

Power shifts in the boardroom



by Kevin Kelly

In the wake of the corporate scandals at the turn of the new millennium – Worldcom, Enron and so on – the corporate spotlight shifted to corporate governance. The boardroom agenda became the board itself: how it functioned; the standards it adhered to; its entire *raison d'être*.

This welcome and necessary debate continues and has already changed the shape of boardroom life. The sense of entitlement and privilege which was often evident in some boardrooms is fast disappearing. As boardroom behaviour is scrutinized with ever more rigour, there is no room for indulgent appointments. Cronyism may be alive and well in politics, but it is fast disappearing from corporations. The growing involvement of outside agencies in rating board decisions and monitoring boardroom performance ensures that stricter codes of behaviour and involvement are now applied. So far, so good.

But, changing boardroom expectations bring one critical implication. As the pressure on boards intensifies, one person feels the squeeze more than anyone else: the CEO. Boards are intent on passing the pressure down the chain.

In corporations power has shifted. While the CEO once held power, increasingly it is now boards that call the shots by closely monitoring the CEO's performance and determining his or her successor. The nightmare scenario for a board member is to be in the position of a number of the Enron board: powerless, ignorant and innocent in the shadow of a rogue CEO.

It is worth noting that when Jeffrey Sonnenfeld, a corporate governance expert based at the Yale School for Management, examined the boards at Enron, WorldCom, and Tyco he found no broad patterns of incompetence or corruption. In fact, the boards of these companies often exhibited best governance practices in terms of structural and procedural issues – for example: the make up of committees; attending meetings; board size and composition; and financial literacy. They also scored highly on accountability mechanisms such as codes of ethics and conflict of interest policies. In effect, they were “good” boards, but they had limited knowledge of what was actually going on in the companies they purportedly led.

Waldemar Schmidt, chairman of Superfos and Thrane & Thrane, a board member of other companies, and formerly group chief executive of ISS, is one of Europe’s most experienced board members. “There has been quite a change in the way boards spend their time,” he reflects. “In the past I would say that most boards spent 80-90 per cent of their time discussing day-to-day business and very little time on the future of the company. That is changing. I’m not saying it’s 80 per cent strategy and 20 per cent control, but there is clearly a shift in how much time effective boards spend on looking ahead.”

The most reported-on manifestation of this shift in power is CEO turnover. The annual study of CEO succession undertaken by the consulting firm Booz Allen Hamilton concluded in 2005 that “boards of directors have become more responsive to shareholder and regulatory pressure, and are more proactive in ousting under-performing CEOs”. More than one in seven companies, according to the survey, replaced their CEO in 2005. This means that boards spend more time dealing with succession issues. Indeed, the growing trend is for boards to spend more time on issues which would traditionally have been the domain of CEOs. “Boards will become more deeply involved in creating value by helping management better identify threats and opportunities, by supporting management’s efforts to effect major change, and by enhancing the quality of the management team,” concludes the Booz Allen research.

The list of CEOs who have recently departed after disagreements with their boards is long and lengthening. They come from all industries and all types of organization. The great and the good can also be humbled by their boards. Back in 2000, Lloyd Ward resigned from Maytag in a disagreement with the board over the strategic outlook and direction of the company. Maytag went on to turnover two more CEOs over the next two years. Others on the boardroom-differences hall of misfortune include Iomega’s Bruce Albertson; Buy.com’s Gregory Hawkins; Equitel’s Mary Walker (who resigned in July

2002 after joining the firm in May); Spectranetics' Joseph Largey; Swiss Life's Manfred Zobl; Motorola's Christopher Galvin; Office Depot's Bruce Nelson; and Swiss Sarnafil's Peter Schildknecht.

Think back to Carly Fiorina's departure from the CEO's job at HP in February 2005 after differences with the company's board on how to execute HP's strategy. Or, consider Marsha Evans' resignation from the American Red Cross due to friction with the board of governors -- Evans' predecessor, Dr. Bernadine Healy, was also forced to resign partly because of disagreements with the board. The cast of corporate Caesars appears to be increasingly outnumbered by the growing population of boardroom Brutuses. "Business has entered the era of the short-term chief executive," notes Charles Lucier, senior vice president emeritus of Booz Allen Hamilton. "The age of the ephemeral CEO is here."

Faced with this shift in power, what can CEOs do?

Relax, it's only complexity

First, they have to accept that they are, for better or worse, stuck in the middle. Shareholders, the board and employees all exert pressure on them – and there is also the increasingly demanding media to consider. They have to accept that this level of complexity comes with the job. There is no simple solution; no CEO-as-dictator option which can be speedily programmed into the organization's *modus operandi*.

Indeed, complexity is likely to increase. With private equity firms piling more dollars into markets (\$180 billion invested worldwide in 2004, up 50 per cent on the previous year) and the rise (almost overnight) of consortium deals with multiple firms buying bigger corporations, the boardroom dynamics are vastly different. CEOs need the ability and appetite to serve multiple owners. Leading a company backed by private equity is often far more complex than serving a public company. The sponsors, inevitably, behave like owners and achieving consensus requires patience and ego management. This phenomenon, and the pressures it brings for CEOs, is likely to extend to Europe and Asia in the quest for bigger deals.

