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Building a forward-looking board

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Directors should spend a greater share of their time shaping an agenda for the future.

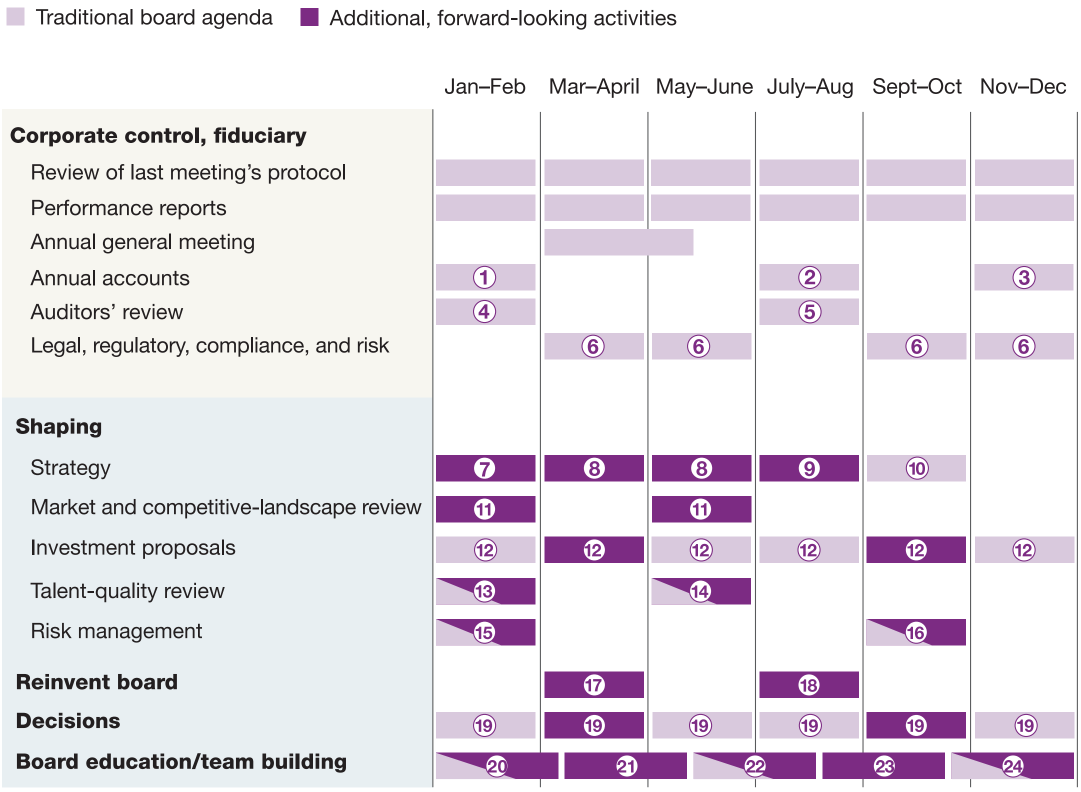
Debate over the role of company boards invariably intensifies when things go wrong on a grand scale, as has happened in recent years. Many of the companies whose corpses litter the industrial and financial landscape were undermined by negligent, overoptimistic, or ill-informed boards prior to the financial crisis and the ensuing deep recession. Not surprisingly, there's been a renewed focus on improved corporate governance: better structures, more rigorous checks and balances, and greater independence by nonexecutives, for example.

Governance arguably suffers most, though, when boards spend too much time looking in the rear-view mirror and not enough scanning the road ahead. We have experienced this reality all too often in our work with companies over several decades. It has also come through loud and clear during recent conversations with 25 chairmen of large public and privately held companies in Europe and Asia. Today's board agendas, indeed, are surprisingly similar to those of a century ago, when the second Industrial Revolution was at its peak. Directors still spend the bulk of their time on quarterly reports, audit reviews, budgets, and compliance—70 percent is not atypical—instead of on matters crucial to the future prosperity and direction of the business.

