



Title	Board evaluation
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A standard, and by now, widely accepted duty of directors is to evaluate the performance of the CEO and top management. This begs the question: How often do boards apply this standard of accountability to their own activities? Should board members be evaluated in the way that executives are? Academic research has found that a distinguishing characteristic of especially effective boards is board self-evaluation. The advantages of board assessment include bringing into the open issues otherwise not discussed, identifying areas for improvement and marrying expectations of the board, the chairman and board members.

Combined Code Requirements

Sir Derek Higgs also recognised the advantages of board evaluation, and such a requirement is now part of the Combined Code applicable to listed companies effective from 1 November 2003. Formal and rigorous evaluations, on an annual basis, should be carried out of boards, board subcommittees, and of individual directors. Annual reports must state how such evaluations are carried out.

Although the Combined Code applies only to listed companies, its provisions represent best corporate governance practice applicable to all organisations whose objective is to be best in class.

Key characteristics of effective boards

The Higgs Report (available at <http://www.ucd.ie/corpgov/links.html>) sets out 11 characteristics of effective boards which are shown in Table 1. These could form the basis against which an evaluation process could be designed.

Table 1: Key characteristics of effective boards

1. Chairman strong complementary relationship with CEO and members of board
2. Culture of openness, constructive dialogue
3. Environment of mutual trust and respect
4. Continuous active engagement between executive and non-executive directors
5. Recognition by management of the value of NEDs encourages greater executive openness and greater non-executive engagement
6. Planned programme of recruitment and retirement of board members
7. Proper balance of skills and experience
8. Boards include both executive and non-executives
9. Strong executive representation – ensures board as a whole is well-informed
10. Non-executive directors to meet regularly on their own
11. Allows concerns (e.g. provision of information, succession planning) to be discussed.

Source: Higgs Report

An essential requirement for board evaluation is clearly defined roles against which the board as a whole, individual directors and company chairmen can be assessed. One of the many advantages of evaluation is that companies will have to articulate and document roles sufficiently clearly to permit evaluation. Individual assessments

are a good way of making performance expectations clear and of actually improving director performance. The existence of board evaluation is likely to motivate directors to be more effective contributors. Evaluation demonstrates to investors and stakeholders that the board is holding individual directors accountable for their performance.

It can be difficult to assess board members against specified criteria, as each director may bring a different set of competencies to a board. In fact, it is generally accepted that better boards are those that are more diversified. It is difficult for a uniform evaluation to capture these diverse contributions.

Methods of evaluation

Methods of evaluation vary widely and include:

- Checklist-type guidelines (see for example the Toronto Stock Exchange guidelines for effective boards (<http://ir.thomsonfn.com/investorrelations/IRfiles/8298/pdf/corpgov04/TSXGuidelines.pdf>),
- Self-assessment
- Peer-assessment, including formal 180-degree (self-assessment and one other) and 360 degree (self-assessment and multiple others) assessment,
- Benchmarking against best practice, interview and psychometric testing. Effectiveness scorecards have been developed which can be customised for companies' own specific needs.
- A combination of methods can be used.

The use of a suitably experienced facilitator can assist the process of evaluation – someone of suitable seniority, and with a good sense of judgement.

Metrics for evaluating boards

The Society of Management Accountants of Canada (2002) sets out 50 metrics for measuring board performance (which they call the board's balanced scorecard). Table 2 summarises the metrics dealing specifically with the functioning of boards:

Communicating the results

Annex J of the Higgs Report provides extensive guidance on board evaluations. The evaluation process should be used constructively as a mechanism to improve board effectiveness, to maximise strengths and to minimise weaknesses. The results of evaluating the board should be shared with the board as a whole, but individual assessments should be confidential between the chairman and the individual director.

Table 2: Metrics for evaluating boards

Board

No. hours spent on preparation
No. days in advance that material is sent out
Attendance at meetings
Board's input (versus management's input) to agenda
No. meetings per annum
Average duration of meetings
Proportion of independent board members
Number of board subcommittees
Board meetings in absence of management

Board composition

Evaluating skills and qualification of directors
Proportion of directors financially literate
Diversity on board
Description of skills requirements before approach and appointment to board

Succession

Job description for CEO
Annual report on succession planning
Interim CEO identified

Skills and knowledge

Board training programme
Induction programme
Evaluation of training and induction programmes

Source: Adapted from Society of Management Accountants of Canada (2002) *Measuring and Improving the Performance of Corporate Boards*, Management Accounting Guideline, CMA Canada

Concluding comment

Like all other aspects of corporate governance, board evaluation can become a box-ticking exercise. For the benefits of such a process to be realised, the engagement in the process has to be real and meaningful. This is what distinguishes first class boards and companies from the second-raters, who pay only lip-service to best practice.

A half-day course on board evaluation is taking place on Wednesday 8 September 2004 at the *Institute of Directors Centre for Corporate Governance at University College Dublin* in the University Industry Centre. For more details see www.corporategovernance.ie or contact Adrienne.M.Corrigan@ucd.ie.

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