



What's going on in our boardrooms?

The impact of
the financial crisis
on the boardroom

*"We all need people around us to
provide support and challenge;
increasingly CEOs are becoming
isolated, causing potentially serious
consequences for our major businesses."*

Introduction

In recent months John Ainley, Partner of The Alexander Partnership, met with a cross section of CEOs, Chairs and NEDs from different business sectors and sizes. The purpose of the discussions was to understand what is troubling these industry leaders and what they make of the changes to the climate of governance and leadership through the financial crisis. Their insights and thoughts are summarised in this paper. The views expressed are those of the Directors interviewed. Their experience amounts to roughly 600 years of accumulated wisdom and not only provides insight into how they are feeling now, but also provides an indication of what the governance of 'UK plc' may face in the future.

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Executive summary

Much has changed in the world of corporate governance over recent years – some of it good. But we must be aware of the genuine concerns and fears being raised by the most senior members of our business community.

These can be summarised in four key points:

- The increased demands of corporate governance when combined with regulator, politician and press fervour are inhibiting governance and the injection of experience into vital roles in UK plc, and making senior positions less attractive to those who are most suitable for them.
- The unitary board system, of which the UK is so rightly proud, is being jeopardised by the need for NEDs and chairs to become almost a second line of executive. We are creating a two tier board system but with two tiers of executives.
- The increased focus on governance makes it harder to develop future CEOs and Executive Directors. NEDs no longer have the time for the arm-around-the-shoulder discussions with the CEO and, indeed, fear being compromised by such closeness. From where will our future leaders find their development and support?
- The stress to which our boards, whether executive or non-executive, are subject will cause good quality people to seek careers elsewhere, thus jeopardising the very entity that regulation and the government want to safeguard.

The increasing pressures at the top

Executive isolation

The new phenomenon of the isolated executive must raise concerns about the health and welfare of our business leaders. We are provided with stark reminders of the stress that can occur in the tragic suicide of Zurich Insurance CFO Pierre Gauthier in August 2013, and the increase in stress cases – most notably Antonio Horta-Osario, the CEO of Lloyds Banking Group and Sir Hector Sants, the recently appointed and then departed executive at Barclays and ex-CEO of the FSA. These events should make us think seriously about the support senior leaders are given. These are tough and demanding roles.

The demonisation of business

Things have undoubtedly changed in recent years. Many leaders complain of an anti-business environment in the United Kingdom that does not exist in the United States, for example, and this antipathy to business and disdain for business people is not only adding considerable stress to the job but also making it increasingly difficult to attract talent. 'Why would anyone want to put themselves and their careers at risk?' one interviewee asked.

Many commented that there are more relaxing environments in which to work, such as the private equity sector, where a simple error of judgment or performance anomaly does not carry the threat of trial by media or even potential legal sanction.

A new morality

In the prevailing mood, many noted that ethical expectations are high, to the extent that even previous 'acceptable commercial practice' such as seeking tax concessions for investing in parts of the UK or elsewhere in the world, is now viewed as sharp practice. At best, this is thought not to satisfy the strictures of the new morality that is expected of multi-national institutions; at worst, corporations are open to criticism for tax evasion.

Driven by contribution

Perhaps strangely, though, senior people remain keen to fulfill these roles. Despite most being independently wealthy, all seek interesting areas in which to work; some look for the opportunity for acclaim, others the opportunity to put something back in the form of the development of executives, the advancement of a business and the maintenance of good governance.

But our business leaders are only human. There is a limit to the sacrifices they may be prepared to make to carry out such duties and responsibilities, especially when those sacrifices can come at great personal cost.

"My only regret is the atmosphere in the UK is anti-business and this is not a good thing, because investment means jobs and that's what we need in this country."

STEFANO PESSINA,
OWNER ALLIANCE, BOOTS



The changing role of the chair

Wrestling with sharks

Once, the chair of a plc was expected to do little more than place a gentle, guiding hand on the tiller, steering the business away from choppy waters and advising the CEO. No longer. Many commented a chair must now be captain, first mate, boatswain and stoker rolled into one and, for good measure, he or she is also expected to be prepared to jump into the water and wrestle with the occasional shark.

