# Evaluating Individual Directors

## by Mark Edwards and Susan F. Shultz

**Board evaluation of individual directors has been a governance ideal for some time—but often remains *only* an ideal. Yet with a growing need for each director to contribute strong, unique skills to the governance mix, tools which allow effective, fair assessment of each member are now an imperative.**

Despite the onslaught of attention, regulations and market forces, change in governance practices is sluggish, deliberate and measured. In no area is this more apparent than in board assessment. Yet today, transparency and accountability are not only expected, but mandated; and over 86 percent of public companies now conduct some form of board assessment.

However, until now, director evaluation has been scorned and too often ridiculed and dismissed. Directors are acutely sensitive to liability and thus embrace credible ways to demonstrate their effectiveness and filter risk exposure.

Most board charters require individual assessments. Institutional Shareholder Services ranks companies higher for rating individual directors. In 2005, 20 percent of public company boards conducted some form of individual assessment. In 2007, according to an NACD study, 46 percent of public companies conducted individual director evaluations. The trend is not likely to change.

The evaluation of board members brings unique challenges to the assessment process. Directors may feel they are above evaluation, and that simply showing up and asking questions proves that they are contributing to the board. Unfortunately, there is no correlation between attendance and asking questions and the value of a director's contribution.

Boards, similar to any team, need credible assessment that identifies strengths, weaknesses and obstacles. The resulting information, combined with teambuilding and leadership development, eases barriers to effective board governance. In today's environment, we know the heightened value of each director. We know the importance of rotating underperforming directors off the board and bringing on new, value-added directors. We all know who the non-performing directors are on our boards. Yet, allegiances naturally are to those we know, our fellow board members. So we rationalize retaining underperformers.

**Directors have strong egos and tend to blame others for dysfunctions. The only way to overcome this impasse is with credible individual assessment.**

Board management is difficult or impossible without credible measures because members fail to agree on specific problems to address. Directors tend to have strong egos and typically blame others for dysfunctional behaviors. The only way to overcome this impasse is credible individual assessment.

Obstacles to board effectiveness that can be moderated by strong behavioral metrics include directors who:

- ☐ Talk too much.
- ☐ Go off on irrelevant tangents.
- ☐ Ask questions that show they do not understand the business.
- ☐ Interrupt others and fail to show courtesy.
- ☐ Use their phones, PDAs, or other devices during meetings.
- ☐ Use a confrontational communication style.
- ☐ Contribute only in their narrow area of expertise.
- ☐ Micromanage.

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☐ Focus backward instead of forward.

☐ Jump to solutions before understanding the issue.

☐ Have problems with attendance, punctuality or meeting preparation.

☐ Rigidly block change.

☐ Are very risk averse.

Each of these behaviors degrades board effectiveness. Sometimes a strong lead director or CEO can help coach a director but denial can undermine the motivation to change.

Boards often talk about becoming more effective but fail in action. Without accurate information on board effectiveness and the performance of individual directors, training and development are limited to generic "feel good" actions. Common board development training examines directors' style or approach to solving problems, but may not drive change.

Strong assessment can provide the board with a targeted approach to solving issues among directors and for developing lagging directors. Strong and credible measures enable the board to address exactly the issues needed, and individual directors can create an action plan to develop the skills that create the most value.

**Many boards only pay lip service to individual assessment. If done at all, it is typically too general and informal.**

☐ *Evaluation requirement.* There should be a statement in the charter of all boards, public and private, for profit and nonprofit, to conduct regular independent, confidential assessments of the board, the committees and the individual directors. We get what we measure. Evaluation provides a rational basis for measuring board effectiveness and serves as the foundation for board training and development.

Many boards only pay lip service to individual director assessment. If done at all, it is typically too general and too informal to provide value. Most frequently, assessment is conducted internally with the help of staff, or a consultant who compiles a questionnaire or simply talks with the directors.