Only connect

Second, CEOs need to communicate more than ever before. The channel of communication between the CEO and the boardroom needs to be constantly

open. In too many cases CEOs seek to communicate with their boards when problems are mounting. On the other side boards are often tempted to spring issues on unsuspecting CEOs at board meetings. Gamesmanship helps neither side win the game.

Clear and regular communications can turn around problems. One Fortune 100 company's fortunes had declined over ten years. By the time its board looked for help it was effectively a turnaround. A new board with broader advisory skills took over but, within three years, it became apparent that the new CEO, while effective at improving operations was not able to reposition the company's strategy. Eventually, another CEO was brought in. He created a weekly communication plan with the board to keep them abreast of the major strategic shifts and allowed an open forum in board meetings so that board members could witness first hand the executive team in action. In this case, open and consistent communication helped the nimbleness of the company's decision making.

Manage expectations and define the boundaries

“You have a group of former CEOs who think they know everything. The trick is to manage their expectations,” one CEO told me. Board members like to know what's going to happen next. In fact, “no surprises” is the cardinal rule for managing boards. Board members don't want to see events unfold in the media; they require it first-hand.

Related to managing expectations is having clearly defined boundaries where responsibilities begin and end. Overlap is dangerous.

Target and manage the chair

The relationship between the CEO and the chairman is key. “An ideal situation is one where you have a chairman who has skills that are different from the CEO and you don't usually get that when the CEO becomes the chairman,” says Waldemar Schmidt. “I also think that these complementary skills are important because the role of a CEO can sometimes be very lonely and there will be certain times when you, as CEO, need to talk to someone who is independent from the day to day business. In that situation the chairman has a very important role to play.”

With boards becoming more independent and the chairman's role being split from the CEO, the CEO-chairman-board of directors relationship will be increasingly crucial to how a company performs.

Historically, the CEO and chairman roles were often combined in American corporations. Separation is now commonplace thanks to corporate governance guidelines requiring greater distance between the board and the CEO to encourage objectivity. A study by the governance ratings firm Governance Metrics International (GMI) found that 95 per cent of the FTSE 350 firms rated by GMI split the roles of CEO and chairman. In France, where the combined CEO and chairman has traditionally been a powerful force, there is now movement in this direction -- with companies such as Renault and Carrefour splitting the roles. In Germany, the roles of the chairman as head of the supervisory board and the CEO as head of the management board are legally separated.

The trend looks set to continue. Tom Siebel has relinquished the CEO title at Siebel Systems to former IBM executive J. Michael Lawrie. Disney shareholders stripped Michael Eisner of his chairman's title and gave the job to George Mitchell, a former U.S. senator. Michael Dell has said he will soon turn over the CEO position at Dell Computer to chief operating officer Kevin Rollins. And, at Oracle, CFO Jeff Henley is chairman with Larry Ellison remaining CEO.

It is also notable that some high profile CEOs have become chairmen of major corporations. This suggests that they see the roles as powerful rather than ambassadorial – examples include former Nokia CEO, Jorma Ollia, becoming chairman of Shell; and AstraZeneca recruiting Louis Schweitzer, the ex-Renault boss, as its chairman.

When it comes to healthy CEO-chairman relationships, best practice is thin on the ground. Successful instances usually involve founders moving from the CEO's job to become chairman. Successful examples include Microsoft chairman and CEO Bill Gates handing over the CEO reins to longtime colleague Steve Ballmer in 2000; eBay company founder Pierre Omidyar becoming non-executive chairman with Meg Whitman as CEO; and Intel's Andy Grove becoming chairman with Craig Barrett as CEO.

There are other instances of a CEO and chairman working together to turn around an ailing company; or the chair acting as a supporter to help a new CEO make the transition into the role.

In reality, the most effective boards are high performance teams. As with all effective teams, members have clearly defined roles, play to their strengths and complement each other.

Looking at boards in this way offers a different and potentially important perspective. Jeffrey Sonnenfeld has observed: "We need to consider not only how we structure the work of a board but also how we manage the social system a board actually is. We'll be fighting the wrong war if we simply tighten procedural rules for boards and ignore their more pressing need -- to be strong, high-functioning work groups whose members trust and challenge one another and engage directly with senior managers on critical issues facing corporations."

A similar perspective comes from boardroom expert, Edward Lawler: "A board is a group, perhaps in some cases, a team. Boards need to be assessed by the same conditions and behaviors that lead groups to be effective."

The future agenda

Boards are slowly starting to pay attention to the role that they were established for – as a sounding board for management. They are spending considerable time and energy thinking about the business, bringing their expertise to bear on issues of growth, and seeking to provide their companies with competitive advantage.

The future boardroom agenda is as complex as it is demanding. The hope must be that boards and CEOs establish their roles more clearly. Uncertainty demands clarity.