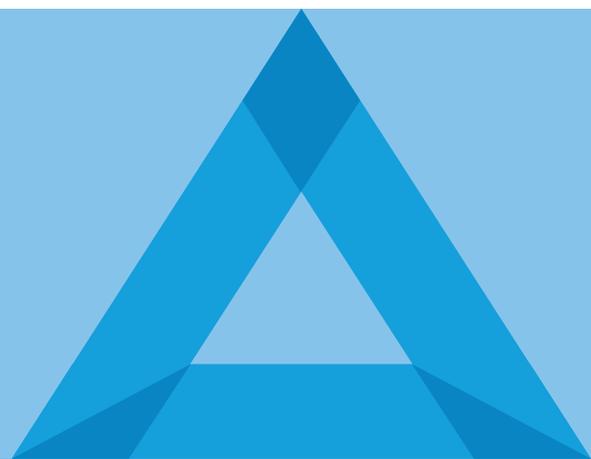
It is not just the levels of responsibility, personal accountability and involvement in the business that have increased substantially for company chairs in the last five years; there is the added threat of reputational risk and loss of office. Indeed, in the last five years more chairs than CEOs have been forced out of their companies.

The chair as pseudo-CEO

Chairs commented that the range of responsibilities now encompassed by the role is enormous – supervising governance; understanding and staying on top of detailed and often complex business issues; dealing with the thorny area of business ethics; managing reputation and brand; as well as the difficult task of maintaining relationships with key shareholders, the regulator, suppliers, politicians, the press, and their own NEDs. Furthermore, the role is increasingly industry-specific and, as a result, is edging closer to the more overtly operational side of business, making the chair almost a pseudo/second CEO. The remuneration of a chair is rightly ahead of the other NEDs but the role does not receive the same level of remuneration as the CEO, despite its similar levels of demand and accountability.

"The Chief Executive gets all the credit when things are going well, but the minute things are going badly the Chairman comes into the spotlight, as has happened with BP."

HELEN PITCHER,
CHAIR, IDDAS



A question of balance

These days a chair has to focus on the requirements of regulation and on delivering results for shareholders while still taking responsibility for overseeing the CEO's performance and development. At the same time, the relationship with the CEO has changed. The chair is expected to be a great deal more challenging towards the CEO than ever before and to be directive and interventionist as appropriate. Many noted that this requires a delicate balance, because these challenges and interventions must be undertaken without at any time appearing to undermine the CEO.

In short, the relationship with the CEO must be one that is neither too close – this is guaranteed to make the NEDs nervous – nor too distant – this undermines how the CEO is viewed by the remainder of the board.

A chair for all seasons

We have asked the question: 'Why would anyone be a chair?', but this also begs the question 'Who should be a chair?'. What type of individual is best suited to this increasingly multi-faceted role? Critically, any suitable candidate must already fully understand or be able to quickly gain a deep knowledge of the business.

While in the majority of cases company chairs are usually external appointees, bringing energy and an often much-needed fresh perspective to the role, some argue that an internal candidate has the distinct advantage of hitting the ground running because they already fully understanding of the business. Plus, to put it bluntly, an internal candidate is likely to 'know where the bodies are buried'.

The prospective candidate should, of course, come with the appropriate executive leadership experience and needs to be tough, prepared to act as the protector of the brand and the company's reputation, but also be prepared to accept accountability and to be much more deeply involved in strategy and operational issues than in the past.

An increasing commitment

Although of course the role varies from business to business, in FTSE 100 companies currently, the chair needs to be focused on the business at least two to three days per week and is expected to have a firm grasp of strategies and initiatives, bringing their wide experience and interest to bear on these.

At one FTSE 30 company, for example, the chair meets with the CEO once a week as well as speaking to him on a daily basis. At smaller midcap companies the role requires only about three days' work a month, although it could be argued that this approach could make the role very remote and render it difficult to cultivate all-important relationships with senior management. There is no one-size-fits-all solution, but among the prerequisites for the role are outstanding emotional intelligence and varied and wide experience.

