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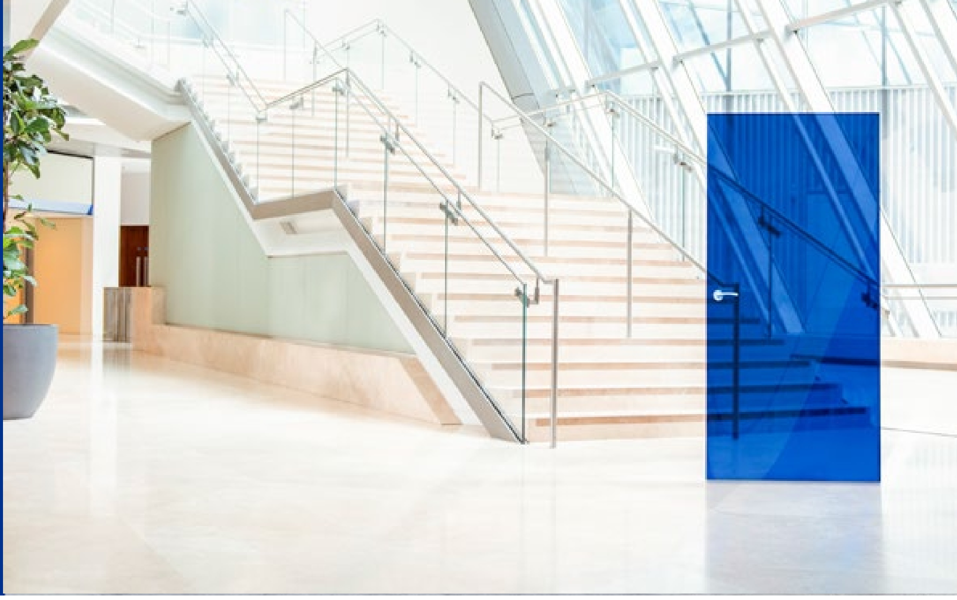
The view from the balcony: Insights on board effectiveness

KPMG Board Leadership Centre



"Non-executive directors should be on the balcony watching the dancers on the dance floor, not dancing amongst them." Dr Tracy Long CBE

We were thrilled that Dr Tracy Long CBE, one of the UK's foremost board reviewers, joined our Board Leadership Centre FTSE350 seminar to share her thoughts on board effectiveness and the challenges for the future. In this paper we summarise ten issues that arose.

1. The long and the short of it

Getting the balance right between addressing the short-term operational challenges that businesses face and dedicating the necessary time to the long-term vision and strategy has been especially hard for boards during the 'pandemic' years. The operating landscape is much less certain and predictable than it has been in the past. Inflation hikes, supply chain issues, complications from remote working, regulatory pressures and growth of non-traditional forms of competition are encouraging boards to revisit strategy much more often. Strategy needs to be co-owned and developed by the board and executive through an iterative process – an annual 'away day' may no longer be enough.

2. Making the most of strategy planning

With boards and executive teams being under so much time pressure, getting value from strategy meetings is key. Preparation is vital - consider circulating key questions ahead of the meetings, supported by robust information and deep dives to facilitate a greater understanding of the business and the risks and opportunities it faces. Would an external facilitator or 'devil's advocate' from outside the business help nurture fresh perspectives? This might be particularly useful for a board where consensus prevails.

3. Good board dynamics can transcend other limitations

If a board is working well and the dynamics are good, the precise structure (eg, unitary board, two-tier board, etc.) is less of an issue – people talk about the same things (strategy, risk and control, people and communication with stakeholders) whether or not they have the formal responsibility. Everything links to the reputation of the business and therefore the reputation of the board.

4. Be ready for activism

Shareholder activism can be seen as a force for good rather than a disruptive threat to management? With the rise of the activist shareholder in the past 10-15 years, many boards are better prepared for this scenario, though there is less preparation for active shareholders who may be looking to give strategic input or take a seat on the board. Thinking like an activist ahead of time can be a useful approach.

