



Corporate governance of private equity-backed companies

‘So, while it is obvious that good decision-making, facilitated by a well-designed process that is staffed by well-informed and competent people, is an essential component of any successful organisation, corporate governance processes in a private equity-backed company are defined and judged largely according to their fitness for that particular purpose. Listed companies and their investors might take note of this aspect of the private equity model ...’

Simon Witney

Evaluating board performance

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Alison Gill

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Evaluating board performance

Alison Gill uses her experience as a board evaluator to draw out what makes a good external board evaluation and the benefits it can bring.

'Boards must grasp the most difficult issues but often they don't ... instead they are prone to delay finding or executing on an answer. An effective board evaluation must highlight where this is happening and bring clarity to how it might be resolved.'

These wise words were gifted to me when we first set up our board Review business in 2010. As part of the development of Bvalco we interviewed 50 chairmen from major PLC's, charities and not for profit organisations to identify what chairmen needed from a board evaluation.

Sir Christopher Hogg, former chairman of Courtauld's, GlaxosmithKline, the Bank of England and the National Theatre was one of those chairmen. As a psychologist and now board reviewer, his words struck a chord and have guided what we aim to do when we conduct board Reviews.

My first experience of a board Review was in fact with a large sports organisation which was in crisis. In essence the board had missed deep rooted cultural matters that brought the organisation into disrepute. Serious cheating on the sports field led to the dismissal of coaches, medical staff and players. It was a very public crisis reported widely in the press. The board was in disarray and sought external help to rebuild itself and restore trust and confidence in the organisation.

The board Review involved interviewing all board members and those who reported regularly in to the board, observing the board in action and then finding a way to feedback the issues in such a way that they could be heard, accepted and acted upon. In many ways it was a difficult Review; anxiety was high, trust was low and accusations were flying. However, there was a clear and accepted need for change.

That board was probably ahead of its time in seeking an external evaluation as a means to help it to get back on track. Like many sports organisations at the time the board lacked proper structured governance and the Review uncovered that the board were handcuffed by a lack of respect and authority. Like many sporting organisations of that era the Head Coach and the best players held the informal power in the organisation and the board lacked teeth.

Board Reviews can be a useful way to help a failing board get back on track but perhaps more importantly, they are a means to help boards continuously improve how they work and hopefully to help prevent crises of this kind.

Over the seven years that I have been working as a board evaluator I would say the most frequent issues that come up in a board Review are:

- a. The performance of the CEO
- b. Board succession, most typically the succession of the chairman
- c. The relationship between the board and the executive staff
- d. The strategy of the organisation – in particular the board's involvement
- e. Problems with power and authority that disable the board or make the board more prone to issues with group dynamics such as groupthink/confirmation bias and other typical dysfunctions of a group
- f. And, of late, the board's role in developing and overseeing the culture of the organisation and setting the tone from the top.

These matters are not confined to boards that would necessarily see or describe themselves as dysfunctional or ineffective but rather are matters that are typically difficult for boards to do well.

Take for example, the performance of the CEO – one of the board's most critical tasks. It is arguably *the* most critical task - a board has to hire the right CEO and, if the CEO is under performing, to fire and replace her or him. However, whether the CEO is performing effectively is a topic on which different directors on the board may hold a different opinion. A board Review is as good a time as any for directors to voice concerns and for the board to openly debate and collectively decide whether the board has full confidence in the CEO, whether he or she needs different objectives or whether indeed confidence has been lost and it is time for a replacement to be found. A board with a degree of ambiguity about the effectiveness of the CEO will almost certainly be hampered in its effectiveness.

People matters such as the performance of the CEO and the succession of the chairman must be handled sensitively, openly and constructively. Board directors may use the board Review to raise a concern about one or other of these things and it is the board reviewer's job to find a way to ensure that the issue is surfaced, openly debated and a

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decision reached and acted upon. The issue may or may not be whether the CEO or chairman are under performing but rather that board members feel it needs a considered and collective discussion and decision.

What is the best way to conduct a board Review?

A board Review typically takes between three six months of elapsed time and involves interviewing all board directors and key stakeholders as well as observing the board and board committees and then feeding back to the board as a whole.

Taking this amount of time is to a certain extent a function of the logistics of how often a board meets and of fitting in scoping meetings and interviews with all the directors prior to observing the board. Interviewing before observing the board is key to ensure that the board has met the reviewer prior to the observation. Knowledge and trust of the reviewer helps to alleviate concerns of trust and confidentiality with regards to observing the board.

Board members who are unfamiliar with observation can harbour concerns that the observers might affect the normal dynamics of the board. In my experience the business of the board is too important for the dynamics to be inhibited for long and typically when asked afterwards, board directors will say that they 'forgot' that the observer was present. When observing we use a framework on behaviour to collect objective evidence about how effectively the board is working together as a team and we use themes from the interview analysis to act as triangulation on particular points. As a board reviewer you are acting on behalf of the board and experiencing a board meeting as a director experiences it is an important piece of research. There is nothing like receiving the board papers and preparing for a board meeting as if you were a director to tell you how good board papers are for example. Observation will also highlight matters such as the quality of debate; whether the board organises and prioritises its time on the most important matters and how effectively the board is chaired.

Prior to observing the board and committees we conduct interviews with all board members and key stakeholders such as those who regularly report in to the board. The process of how to conduct these interviews is important. *There are four important rules to an effective evaluation interview:*

1. *The interviewee should receive a copy of the interview questions prior to the interview so that they have time to think.* These questions will have been agreed in advance with the chairman, CEO and maybe the Senior Independent Director (SID).