A chair's role is to get the right team in place and to contribute to strategy, ensuring that concern about overly onerous government regulations does not completely remove the element of appropriate risk from decision-making or drive talented people away from accepting board positions.

Protect and involve

The chair manages the board in that he or she is responsible for board governance and investor interface on the board's behalf. When things go wrong, it is the chair who is expected to step in to protect the executive team, if such protection is justified. He or she is the judge of the executive and the privacy of that relationship is vital. When it fractures and things go wrong, the board will begin to feel exposed and very much at risk. To reduce the chance of this happening, chairs are working harder to ensure that their NEDs are fully engaged in the business and understand what is going on – so they feel involved in both the problem and its solution.

"...The complexity of the banking industry is such that they need someone in the role of Chairman who is fully conversant with all aspects of the company's affairs. The case for an insider appointment has been strengthened by the fact that some of the banks that were hardest hit by the crisis of 2008-9 had a non-banker as Chairman."

BUSINESS RISK:
A PRACTICAL GUIDE FOR BOARD MEMBERS
(IOD)

Information is power

The chair gains insight from several sources. From the senior independent director (SID) he or she learns how the board is feeling, and shareholders and investors will also provide valuable information. However, a number commented that a proper board review with full confessionals to an outsider can be beneficial, further developing the chair's knowledge of their board. The recent requirement to hold regular reviews of the board and its members' performance is welcomed, although the increased supply of 'tick box' approaches to evaluation runs the risk of missing much of the nuance in the relationships and performance of individual board members.

Regarding the CEO specifically, it is the chair's job to discuss the CEO's performance with him or her and to plan for their development. Meanwhile, NEDs have a duty to ask questions about performance, as they arise. However, this vital developmental task is being made more and more difficult.

Chair as CEO coach

Many chairs commented that to fully take on the role of coach requires a great deal of engagement and involvement, and some of the chair's other responsibilities may suffer as a result. Nonetheless, the chair can be a tremendous mentor, given his or her width of experience and knowledge. And the real benefit of a coach comes from their independence from the company and its politics.

"A dysfunctional relationship between the Chairman and the CEO, communication failures between the two or between the Chairman and the board, or the actions of an overreaching Chairman can all undermine effective governance."

BUSINESS WEEK

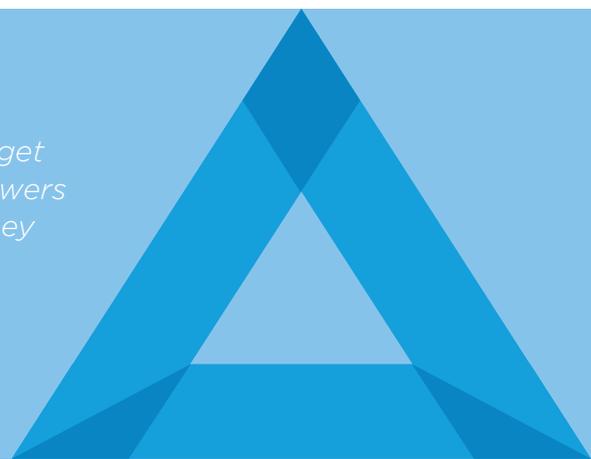
Reputational damage

There is also a prevailing pessimism amongst directors, however, and some are wondering why anyone in future would want to take on the role of chair or NED, particularly in financial services or the energy sector. They reason that all businesses have cycles and it is merely a question of waiting your turn for a major problem or unanticipated underperformance to hit your business. In the event of such catastrophes, executives and their families can be exposed to press victimisation, the stress of which can affect a board member's health as well as their career.

Director of the Serious Fraud Office, David Green and more recently Vince Cable have talked openly about criminal charges being brought against NEDs and chairs in instances where things have gone badly wrong. It is clear that if criminal charges are introduced it is increasingly unlikely that people will want to put their heads above the parapet. Instead, they will take positions with private equity firms, enjoy the garden or work in the not-for-profit sector where they would not be subjected to such potentially damaging scrutiny.

"If we're to get our economy back on track, we need to get the banking system back on track first. Creating new powers to jail bankers who are reckless with other people's money and getting more competition into banking, is a start."