5. Risk and strategy; side-by-side

Risk should be aligned with the strategy, as two sides of the same coin. Executives are immersed in running the business, looking around the corner and staying competitive – as they should be. Non-executive directors are bringing a wider window on the world and may be more open to taking risk (and opportunity) than the executive team. In any event, long term strategy should be aligned with the board's appetite for risk. The 'three lines of defence model' can work well in any sector (not just financial services), as it defines clearly who owns risk.

6. ESG is <u>much</u> more than ESG

Environmental, Social and Governance (ESG) is a huge area – often with competing agendas. As such, it can be a mistake simply to put everything ESG-related under the umbrella of an ESG or Sustainability committee. For some issues – perhaps those around society and people, or systems and data – there may be better forums for discussion. Equally, responsibility rests with the full board and there may be issues best addressed at that level rather than at a delegated committee.

ESG saturation can be an issue too. Large companies have so many separate ESG initiatives it can be hard for boards to get a sense of what's working.

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Recently positive trends have emerged with harder links between ESG targets, tangible measures and executive remuneration.

7. It's not what you know...

In the ESG space, how well do you truly know who you work alongside or who you work with? With rising scrutiny and the potential to have significant reputational impact, who is responsible for the integrity of supply chains, partners, customers and clients? Some boards are debating the necessary levels of assurance to avoid damaging associations. There are no right or wrong answers but keeping the dialogue open and asking the difficult questions is important.

8. Thawing the frozen middle

Assessment tools, staff surveys, dashboards, mission statements and values are only part of the cultural picture of a business. It's the responsibility of the executive to set the culture and the tone from the top. For non-executives, understanding the culture below the executive team has been particularly difficult during the pandemic, but spending time 'walking the floors' and having face-to-face conversations with people without a specific agenda can now start to be reintroduced. Attending site visits and 'townhall' staff meetings, asking for insights from HR, internal audit, customers and suppliers and keeping in touch with social media comment is also important.

Typically, new hires are often quite enthusiastic and forward-looking. It is the 'frozen middle' – the longer serving, middle management, who may be disillusioned and frightened of change – who might have a negative impact on culture.

There are signals - is there pressure to take shortcuts or increasing tolerances towards smaller breaches? The workforce voice mechanisms introduced into the 2018 UK Corporate Governance Code (the Code) to facilitate more interaction with employees can be useful if done well.

Think about rotating the NED with delegated responsibility for bringing the voice of the workforce to the boardroom table – or having more than one to (say) cover different geographical territories.

9. Futureproofing without a crystal ball

Relevant board composition is fundamental. Effective succession planning seeks to address diversity of background, voice and perspective – but this is not always easy where the future is uncertain and it is difficult to predict where the company will be in (say) five years.

A good board needs a combination of skills, experiences and a blend of voices, including those who offer contrarian views, who can drill down into the detail, who can listen and self reflect and who can cope with intensive and detailed work around a challenging and demanding agenda.

10. Right people, right time

Succession planning, particularly for the chair role, is an area where planning ahead can pay dividends – particularly in light of the Code capping chair tenure at nine years from their first appointment to the board.

Avoiding a situation where the chair and the senior independent non-executive (the SID) leave at the same time is essential. Annual individual feedback conversations between the chair and individual non-executives are also valuable – what to do more of (or less of) in order to strengthen the team dynamics and added value of the board.

Having the right people around the boardroom table and a good relationship between the chair and the CEO generally means issues are addressed faster and more effectively.

The KPMG Board Leadership Centre

The KPMG Board Leadership Centre offers support and guidance to non-executive directors, whether managing a portfolio non-executive career or embarking on a first appointment. Membership offers you a place within a community of board-level peers with access to topical and relevant seminars, invaluable resources and thought leadership, as well as lively and engaging networking opportunities. We equip you with the tools you need to be highly effective in your role, enabling you to focus on the issues that really matter to you and your business.

Learn more at www.kpmg.com/uk/blc.

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