## Board Member Strategy Matrix

### Where Do Your Directors Fit?

| | Low Analysis | High Analysis |
|---|---|---|
| Strong Preparation | **Modest Contribution 10%** | **High Performance 70%** |
| Weak Preparation | **Low Performance 5%** | **Modest Contribution 15%** |

Director feedback may come from a lead director, administrator, CEO or other source and is typically informal and unstructured. Some boards use a lead director to collect comments about board members and circulate a questionnaire compiled by staff members or a board member.

The lead director knows that directors are reluctant to criticize their board colleagues. Consequently, lead directors typically report that directors are satisfied with one another. Often, such reports emphasize issues like attendance and punctuality because those are easy to measure. Because they have been difficult to capture, they ignore the substantive, qualitative issues that define the best directors.

☐ *Discovery.* Many boards have expressed a desire for credible director evaluation but, too frequently, perceived and logistical obstacles block an effective approach.

One of the main issues is concern over legal liability and whether director evaluation is discoverable. Discovery, whereby a claimant in a lawsuit may demand to see actual director ratings in a court action, is still untested. If discovery is possible, then the assessments by other board members and respondents would not be anonymous.

In order to gain valid feedback, two conditions must hold:

▫ Anonymity to those who provide assessment information.

▫ Appropriate confidentiality to those who receive feedback.

## Example 360° Assessment
### Board Make-up vs. Company Needs

At the Board Institute, we recently conducted individual, 360º assessments of the directors of a NASDAQ-listed company.

A total of nine directors serve on the board, two of whom are women. Two of the directors have served on the board 21 years and are over age 70. There are two new members who joined the board in the last six months. All but one director qualifies as an independent.

The company has reorganized with an ambitious and highly regarded CEO who has built a strong team.

Each director completed a confidential, anonymous assessment of each of his fellow board members. In addition, each member evaluated himself on the same scale.

The results, exclusive of the individual self-assessments, were compiled, and the combined results for each were shared with that particular board member. In conformance with prior research surveys, male self-assessments were slightly higher than the consensus, and women's were slightly lower.

The summaries of individual feedback were seen exclusively by the evaluated individual and the chair of the governance committee. The summary of total feedback was compiled into a single chart and shared with the full board.

The results showed that attendance was good, and the board unanimously approved of the management team and the new direction of the company. Board structure was excellent.

However, the overall board was described as highly risk averse and slow to change. They prioritized individual risk over that of the company and were not seen as adding value to the strategy of the company.

☐ Several directors did not know what the key metrics for the company are.

☐ One director was considered "high maintenance," and received considerably lower evaluations than the other eight.

☐ Most directors did not have an appropriate understanding of the markets and opportunities for the company.

☐ Education for the board and succession planning were described as sub-par.

At the first board meeting following the director assessment, there was a significant improvement in the comportment of the director who had received the low assessment. Also, a new initiative was adopted to educate the board. Action was taken to rotate members off the board and bring on new directors who could help the new CEO take the company to the next stage of growth.

These conditions can be met with a third party who provides only summary reports back to the company and commits never to reveal individual assessment data. The third party uses safeguards to assure that those who receive feedback are also protected with appropriate privacy.

Some states, such as Florida, Georgia, Michigan and California, have sunshine laws that require employee assessment information to be available to the employee. Even in states where sunshine laws or discovery may be a threat to anonymity, the legal system provides a work-around called an "order of protection."

Under an order of protection, a claimant is forbidden to see the actual ratings. The only reason to see the ratings is to verify that they were used accurately to create the feedback report. The court may allow the claimant's attorney to review the actual ratings under the express promise not to reveal individual data to the claimant.

Some boards also use a work-around that uses external attorneys to interview directors for the evaluation. The information may be protected under attorney/client privilege if the attorney renders advice and does not merely serve as a pass through. However, several problems can weaken the attorney interview approach.

First, attorney interviews are an expensive way to gather information, and the resulting information is often too general to be actionable. The focus is on legal issues and not the scientific methodology and content that generates an effective and independent assessment. Research also shows that people are less candid when talking to another person face-to-face rather than responding privately on the web or paper under the promise of anonymity.