VINCE CABLE



Paradoxes for CEOs

The managerial merry-go-round

Just as for the company chair, the pressures on CEOs have increased immeasurably during the last few years, especially the pressure to deliver results in the short term. CEOs increasingly feel that unless they deliver positive results quickly, they will be out of a job. Many interviewed feel that the turnover of chairs and CEOs in public companies is too high and their tenures are too short.

In such an environment, executives are taking great risks with their careers. It is little wonder then that, like football managers, CEOs strive to put in place pre-agreed leaving settlements to compensate them for such risks. Nonetheless, in the current environment, they are subject to unprecedented criticism for seeking such arrangements.

“Short-termism curtails ambition, inhibits long-term thinking and provides a disincentive to invest in research, new capabilities, products, training, recruitment and skills.”

SIR GEORGE COX,
OVERCOMING SHORT-TERMISM WITHIN
BRITISH BUSINESS

The short-term approach is exacerbated by the fact that businesses are increasingly being run from quarter to quarter, rather than for the longer term. Interestingly, several major businesses which do not need to adhere to the short-term approach – John Lewis, for example – are enjoying success as a result of playing a longer game. There is something of a contradiction here, since financial reward for the executive is increasingly focused on long-term results. Some are even calling for a ten-year deferral of bonus payments, despite the fact that business results are reported and discussed quarterly with analysts who are looking for a regular short-term performance.

The blame game

In the face of enormous pressure from numerous stakeholders – regulators, shareholders, customers, press and staff – CEOs are generally feeling less secure in their jobs than they were five years ago. This has been especially the case during the financial crisis. Although many comment that regulators are as responsible as CEOs and chairs for the events of the last few years, they believe that regulators have become adept at placing the blame squarely on the shoulders of the other two. This has understandably made some CEOs extremely defensive.

Working together

In the past, the roles were clearly defined and delineated. The chair was responsible for the board and the CEO for the business. Now this has changed, and the chair must be deeply involved in all aspects of the business, while a financial services CEO, for example, is typically embroiled in governance for around two-and-a-half days a week, mainly because of the impact of regulation and risk.

CEOs comment that their positions are often lonely and remote and they need a partner, not a disengaged governor for a chair. The relationship was once analogous to that of 'coach' and 'athlete', where the chair was the coach. But now the chair has to be seen to be independent and separate from the CEO, although he or she must still be available to act as a sounding board. If the CEO and the chair seem to have too close a relationship, NEDs are liable to worry about the independence of the chair and consequently the governance of the firm.

An abrasive or frustrated group of NEDs can quickly become overly confrontational or challenging to the CEO, risking the CEO becoming disenchanted and perhaps leaving the job - adding considerably to the NEDs' workload in the short term. Another undesirable result of a 'difficult' board is that the CEO might use the board's recalcitrance as an excuse for inactivity, or seek to take risks that have not been fully discussed. 'I could never get this past the board', he or she might say. In fact, if a CEO feels that the board is not supportive, or that he/she is being distanced from it, it is his/her duty to force a frank and honest discussion with the chair.

"The relationship [between Chair and CEO] only works if the two people are clear about what they are responsible for, recognise the value of each other's contribution, and have mutual respect. Ideally they should be complementary both in temperament as well as in background and experience."

BUSINESS RISK:

**A PRACTICAL GUIDE FOR BOARD MEMBERS
(IOD)**

Accessibility

Additional pressure and workload for the CEO arises from the use of social media by customers who, with the democratisation of communications, seek and expect instant access to CEOs and senior management to resolve problems. Failure to respond immediately can result in a complaint being posted on a public website, doing long-term damage to a brand. What's more, these comments can remain in place for a long time, whether the problem has been dealt with or not. This type of pressure is forcing executive teams to communicate more effectively and rapidly than they had been accustomed to previously. In many cases executives are on call 24/7.