The alternative is to develop a dynamic board agenda that explicitly highlights these forward-looking activities and ensures that they get sufficient time over a 12-month period. The exhibit illustrates how boards could devote more of their time to the strategic and forward-looking aspects of the agenda. This article discusses ways to achieve the right balance.

Exhibit

How forward-looking boards should spend their time



Details on selected activities (all others are self-explanatory, as labeled)

Fiduciary
1. Annual accounts
2. Annual budget directives
3. Next year's budget
4. Auditors' report
5. Audit-planning approach
6. Audit-committee reviews

Strategy
7. Set framework for the year
8. Define broad options
9. Outline/select options
10. Approve final strategy approach
11. Review strategic and competitive position, key performance indicators

Investment
12. Engage in ongoing review of investment proposals

Talent
13. Set talent-review objectives for the year
14. Review top 30–50 people

Risk
15. Determine risk-review objectives for the year
16. Conduct annual risk review, including mitigation approaches

Board reinvention
17. Conduct board 360° evaluation
18. Determine approach for board-process enhancement

Decisions
19. Engage in decision making—eg, on budgets, investments, M&A, and key nominations

Board education
20. Travel with sales staff, customer visits
21. Visit R&D facilities
22. Visit new geographies
23. Inspect production sites
24. Attend customer conference

The case for change

Our conversations with successful chairmen showed a strong continuing bias toward fiduciary tasks but also a desire and willingness to shift focus. “Boards need to look further out than anyone else in the company,” commented the chairman of a leading energy company. “There are times when CEOs are the last ones to see changes coming.”

This forward-looking imperative comes in part from the way long-term economic, technological, and demographic trends are radically reshaping the global economy, making it more complex to oversee a successful multinational business. As executive teams grapple with the immediate challenge of volatile and unpredictable markets, it’s more vital than ever for directors to remain abreast of what’s on (or coming over) the horizon.

Second, and compounding the short-term executive mind-set, the length of CEO tenures remains relatively low—just five to six years now. That inevitably encourages incumbents to focus unduly on the here and now in order to meet performance expectations. Many rational management groups will be tempted to adopt a short-term view; in a lot of cases, only the board can consistently take the longer-term perspective.

Distracted by the details of compliance and new regulations, however, many directors we meet simply don’t know enough about the fundamentals and long-term strategies of their companies to add value and avoid trouble. It doesn’t have to be this way. A select handful of banks and other multinational corporations with prudent, farsighted, and independent-minded boards not only survived the financial crisis largely intact but also continue to thrive.

Rather than seeing the job as supporting the CEO at all times, the directors of these companies engage in strategic discussions, form independent opinions, and work closely with the executive team to make sure long-term goals are well formulated and subsequently met. How can a board better focus on the long term and avoid becoming a prisoner of the past?

Foundations of a forward-looking board

Board chairmen and fellow directors will quickly grasp the point by studying the exhibit. The light-purple part of the annual schedule depicts how a board preoccupied with its fiduciary responsibilities typically spends its time. The dark-purple agenda items, by contrast, show what the calendar focus of a predominantly forward-looking board might look like. It’s impossible to effect this change without a solid foundation: the right directors, knowledgeable about their roles and able to commit sufficient time.

Roll back the future to access top board members

Too often, vacancies on a board are filled under pressure, without an explicit review of its overall composition. An incoming chairman should try to imagine what his or her board might look like, ideally, three years from now. What kinds of skills and experience not currently in place will help fulfill the company's long-term strategy? What, in other words, is the winning team? A willingness to look ahead expands the number of candidates with appropriate skills and heightens the likelihood that they will sign up if and when they become available.

One of the world's leading food companies used this approach to introduce a range of expertise clearly reflecting its strategic direction and requirements. Of course, its board has high-profile (former) executives and top professionals with a profound finance, risk, or general-management background and diverse geographic experience. But now it also includes people with successful track records in health, nutrition, the public sector, and welfare. Other companies need specific kinds of expertise to help them adapt to cutting-edge technologies or market disruptions. Here, advisory boards without formal governance authority are especially useful.

