culture of the organisation—both of which are agreed by the board—and makes sure members understand the views of senior management on business issues.

In a well-tuned, effective board, **executive** and **non-executive members** bring different experiences to the table, and although executives are often seen as board leaders, non-executives have a vital part to play. Good, seasoned executives are willing to share their deeper knowledge of the business and day-to-day operations with other members, while non-executives bring a broader, external view to issues and, when necessary, provide constructive challenge as part of the governance process. Listening skills are important for all directors. Getting the delicate balance right on this is what distinguishes high-performing boards from average ones.

The **senior independent director** is another key player and particularly valuable if there is a dispute between the chair and chief executive, or if non-executives or shareholders believe they are not being listened to. The European Commission recommends a list of criteria that independent directors should fulfil, including not having been an executive or managing director of the company or an associated company in the previous five years, or representing or being a controlling shareholder.
The glue that permeates the entire board and organisation is the company secretary, who works with all parts of the board and committees, supports the chair in the smooth running of the team, advises directors on governance and compliance issues and organises professional training.

Best-performing boards set out the responsibilities of committees such as audit and risk, remuneration and nomination, and make clear how they relate to it. Boards tap into the advice of each committee but take overall responsibility for decisions on appointments, audit, risk or pay.

**Information flow**

Accurate, comprehensive and timely information is the oxygen of effective boards. Without this, directors cannot ask informed questions to senior management, mitigate risk or make good decisions. Non-executive directors, in particular, should insist on receiving high-quality information in advance of a board meeting in order to be able to discuss issues, according to the FRC’s board guidance. Internal and external information on market conditions, competitors, political, economic, social and technological change give boards a broader picture and an edge in becoming high performing.

As pressure builds on boards to get the right information at the right time, the task of collecting, sharing and storing information is vital and discerning chairmen are increasingly using digital board packs to improve efficiency. “A good portal helps the collaborative process of clear information building, provides continuity between meetings, and a transparent audit trail,” says Thomas Deutschmann, CEO of Brainloop, a board portal provider.

**Clear vision and culture**

In order to be effective, boards need to have a clear and common vision of the purpose of the company, and the values and behaviour that shape its culture, as these have a profound impact on thinking and decision making. Company culture, which is defined by the board, must come from the top, and all board members should deliver it so that it becomes embedded throughout the organisation. They should also match their own values and behaviour to its standards. In its 2017 good practice guidance on culture, the Institute of Business Ethics encourages an open culture where people can speak up about concerns and be confident they are listened to.

Establishing a clear vision and culture is very much a shared task between the CEO, chairman and entire board. If directors see that the CEO is not supporting the culture then they need to challenge him or her. An insightful board is not afraid of change that leads to improved behaviour and better outcomes.
Strategic focus

High-performing boards spend time shaping an agenda for the future rather than just tackling current issues or looking backwards. Boards that take a longer view are much more likely to see relevant changes on the horizon, including opportunities and risk, and are better placed to protect value. It takes knowledgeable directors to build a forward-looking board, whether it is looking ahead to CEO succession, identifying and filling gaps where skills or experience are missing, or investing in training for risk management and new technologies. It is all part of creating a sustainable long-term strategy.

Board engagement and dynamics

The amount of time boards spend on meetings is on the rise but that does not always feed into improved efficiency and decision making. One recent survey suggests that directors become too engrossed in strategy and fail to leave time for risk management, talent management, governance, stakeholder management and other value-adding tasks.

A far-sighted chairman who is striving to improve board performance and impact will make sure all areas of board work are covered through an efficient use of time. He/she will also make sure every member of the board is engaged in the process, and well prepared to contribute, in order to get the most out of the team. Some board members will have specific expertise—in technology or risk—and a good chairman will draw on these skills during meetings. The chair should also allow time to deal with tough questions and a follow-up when needed. An engaged board will make the most of limited time.

Board engagement with shareholders, customers, and employees should also be part of the agenda, particularly at a time when pressure is increasing from wider stakeholders.
Getting the **boardroom dynamics** right is a fine art. Some members tend to dominate the discussion and others fail to contribute, which is when an experienced chairman must take control. Behaviour between board members should be respectful; this is particularly helpful if areas of conflict arise. Respect and understanding of different roles also applies to conflicts between management and the board, which the chairman should oversee. The senior independent director has a valuable role to play in resolving conflict.

## Board evaluations

Objective, rigorous evaluation—whether it is internal or external—is crucial to improving board performance. Directors striving to be more effective are open to scrutiny and use the feedback to work on weaknesses and further improve strengths. Evaluation helps to assess the effectiveness of individual directors, company secretary and committees, and also how they relate to each other. High-performing boards will also make sure an evaluation of the audit committee is carried out to determine the quality of work on audit, risk and internal control.

The Corporate Governance Code recommends that FTSE 350 companies have external board evaluations at least every three years because they bring a fresh perspective and a keen eye to boards. Companies are also required to carry out internal evaluations on an annual basis. Guidance from the Charity Governance Code for not-for-profit companies are advised to follow suit, with larger charities required to carry out a three-year external review. Smaller companies and charities are increasingly seeing the value of board and trustee appraisals too and organisations such as ICSA: The Governance Institute provide guidance questions to help charities make internal evaluations.

ICSA believes board evaluations have “an important part to play in identifying and correcting weaknesses and optimising performance”, and is leading a group review of the quality and effectiveness of board evaluations with the aim of setting up a code of practice for external evaluators. The move is part of the UK government’s attempts to raise governance standards in business and will boost efforts by boards seeking to be more effective.
Summary

While each board will be affected by specific compliance and regulatory requirements of its location and sector, there are some facets of successful, high-performing boards that are common to all types of organisations. *The Art & Science of Creating an Effective Board* is a guide that provides actionable advice about these key determinants of success.

These include creating an optimum board composition, via the establishment of a well-planned recruitment approach and achieving diversity in outlook as well as ability and experience. Board structure, the importance of role division and responsibility, and avoiding task overlap is at the centre of a well-run board. There must also be clear internal communication guidelines within the board so that there is effective sharing of quality, up-to-date information—to and from the board. This is a paramount issue, at a time when gathering, assessing, communicating and protecting accurate data and information is at a critical point.

Every high-performing board needs to establish, direct, observe and measure corporate culture across the entire organisation. The board must also set aside time for a strategic focus where the agenda looks to the future, as well as tackling present challenges. Value is inextricably linked with reputation and so meaningful engagement by boards with all stakeholders is now, more than ever, a critical success factor. Management of personal behaviour and the relationship dynamics within the board are also key to creating effective boards.

Finally, the need for thorough internal and external evaluations to spot weaknesses and strengths is a vital step. Learning from the reviews and putting the findings into action will prove the real test and mark out high-performing boards from average ones.