AGENDA
A Financial Times Service

Print | Close Window

Your Q&A

When Is It Time for a Director to Step Down?

January 7, 2013
Your Q&A is your opportunity to get your questions answered by industry leaders.

Q:

When is it time for a director to leave a board?

Independent director

Answered By

Susan Shultz

Susan Shultz is CEO of the **Board Institute** and president of **SSA Executive Search International**.

A:

Too often boards of directors are overloaded with directors who are disruptive, passive, no longer current, or just taking up seats that could be used by more qualified individuals. Unfortunately, a top boardroom challenge is to devise ways to have more frequent director rotations.

On average, a board brings on a new director once every other year, according to **Equilar**. In 2012, S&P 500 boards elected only 291 directors, the smallest number of new appointees since 2001, **Spencer Stuart** data shows. Unfortunately, boardroom culture can too often be like that of a club, in which members consider it disgraceful not to be asked to stand for reelection. Board members must recognize that director seats are not an entitlement in perpetuity.

Why is it so important to rotate board membership? First, director seats are few and far between, and need to be used wisely. Shareholders deserve nothing less. A new director can revitalize the board's effectiveness with new expertise, perspectives and background. This insight can help companies navigate through global expansions, M&A transactions and succession planning issues, among other matters. If boards that think strategically add value, and if directors are recruited to focus on the company's critical future needs, then shouldn't qualified new directors be added to boards more frequently? Likewise, directors who have contributed to the company but whose skills have lost relevance should be rotated off of boards regularly.

Ideally, board member retention will be based on merit. According to Spencer Stuart, however, 73% of boards instead rely on age limits, and 4% on term limits, to ask for a director's resignation. I feel this is an arbitrary means of accomplishing director transitions. For example, **George Shultz** [not a relation] was rotated off the board of **Bechtel** at age 70, yet an observer might reasonably think that the former secretary of state could have continued adding value to board meetings. Directors who are meaningfully contributing to strategy and critical discussions of key governance issues should be retained, regardless of age.

The key to retaining directors based on merit is an objective and actionable evaluation of each director, the committees and the overall board. And the only people who can assess a director effectively are other board members or associates working inside the boardroom.

What are the signs that a director should leave the board? I believe the following signals might indicate a seat rotation is called for:

- The director's allegiance is to management and other board members, rather than shareholders. Directors may have become dependent on retainer fees or hold so much stock that their objectivity is compromised.
- The director is overly risk-sensitive. Do compliance concerns overtake the director's appetite for corporate growth and innovation? If the threat of lawsuits makes directors too uncomfortable to take risks, regardless of insurance protections, they should step down.
- The director has lost interest in the business. The board member may have joined the board because a colleague suggested it or because of a relevant skill set. Such a director may no longer find the business interesting, or may no longer have confidence in management. If directors can't support management, their responsibility is to advocate for leadership changes or resign. Their first responsibility is to ensure the right leadership is in place and has the necessary resources.

Directors who contribute only in their specific area of expertise, and those who are too busy to devote adequate time to board service, may also be good candidates for rotation.

It is understandable when directors rationalize retaining underperforming directors out of loyalty to their colleagues. However, boards can move beyond such practices by more assertively understanding the company's evolving needs, conducting more rigorous director assessments and regularly identifying suitable boardroom candidates. When a continual director rotation process is established, it validates the board's recruitment and retention processes. It also helps attract the best overall directors to the table, for the good of all stakeholders.