People skills

With the insecurity felt by many workforces – driven by corporate restructures and the economic environment – the CEO's ability to inspire, engage and motivate in the face of uncertainty and ambiguity is increasingly important. Coupled with this, the role of CEO is becoming even more outwards-facing, with the importance of communications with the press, regulators, consumers and other key stakeholders. However, many CEOs with technical and financial backgrounds can lack these core communications skills. In some instances the chair can support the CEO and even play this role to some extent. But CEOs increasingly need to be great 'people leaders' while also being great stewards of their enterprises.

"The real team in fast moving companies, even when things are going wrong, share things with each other completely."

SIR ARCHIE NORMAN,
CHAIR, ITV



Changing dynamics in the boardroom

NEDs – an increasingly demanding role

In the past, NEDs were seen as something of a 'necessary evil', a group to be 'managed', but this has changed. The Walker Review of Corporate Governance of the UK Banking Industry provides wise counsel on the subject of non-executive directors, recognising the demands on the role in terms of time and commitment, as well as the depth of knowledge required about a business.

Walker recommends NEDs should work at least thirty days a year. Given that, on an hourly basis, NED pay is very low for the responsibility involved, they should receive greater remuneration.

The Saltz Review of Barclays' Business Practices suggests an increased amount of time should be devoted to the NED role – between fifty and one hundred days a year – but adds that it would be difficult to find people who would be prepared to give so much time to it.

“Increasing levels of boardroom regulation and risk have placed greater demands on the non-executive director (NED) community. The days of turning up for a quick hour and a good lunch are long gone...”

SIR BRYAN NICHOLSON,
FORMER CHAIRMAN OF
THE FINANCIAL REPORTING COUNCIL

Risks

NEDs are, naturally, very concerned about their reputations, which are increasingly being threatened by the wise-after-the-event attitude of some politicians and the press towards plc boards. As a result, it has become more difficult to recruit NEDs for financial services plc boards.

The change is also affecting the way NEDs perform in their role. Faced with juggling the paradoxical elements of regulation, judgment and experience, many NEDs feel it safer to stick to the rules as closely as possible. This, of course, removes a great deal of creative thinking from their actions and decision-making. Moreover, the impending threat of legal action and even criminal charges for mistakes inevitably discourages talented people from coming forward. This has persuaded some NEDs – aware that every company will go through a sticky patch and fearful of the damage to their reputations as a consequence – to turn increasingly to positions on the boards of private companies and 'safer' unregulated sectors.

The levels of responsibility and personal accountability, particularly in the finance sector, have increased substantially. Finance NEDs are at risk of exposure to negative press comment and unreasonable criticism from politicians. The reputational risk involved and the personal liability of a non-executive director is exactly the same as that of an executive director. This, however, has given some NEDs an unbalanced view of their duties and leads to their spending time challenging instead of providing support for the CEO, which is an important part of their role.

End of the old boys' club

NEDs increasingly require a specific skills set. They need a substantially greater knowledge of their business than ever before. It used to be enough for a NED to possess good general experience; now he or she needs deep and specific sector knowledge. This knowledge is partly technical – although that type of knowledge can be brought in – but it mainly consists of knowing the business well enough to understand when to challenge and when to be supportive.

Most NEDs used to rely only upon what they were told by the executive. Now they need to know enough about the business to be able to pose challenges. They need to commit time and energy to meeting and listening to the workforce in order to find out what is really going on in an organisation. In short, in these post-financial crisis times they have to take the role very seriously.

Consequently, NED appointments are now much more considered than in the past and there are regular formal checks on performance via annual internal reviews as well as external reviews every three years. These changes have served to destroy, once and for all, the 'old boys' club' ethos of the past and have helped to raise boards of financial institutions to a more professional level. There are now thorough induction processes for NEDs and they no longer have the luxury of learning on the job.

Being a board member for the first time can have its difficulties and new NEDs often struggle during their early days to make the most helpful contributions. It takes time to learn the skill of effective challenge and support to the executive team. Typically, a new NED errs too much on the side of forensic and overly detailed challenge rather than using his/her experience to guide, support and challenge.

There is an enormous desire amongst NEDs to ensure that they are doing the 'right thing' – currently be defined as providing shareholder value and displaying ethical behaviour. In fact, the amount of regulation now in force has shifted the NED role towards being one of governance, of policing the business.