Define the board's role clearly

The familiar roles of a well-functioning board—such as setting strategy, monitoring risks, planning the succession, and weighing in on the talent pipeline—are easy to list. But in practice, things are never simple. CEOs and their top teams, for example, are often touchy about what they see as board interference. Equally, weighty boards with years of experience and members used to getting their own way are frequently frustrated because they can't intervene more actively or their advice is ignored.

It's critical to defuse these tensions at the outset by clearly defining the board's role and establishing well-understood boundaries. Unless roles are clear, the relationship between the CEO and management, on the one hand, and the board, on the other, risks devolving into misunderstandings, loss of trust, and ineffectiveness. An annual discussion between the board and management, perhaps including a written letter of understanding setting out the roles of each party, is always a productive exercise. For instance, a large Nordic investment company creates work and role descriptions, for the board and management, that are reviewed and approved every year. This process always generates valuable discussions and makes roles more clear.

Get your board to work harder

Most board members we know are hard working. The old caricature of long lunches and big stipends is just that—a caricature.

Yet the 10 or 12 days a year many board members spend on the job isn't enough, given the importance of their responsibilities. Several well-performing boards prescribe a commitment of up to 25 days of engagement for nonexecutive board members.

Some of that extra time should be spent in the field. Boards seeking to play a constructive, forward-looking role must have real knowledge of their companies' operations, markets, and competitors. One big international industrial company we know requires all its board members to travel with salesmen on customer visits at some point each year. Other companies ask their directors to visit production and R&D facilities. The chairman of a manufacturing company we interviewed adds that "You can't fully understand the business, analyze the competition, review succession plans, visit a company's facilities, travel with salespeople, and set strategic goals by working a handful of days."

How can companies achieve the right degree of commitment? Higher pay will not be the answer, even if there were no governance watchdogs who would doubtless conclude that directors are already well paid or at least rarely need the extra money. The question of pay has never been an issue at a major oil company that requires its board members to set aside 30 days a year, for example. What does actually help (as in this case) is a board environment that encourages participation and allows board members to derive meaning, inspiration, and satisfaction from their work. The reward for individuals will be an opportunity to enhance their reputation for good boardroom oversight, to strengthen their personal networks, and to influence decisions.

Putting the board's best foot forward

The best boards act as effective coaches and sparring partners for the top team. The challenge is to build processes that help companies tap the accumulated expertise of the board as they chart the way ahead. Here are four ways to encourage a forward-looking mind-set.

Require the board to study the external landscape

As a starting point, says the chairman of a finance company, "We invite renowned experts and professionals in various fields—such as technology, regulatory matters, and economics—to board meetings, who talk about specific topics." Board meetings also may be held in overseas locations where directors can be exposed to new technologies and market developments relevant to a company's strategy.

To be able to challenge management with critical questions, a company's directors should regularly compare internal performance data with those of their competitors across a range of key indicators. The chairman of one telecommunications company says his board "regularly develops an outside–in view of the industry and business from public information. And from time to time, we seek outside advice to get an independent view on the firm's strategy and new potential development areas."

Make strategy part of the board's DNA

The central role of the board is to cocreate and ultimately agree on the company's strategy. In many corporations, however, CEOs present their strategic vision once a year, the directors discuss and tweak it at a single meeting, and the plan is then adopted. The board's input is minimal, and there's not enough time for debate or enough in-depth information to underpin proper consideration of the alternatives.

What's required is a much more fluid strategy-development process: management should prepare a menu of options that commit varying levels of resources and risks. In this way, board and management jointly define a broad strategic framework, and management defines options for board review. Finally, during a special strategy day, the board and management ought to debate, refine, and agree on a final plan. "At the beginning of the annual planning process, the board's role is to help management broaden the number of strategy options," says the chairman of a large transportation company. "At midyear, it is to discuss strategic alternatives and help select the preferred route, and at end of year, it is to make the final decision to implement."