2. *The interview should start and finish at a particular time (typically one hour is sufficient).* Time is psychologically very important – particularly when discussing the most sensitive issues. That's why counselling sessions always last for a specific amount of time so that the 'patient' knows that their anxiety will be bounded by time; no matter how difficult it is to talk, time will bring the session and anxiety to a close. Whilst I am not suggesting for a minute that most board directors need psychotherapy, they do often want to discuss or disclose things that are highly confidential or matters about which there is some ambiguity or anxiety. I typically find that it is the last 15 minutes of an interview where the most interesting discussions happen.

3. *The interview should be semi-structured, with open questions* and the final question is: 'Is there anything else which you think it is important or useful for me to know that will help the board to improve its effectiveness?' The best interviews feel thorough although conversational in nature and cover a lot of ground in a short time. The board reviewer needs to be skilled at building rapport and at encouraging trust, confidence and openness and must handle sensitive matters in a frank and straightforward way. A board Review interview will deliver a degree of insight as interviewees can openly debate or make sense of an idea or issue in a way that they may not previously have had the time or inclination to do.

4. *And finally, the interview must be confidential.* Interviewees need reassurance that what they disclose will be non-attributable. Directors often use board evaluation interviews to discuss with an objective person matters that have been troubling them or matters that for whatever reason have gone unnoticed or not grasped. Sometimes the discussion in its own right is enough to resolve the issue in their mind or to bring it up the priority list. By interviewing all the directors and other key stakeholders the board reviewer will be able to identify issues that are common concerns amongst all or most of the directors that need action but also to identify matters or observations that are of particular importance to maybe a smaller number or even just one director.

Feedback to the board is not always in the format of a report. The end of the board Review is not the feedback but rather agreement with the board on what matters they will act upon and how they will monitor progress against the actions. *It is not the role of the reviewer* to tell the board what to act upon, rather to facilitate the board's decision-making.

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In the years between a formal external evaluation, the board may find it helpful to use a structured questionnaire as a means to collating feedback from board members. The SID along with one other director, or the board secretary may be the best person to objectively collate the findings and produce a thematic report to the board. In my opinion questionnaires can be a useful aid to a board evaluation, they can be used to improve the efficiency and cost of the process, however, the results are typically relative not absolute and are not a replacement for a thorough, qualitative review. Most directors find the individual interviews to be helpful in their own right and value the collective discussion following the feedback. It can be a lonely task being a board director so this time set aside to review and reflect, if used wisely, can be a useful critical eye.

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What is the key to a successful review?

Over the years that I have been conducting board evaluations I have found there are a number of things that help a successful review. The board is a vehicle of influence, board directors influence change; it is the executive that must execute and so the relationship between the board and executives must be an effective and productive one. The CEO has a lot to gain from an effectively functioning board and a lot to lose from a dysfunctional board. CEOs have a tendency to think the board Review is not something that really concerns them, this is a mistake, so whilst the chairman runs the board and the board Review, the CEO must be actively engaged.

Secondly, a board reviewer often has to raise matters that are unpalatable or that for some reason the board has been unable to deal with themselves. This is not a job for the faint-hearted. A board evaluation must shed light on the most difficult issues. A board reviewer does not have to be right in their observations. I describe my findings as a series of hypotheses and conclusions with varying degrees of evidence in support; sometimes what is said as part of a board Review is based on insight and intuition, group dynamics in particular are felt as much as they are seen. Surfacing issues inevitably can create anxiety and defensiveness. How the reviewer (and the chairman) manage the reaction will be critical to success. For example, at a recent review, the board was clearly struggling with

their role in the culture of the organisation; the CEO was adamant that culture was her remit, the chairman and a number of directors clear it was the domain of the whole board. The matter was, on the surface, being dealt with yet dissatisfaction seemed pervasive. Surfacing the dissatisfaction enabled a debate to be had.

What is the use of an external board Review?

I asked this question of Brian Quinn, a highly experienced non-executive director including having been former chairman of Celtic Football Club and Deputy Governor of the Bank of England and here is his response

‘First, they tell you what you already know. It can be truly helpful to have your opinions of the working of the board, good or bad, confirmed by an outside independent observer.

‘Secondly, they tell you what you don’t know. Either because of the pressure of work, or because the opportunity goes unnoticed or is not grasped, boards can overlook important issues affecting their work. An outside observer can produce insights that otherwise are invisible.

‘Thirdly, an external observer looks at the operation of the board as a whole. This goes beyond the contribution of individual Directors and encompasses how the board functions as a unit.

‘Fourthly, and more specifically, the external observer can focus on the relationship between the Executive and the Non-Executive Directors. This is a key issue for most boards.

‘Lastly, the external observer puts it all together: process, performance and people.’

At worst if the Review tells you what you already know, at least you can have the peace of mind you are on track. And at best it will help your board tackle the difficult issues that for some reason the board could not find space to hear or the ability to resolve.

Alison Gill is a psychologist by background. Alison works with boards of directors to strengthen relationships, enhance decision-making and improve board effectiveness through Bvalco www.bvalco.com. Additionally, Alison acts as an advisor on matters of culture and behaviour and is co-lead tutor and co-author of the Financial Times Non-Executive Director Diploma, a qualification designed to train people to be effective board members. At the end of last year Alison spoke at an ICOSA: The Governance Institute’s conference on evaluating board performance in sporting organisations. This article is an extract from her remarks.