EVERYTHING ABOVE BOARD

WHY A BOARD OF DIRECTORS NEEDS TO ACT IN THE COMPANY'S BEST INTERESTS, NOT ITS OWN.

By Adonis Adoni | Photo by Michael Kyprianou

In 2018, Carillion plc, one of the largest construction companies in the UK, announced that it was entering into compulsory liquidation. It was just one of the spectacular collapses in recent years of companies which, on paper at least, should never have reached that situation. At the heart of these failures were questionable practices and decisions at Board level, says Helen Pitcher OBE, the keynote speaker at an event organised last month by the KPMG Cyprus Audit Committee Institute (ACI), in collaboration with INSEAD Independent Directors Network on the subject of Directors' Remuneration and Performance. Here, she speaks to GOLD about the need to ensure that company directors are well chosen.

We should not be surprised that money often takes centre stage when it comes to bad governance, says Helen Pitcher, noting that the attitudes of company directors haven't changed over the years and they all want to maximize their earnings. But while the extra zeros on their bank statements also mean increased responsibilities and liabilities, becoming dependent on their own compensation can handicap their decision-making abilities. Various reports have indicated that high compensation packages for Board members, whether executive or non-executive directors (NEDs), can lead to the unwelcome practice of mutual back-scratching and the rise of cronyism.

"In the UK, investors have started to veto high salaries for directors but that has caused a number of CEOs to leave their positions," she says.

Pitcher, who is the Chairwoman of the INSEAD Directors' Network (IDN) and of Advanced Boardroom Excellence, has led numerous Board evaluations and served on various Boards at FTSE level, which firmly places her at the heart of corporate governance. One of the things she often says is that a Board will only be as good as the individual knowledge each member brings to the table. Unfortunately, most people stop their training as soon as they get an executive role.

"If you look at an organisation like Carillion, they were using cash to pay dividends to keep their shareholders happy," she says. "No-one on the board wondered why they were burning cash while having a mounting debt. I honestly believe they thought that either the banks or the Government would bail them out. There wasn't simply not enough financial knowledge on the Board to avoid this problem." Add to this a fundamental lack of communication between the Board members and the Chairman and you have a company in crisis.

In one of the Board evaluations that Pitcher conducted, everybody pointed their finger at a particular member, seeing him as someone who did not add value, by virtue of his silent demeanour. When she gave this information to the Chairman, he was flabbergasted. The Board member in question happened to be his most valuable asset, who was constantly giving him vital information about how the company operated.

"Your Board is only as good as the information that is being fed to it," she says.

Performance-based compensation has also been under the corporate governance microscope for some time. Its effect depends on the industry and culture in which a particular company operates. In publicly quoted companies, for instance, bonuses can blind NEDs to the catastrophic consequences that certain of their decisions may bring about. "I've seen some companies paying bonuses when they couldn't handle it and retaining cash to do so," she recalls. "That meant suppliers weren't paid, which is an absolutely unethical practice," she adds. Leaning on performance as a way to measure success has also been partly blamed for the recent economic collapse. Focused on their need to report quarterly results, companies were too short-sighted and failed to see the forest for the trees. As a response, a number of companies have switched to half-yearly reports but, says Pitcher, that is nothing but a half-measure. "What they need to do," she explains, "is to take a longer-term view of what profitability means for a company."

Long-termism, though, can be an abstract concept difficult to translate into a set of practices. A more readily available approach that companies can adopt is that of implementing better recruitment strategies by developing good nomination committees. In the UK, some organisations have given their nomination committee oversight as regards the hiring of managers and employees in order to create a sustainable pool from which they can pick their next director. Headhunters also play a big part in this regard.

"There are numerous CEOs, who have had several roles in different boards simply because a headhunter has been able to place them there. And headhunters get a pretty good fee for their trouble. That creates the additional problem of over-boarding. "You can always tell who is over-boarded," Pitcher says. "Their focus is split and their energy is drained."

Besides making the hiring pool more inclusive, recruiters should also start expanding the list of characteristics they look for in a Board member. As long as someone is charming and intelligent, recruiters seem to stop scratching the surface, she says. They do not ask whether that individual can competently serve the Board or be a leader. "A previous track record can be a poor indicator, as it will not always translate into a new setting," she explains.

Diversity is another hallmark of good governance. Contrary to public perception, diversity is not limited to characteristics such as race or gender. It also deals with diversity in thought. "In Board evaluations, we often see that people who are considered as nuisances or troublemakers are those with different set of opinions who are asking good questions that the others don't want to answer," she tells GOLD.

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Looking to the future, companies will be faced with an almost unrecognizable corporate landscape, says Pitcher. "If they don't keep up with technological advancements, they will be swept away by the changing tides," she notes, explaining how the fall of the high street market in the UK is a cautionary tale of how behemoths like Debenhams can turn into dinosaurs. "Artificial intelligence algorithms will become sophisticated enough to automate most of the decisions a Board member takes nowadays," she says, acknowledging that, on the upside, this will give Boards the freedom to envision a long-term plan and place their worries about short-term results behind them.

Future boardrooms, Pitcher says, will also have chairs for young people, who will be vital in helping the company to keep up with the 'flavours of the month'. "One of the Boards I'm on is going to campaign for an employee to join and then mentor that person to understand the complexities of a boardroom and to ask the right questions. I think that will give us far more insights into the culture of the company," she explains, adding that, "People look at 'happiness sheets' and study employee engagement surveys, but it's not enough. We need to get a real feel for what's happening and bringing young employees onto the Board will gives us different insights."

At the end of the day, Helen Pitcher says, a Board is the cheapest form of consultancy that any business will get. "Companies need to arm themselves with people who are mature enough to understand how to pull out the best out of their Boards and effectively manage themselves to the next level."