Strategy should always provide the context for proposed acquisitions or stand-alone investments. "Without reference to long-term objectives, stand-alone investment proposals do not make much sense—but they are not unusual," says the chairman of a bank. Strategy and policy go hand in hand. Policy is not only among the most powerful tools a company can use to propel its culture and employee behavior in new directions but can also contribute significantly to the effective implementation of strategy. Yet most boards are aware of neither the full set of company policies nor their content.

Unleash the full power of your people

Forward-looking boards are powerfully positioned to focus on long-term talent-development efforts because they understand the strategy and can override some of the personal ties that cloud decision making over appointments. Divisional managers, say, might be tempted to hang on to high performers even if the company's interest would be to reallocate their skills and experience to a business with more potential. For example, a large media company, prompted by its board, recently reassigned its strategic-planning director to lead digital development projects on the US West Coast. The move was remarkably successful: working in close cooperation with some of the most accomplished digital giants in the United States, the business quickly got up to speed on the newest technological trends.

Many forward-looking boards hold annual reviews of the top 30 to 50 talents, always with an eye on those who might eventually be suitable for key executive roles. Here's how the process works in one manufacturing company. Each executive director selects, for presentation to the board, three to five promising managers. The board gets a photograph, information on their educational background, and performance reviews over the last three years. The presenter organizes the information on an evaluation grid showing categories such as performance, leadership, teamwork, and personal development. The directors then spend 10 to 30 minutes on each person, discussing key questions. How can the company coach and develop talented people? What personal and professional development opportunities, such as an international posting, might help broaden an individual's experience? What are the potential next career steps? In addition, during corporate projects, client gatherings, and trade shows, directors should take any opportunity to meet—and assess—upcoming executives and fast trackers informally.

The key is that the board must agree with management on a sensible approach to reviewing executive talent. Appointing a board member with a successful people-leadership track record to lead the effort is one way of boosting its impact.

Anticipate the existential risks

Every company has to take significant risks. But while it has long been understood that overall responsibility for risk management lies with boards, they often overlook existential risks. These are harder to grasp—all the more so for executives focused on the here and now—yet harm companies to a far greater extent than more readily identifiable business risks.

"Instead of only discussing competitive risks, boards should put in place a well-functioning crisis-management system" for cybercrime, insider trading, or corruption, says a consumer-goods company chairman conscious of the dangers of corporate secrets falling into the wrong hands. "We want to be ready for existential risks if they occur."

The best-managed companies in safety-sensitive sectors such as oil or autos—where a rig explosion or product recall could have significant consequences for large numbers of people or cost a year's profits—are already vigilant in this area. The board of one oil-exploration company we know regularly receives reports on the safety record of its on-platform activities. The reports trigger intense discussions about the root causes of problems and remedial action where there is any deviation from norms. The boards of other businesses should also demand that management supply quarterly reports (probably to the audit committee) on the observance of safety, quality, and ethical standards and hold management to account. Directors of a media company, for instance, could regularly ask its news executives to lead reviews of editorial standards.

Yet even the best systems will not identify all the risks, and boards and management must somehow try to grasp the unthinkable. The best way may be to tap into the concerns and observations of middle management, the group most likely to be aware of bad practices or rogue behavior in any company. Boards have a duty to ensure that management teams pursue bottom-up investigations (through confidential questionnaires, for instance), identify key risk areas, and act on the results.

Forward-looking boards must remain vigilant and energetic, always wary of bad habits. An objective 360-degree review, built on personal interviews, is generally a much better option than the box-ticking self-evaluation alternative. Winning boards will be those that work in the spirit of continuous improvement at every meeting, while always keeping long-term strategies top of mind. Only by creating more forward-looking boards can companies avoid the sort of failures witnessed during the last financial meltdown the next time one strikes.

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