Finally, attorney evaluation focuses primarily on critique and developmental recommendations, and ideas are often missed. By using an independent, outside evaluator, attorneys can optimize their best use by recommending and helping implement portions of the action plan.

☐ *Process design.* Experience across many public and private organizations suggests that the evaluation process should be:

- Fast—taking a minimum amount of time.
- Actionable—provide valuable information that motivates action.
- Simple—easy to use and to understand.
- Targeted—yielding strategic information for each director.

Director 360° feedback applies scientific tools to create credible observations from those with whom each board member interacts. The process creates behavioral feedback and extends the organization's commitment to continuous improvement.

Director feedback from multiple sources provides a systemic assessment and reflection process for directors to support their leadership development. To enhance the process quality and validity of the results, directors should:

- Customize the assessment tool to fit their culture and strategic goals.
- Provide honest feedback for other directors. Feedback may be captured on paper or on-line, but it must be brief, or respondents will not participate.
- Participate in a feedback coaching session, through the board chair, the governance committee chair, the lead director or consultant that discusses their personal results.
- Agree to create an action plan to strengthen their board contributions.

**Male directors in North America tend to self-rate about two points higher than others. Women directors tend to self-rate near the consensus.**

☐ *Director feedback.* On-going feedback helps diagnose career-limiting behaviors, called "derailers," that interfere with director effectiveness. These measures also support leadership development.

A feedback report of ours shows a director whose strengths include "is independent" "sustains confidentiality" and "acts ethically." This director needs to improve in the areas of "managing conflict" and "thinking strategically."

When he saw these results, he took corrective action, learning more about the business model and markets. In the area of conflict resolution, he has become less confrontational and more thoughtful when the directors disagree.

Self-assessment allows each director to compare self-perceptions with others. Male directors in North America tend to self-rate about two points higher than others, while women directors tend to self-rate at or slightly higher than the consensus. In Asian cultures, participants tend to self-assess slightly below the consensus of others.

Narrative comments add value to the feedback because they provide specificity and useful examples. Most of the comments positively motivate participants to strengthen behaviors that make the board more effective. Constructive comments also guide behavioral improvements. Narrative comments help eliminate nuisance behaviors such as answering e-mails during meetings, arriving late, and monopolizing discussions.

Director interviews combined with 360° feedback confirm both the strengths and weaknesses brought to light by the assessment. Interviews also show the distribution of talent among directors. While some directors receive low scores on specific behaviors (such as addressing conflict and thinking strategically), others are strong on those abilities.

**A summary profile can be a team-building tool when shared with directors. There are two choices for underperforming directors—improve or leave.**

☐ *Acting on feedback.* A summary profile, the composite of all the respondents' feedback, serves as a team-building tool when shared with the directors. It provides a roadmap for enhancing board effectiveness, reduces barriers and enhances communication, analysis and decision-making.

The board might pick two factors and ask each person to make a few recommendations on how to improve on them. The ideas may then be combined and distributed to members for board development. Some boards create norms to reinforce positive behaviors.

Thinking strategically causes most boards difficulty because each director's perspective on strategy may be formed from a different knowledge base (finance, operations, marketing, etc.). However, a shared understanding of the company business model and industry relationships helps dramatically in business and strategy discussions.

There are two choices for underperforming directors—improve or leave the board. Ultimately, there is nothing wrong with thanking a director for her service and rotating her off the board. This is not a sign of failure, but simply that the company is moving in new directions, with new experience, background and expertise demanded.

Director assessment serves as a critical action for board effectiveness. Failing assessment, boards often experience dysfunctional behaviors by certain members and have no way to motivate change.

An independent, educational 360° feedback process provides a credible, actionable assessment of each director's behavior. The combination of statistics, and narrative feedback from trusted board colleagues, provides strong motivation to improve in ways helpful to the board and the individual director.

The board's summary profile acts as a guide to drive board training and development. This team-building tool enables the board to remove boardroom obstacles.

Today, virtually every director embraces his role with the highest intentions. The best directors welcome an objective metric to ensure that they will function at optimum levels, truly adding value to the company. All directors want to demonstrate their commitment to best practice. The best directors want to be better. ■