Diversity is vital for a board, particularly diversity of experience. However, a few interviewees commented that the recent rush to make boards gender-diverse has resulted in the appointment of some women who are not yet 'board ready'. This can be detrimental to the reputation of the vast majority of capable and suitably experienced women who are already holding board positions. It also runs the risk of denuding the talent bank of experienced women while ignoring some talented males.

The focus should, instead, be on providing appropriate executive development for women so that they can become NEDs with the right experience and skill set over time.

The SID – Mr or Ms in-between

The senior independent director's role is a tricky one. Like the chair, he or she has to be challenging but also have the ability and the standing to act as a sounding board for other directors. As with other roles, that of the SID now brings more responsibility, personal accountability and reputational risk than ever before, adding more stress and undoubted complexity to the role. The key job of the SID is to keep the chair informed about the prevailing mood of the board, but these days SIDs have more power and influence and some act as an independent liaison point with shareholders.

“The overall time commitment of NEDs as a group on a FTSE 100-listed bank or life assurance company board should be greater than has been normal in the past.”

THE WALKER REPORT:
A REVIEW OF CORPORATE GOVERNANCE
IN UK BANKS AND OTHER FINANCIAL
INDUSTRY ENTITIES

SID as lightning rod

The CEO who considers him or herself to be infallible can be one of the key causes of board disunity, leading NEDs to hold different views about how to deal with the problem. Often a period of sustained success leads to over-confidence, which can then lead to reluctance on the part of the CEO to listen to others and sometimes on to dramatic subsequent failure. Another threat lies within the relationship of the chair and the CEO. There is a danger that they might get too close; it is essential that this relationship preserves a delicate balance of mutual respect and support, but there must also be challenges and honest criticism within it.

“The principal role of the Senior Independent Director (SID) is to support the Chairman in his role; to act as an intermediary for other Non-Executive Directors when necessary; to lead the Non-Executive Directors in the oversight of the Chairman and to ensure there is a clear division of responsibility between the Chairman and Chief Executive.”

HSBC.COM

It is always vital to remember that the chemistry between the chair and CEO has to be right – the chair must make every effort not to be either a relentless critic or an adoring fan; there must be trust and mutual respect and they must share the understanding that they are working for the good of the firm and not for personal aggrandizement.

Many of our interviewees noted that it is in managing such areas that the SID really earns his or her spurs. For general board wellbeing, it is advised that a review be held in which each director discusses the other members of the board and its actions in a full ‘confessional’ with an outsider and the SID has to do the same for the chair.

In conclusion, the SID should act as a lightning rod for the board, but should also ensure its independence of action and decision-making. For most of the time, the SID will have little to do beyond his/her NED duties, but the role can very quickly and very suddenly become extremely significant in maintaining the integrity and efficacy of the board.

Other stakeholders

Politicians have, in recent years, become severely and many say unfairly critical of the boards of large businesses, passing blame that they invariably should share onto regulators and the management of companies. Many also see the UK press being typically and, at times, unhelpfully aggressive towards individuals and businesses they chose to pillory. This could be said to be a positive aspect of our democracy and an example of the way in which we insist on a free press, but it is wearing and can be devastating for both individual and company reputations.

“Before 2007, the only time there was a speech about regulation from the prime minister was when there was an attack on the FSA for over-bureaucratic regulation. That was the climate in which the regulators operated. It was extraordinarily difficult. They knew that if they were tough on a bank, the Chief Executive would go straight to No 10 or No 11 and say: “This was an attack on the UK’s most successful industry”.”

SIR MERVYN KING,
FORMER GOVERNOR OF
THE BANK OF ENGLAND

The background features a light blue gradient on the left side, transitioning into a series of overlapping geometric shapes in various shades of blue and teal on the right side. These shapes include a large dark teal triangle pointing downwards, a medium blue triangle pointing upwards, and a light blue triangle pointing to the right, creating a dynamic, modern aesthetic.

“Alexander is committed to helping leaders, their teams and their organisations, to grow, change and renew themselves in order to fully realise their potential within the new and emerging environment.”



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