

OPINION

¶734 The real changes sweeping boardrooms

By Lynn Ralph, Managing Director, Cameron Ralph Pty Ltd, a consultancy which assists boards provide effective leadership, improve their performance and build positive reputations.

In the past year, the focus of the discussion on governance, has by and large, focused on the regulatory side — the full implementation of the ASX Listing Rule requirements to report against the principles, the first Sarbanes-Oxley sign-off by CEO/CFO, the implementation of CLERP 9. The debate about further legislative change won't abate (even with a government controlled Senate), as governments and lobby groups deal with the issues arising out of the *James Hardie* case. These are likely to include corporate manslaughter, tort liabilities of groups of companies, insolvency laws, obligations to creditors during capital reductions, and widening directors' duties to require they consider broader community/social issues.

We know that boards are therefore dealing with different issues — but are they tackling them differently today than they were a few years ago? What practical behaviour changes are we seeing inside the boardroom? And most importantly, has the quality of decision-making within boards improved as a result?

From our experience, the first and most noticeable change is that more boards are taking the time to articulate the respective roles of board and management. Whilst most boards would say that they have always understood the division of responsibilities clearly, this has mostly been an "implicit" understanding and more often than not the cause of some unnecessary friction. Whilst not universal, we are also seeing this extended to board committees as well as to expectations of individual directors.

No doubt some will decry this as "creeping bureaucracy" however our observation is that properly done, this effort can produce a qualitative improvement in the practical day-

to-day operations of the board. It is not the document that counts but the process of developing and documenting the understanding.

Our second observation is the changing nature of board committees. It's true that audit and remuneration committees have been around a long time, but our observation is that the scope, rigour and processes of board committees has lifted noticeably. For example, the increased focus on risk management has often only been possible because the additional time it takes has been delegated to a committee. We believe that the expanded role committees are playing will strengthen decision-making in the longer term, although with committees probing further into detail, clarity around board/management roles and board/committee delegations will become even more critical.

Third, and related to the increased role for committees, is simply that more time is clearly being spent on the task of being a director (though there is no evidence of it reaching unreasonable levels). Whether that extra time is being spent on the right things and is genuinely adding value remains to be seen. One thing directors are doing with that extra time is undertaking more development activities and more training, both in-house and external — which should, over time, have a positive impact.

Fourth, board performance review is becoming more common, albeit gradually and in a variety of forms. Whether it be informal discussions between the chair and directors on the one hand, or full, external independent assessments on the other, board performance review will produce several key benefits. Firstly, it sends a strong message to management and the organisation that assessment, learning and improving is as good for the goose as it is for the gander! Secondly, unless very poorly or superficially done, it must inevitably result in some improvement in practices. And thirdly, it might one day give a board some welcome leverage with their D&O insurer!

Finally, there is a discernible (although arguably too slow) change to the fundamentals of the relationship between

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board and management. Although this remains by and large based on intuitive trust and support, more boards are practicing what one prominent director refers to as "trust but verify".

This remains one of a director's most difficult tasks — that is, maintaining a positive relationship built on trust, but at the same time, constantly verifying. (After all, the management you trust as competent today, is constantly facing a changing environment. Simply trusting that they will always be as competent as they were yesterday is to ignore the evidence of many of the recent disasters.) For example, many boards which traditionally interacted with only the CEO and CFO, are now insisting on having first hand contact with one or more levels down — not because they don't trust the CEO, but rather to satisfy themselves of the depth and quality of the whole senior management team.

Overall, these changes should have a positive impact on the quality of boards' decision-making. But further progress will only occur if shareholders keep the pressure on. With the Australian share market putting in a stellar performance in the last 12 months, we risk the re-emergence of the all too familiar "love is blind" syndrome. But that's a story for our next article.