

Chairmen slate parts of governance code as 'crazy'

By Alison Maitland, June 27 2010

Annual re-election of board directors, as required by the revamped UK corporate governance code, is "crazy" and represents "political correctness gone mad", according to FTSE chairmen interviewed for a report to be published on Tuesday.

Their objections reinforce criticism from the Institute of Directors and Confederation of British Industry of the Financial Reporting Council's decision to insist on annual re-election of directors of the 350 largest companies.

"This shows ignorance of what the role of a chairman is all about, and is wholly inconsistent with the role's responsibilities," said one chairman interviewed for The Chairman's Perspective report by Iddas, a boardroom consultancy. "No one will subject themselves to a regime of 12 months. You need consistency and continuity."

Another chairman dismissed the measure on the grounds that it would make no difference. "If a chairman is failing, then he should be voted out anyway. If the shareholders and board haven't sussed out that the chairman needs to go, then they should all go."

The report, which examines the pivotal role of chairmen in board effectiveness, comes at a time of intense scrutiny of boards following the failures of corporate governance in the financial crisis.

The 21 chairmen of FTSE 350 companies and other large businesses, interviewed anonymously by Iddas, were divided over the code's specification that searches for board candidates should take account of the benefits of diversity, including gender diversity, to avoid the dangers of "group think".

Some chairmen warned against "formulaic representation" and tokenism. "Diversity of experience and wisdom is essential. Other types of diversity [ethnic background or sex] are completely irrelevant," commented one.

However, with women accounting for only 12 per cent of FTSE 100 directors, one chairman said: "If a board does not have a woman, they should seek one." Another remarked that the best women directors "can challenge rigorously without causing offence, which men may fail to do".

The revised code also recommends that chairmen hold regular development reviews with each director and that board effectiveness reviews should be carried out with an external facilitator at least every three years.

Some chairmen conceded that evaluating fellow directors was hard. "I find it quite challenging to ask board members to comment on the behaviour of colleagues around the table," said one. "Even when I do, I'm not sure they can be honest, and I find feedback difficult to do."

However, investors show little interest in evaluation, the chairmen said. "Shareholders are so far off the pace on governance that I'm not sure they have clear expectations of an effective board," said one. "You will find disappointment among the chairmen, because we get very little input, advice, or knowledge from our shareholders."

Managing people and relationships often takes up more of a chairman's time and energy than strategy, finance and governance, the report found. Nearly half the chairmen said issues related to the chief executive were among the toughest they faced. "The CEO is usually the biggest ego round the board table and you can't have two," was one chairman's comment.

Finding the right balance between supporting and challenging executive directors could be "bloody difficult", chairmen said. This is echoed in a separate study just published by Heidrick & Struggles, the executive search firm, which finds that chairmen are increasingly required to be "strategic and visible co-leaders" with chief executives.

"It will be even more important for them to build resilient, trust-based and non-competitive partnerships with their CEOs. This is a delicate balance which good chairmen achieve by suppressing their own egos, influencing rather than directing," says the study entitled, Purposeful Partners.

The difficulty of this balancing act has been demonstrated in BP's handling of the Gulf of Mexico oil spill and Prudential's aborted bid for AIA. Carl-Henric Svanberg, BP chairman, has been criticised for his low-key role in the company's response to the disaster, while Harvey McGrath, Prudential chairman, has come under investor fire for strongly championing the AIA bid.

The Heidrick & Struggles report, based on the views of more than 50 chairmen, chief executives, directors and governance experts, says the biggest risk in the boardroom is a supine or dysfunctional culture that prevents effective scrutiny and debate.

Boardroom culture is to be tackled in forthcoming guidance from the Institute of Chartered Secretaries and Administrators, designed to help companies understand and implement the revised code.

The guidance will ask directors to give serious attention to areas of dysfunction such as a dominant personality or group, a weak ethical culture, or unchallenging directors, according to Seamus Gillen, ICSA director of policy.

Both of the new reports on the role of chairmen reveal a fundamental conflict that should concern shareholders. The prevailing expectation is that candidates for the role of chair must have CEO experience – yet former CEOs often find it hard to shed the habit of being in charge and to switch to “influencing” mode.

Some of those interviewed by Heidrick & Struggles suggested alternative candidates with the right consultative skills, such as senior civil servants, heads of professional service firms or investment bankers, might make equally good, or better, chairmen. As one put it: “Trophy chairmen who look the part and have the right City profile may not be the right choice.”