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REGULAR BOARD EVALUATION IS MORE THAN SIMPLY A RECOMMENDATION

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Management guru, Peter Drucker, is often quoted as saying, *"If you can't measure it, you can't manage [or improve] it"*. Constructive feedback is integral to a process of development, growth and improvement, not least in an organisational setting, and especially in the case of boards of directors. In their leadership roles, directors are expected to fulfill their statutory, fiduciary and ethical duties towards an organisation, and their performance in this role should be evaluated so that their effectiveness can be assessed and tested against best practice and appropriate benchmarks. Where lacking, actions for improvement should be put in place -- whether on an individual or collective basis -- for the benefit of the board as well as for the organisation and its stakeholders.

Good in theory; required in practice?

In South Africa, and many other countries internationally, there is no statutory requirement that board evaluations be conducted, so boards may be forgiven for treating an evaluation as a box to be ticked on an annual or biannual basis, if at all.

However, in addition to the intuitive benefits of evaluating the performance of the board on a regular basis, the requirement to do so is in fact becoming more of a critical governance imperative for organisational sustainability.

The King IV Code on Corporate Governance for South Africa, 2016™ ('King IV™'), which is regarded internationally as a gold standard for good corporate governance, states that "the [board] should ensure that the evaluation of its committees, its chair and its individual members, supports continued improvement in its performance and effectiveness".

The reporting requirements in Principle 9, Recommended Practice 75 of King IV™ require that the integrated report includes "a description of the performance evaluations undertaken during the reporting period, including their scope, whether they were formal or informal, and whether they were externally facilitated or not; an overview of the evaluation results and remedial actions taken; and whether the [board] is satisfied that the evaluation process is improving its performance and effectiveness".

"Mounting stakeholders' expectations, challenges faced by companies to operate under fluctuating economic conditions, pressures of globalisation and increased regulatory requirements have brought the quality of performance of the Boards of Directors under greater scrutiny. Boards have recognized that it would be important for them to continually assess how effectively they are performing their roles against the objectives and the goals they have set for themselves."

Performance Evaluation of Boards and Directors

Deloitte

King IV™ follows an "apply and explain" approach to governance compliance, meaning that its principles should be applied by all organisations wishing to practice good corporate governance. Organisations should then go further and explain to their stakeholders *how* the application of the principles has contributed to the enhancement of governance in that organisation. Proof of the completion of a board evaluation, whether conducted internally by the Chairman of the board and the company secretary, or externally by a duly appointed service provider, is one way in which an organisation can demonstrate its application of good governance principles to its stakeholders. Showing that the recommendations arising from the board evaluation are being actioned certainly adds weight to the claims made by the board; that it is indeed strong in its leadership, vision, experience and independence.

In addition to the "apply and explain" imperatives of King IV™, the principles of the earlier King Code on Governance for South Africa, 2009 (King III) -- including the requirement that board evaluations be conducted -- have found their way into common law through court precedent, which begs the question why all organisations are not implementing board evaluations as a matter of course?

In countries other than South Africa, corporate governance codes will usually require listed organisations to conduct board evaluations, with a recommendation that all types of organisations do so. Generally, if board evaluations are not conducted, sufficient explanation must be provided as to why not.

Add to these governance imperatives and guidelines the demands made by an organisation's informed stakeholders that the board must be held accountable for its actions, as well as that the organisation itself must be accountable for the composition, skills, independence and diversity of its board, and the process of evaluating the manner and degree to which the board lives up to these demands, becomes essential.

Why board evaluations matter

Organisations may still remain unconvinced that they need to conduct a board evaluation, since the implementation of the provisions of King and other corporate governance codes are generally not mandatory. In addition, some organisations may feel that stakeholders can be convinced that the board is indeed functioning as it should, since the organisation is generating profits and potentially creating value in the short term.

However, there are other matters which should be considered, and which impact the organisation's value creation in the medium and longer term. Before disregarding the necessity of a board evaluation altogether; the benefits to the board itself, the directors individually and collectively, including the organisation's stakeholders and the organisation as a whole must be carefully considered.

"Boards continually need to monitor and improve their performance. This can be achieved through evaluation, which provides a powerful and valuable feedback mechanism for improving effectiveness, maximising strengths and highlighting areas for further development. The evaluation process should be objective and rigorous."

Financial Reporting Council (United Kingdom)

(2018)

Board evaluations provide concrete evidence of whether or not the board members are in fact ensuring that the strategic direction of the organisation is being followed and whether or not they are fulfilling their fiduciary duties in the best interests of the organisation and its stakeholders.

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Board evaluations act as a beneficial feedback mechanism for improving the effectiveness of the board, and will assist the organisation to formulate and maintain a board matrix, which will track the strengths and weaknesses of its members, highlighting skills or knowledge gaps, and areas for further development, improvement and training, as well as future director rotation and appointments. Team dynamics will be analysed and can be adjusted or improved, and through this process, a sense of mutual trust and appreciation will be developed between board members, including executive management who interact with them at board and sub-board committee levels. Primarily, the process provides an ideal opportunity for directors to gain clarity on the performance standards required of them, as well as being reminded of their legal and fiduciary duties and responsibilities.

On an organisational level, there are many benefits related to conducting board evaluations, including the fact that they may assist in identifying problem areas within the board and its sub-board committees or between individual members of the board and the committees before they become a crisis. Board evaluations done correctly also assist to improve relationships between the board and executive management, by highlighting areas which may be problematic; clarifying what is expected from board members in terms of their performance; and ensuring high-level policy frameworks exist to guide the organisation.

"Board assessment is both a critical opening step and concluding phase of the board-building framework. Done well, it provides fantastic opportunity for boards to monitor their progress and renew their commitment to doing good work. Done badly… it can turn into a mechanical exercise that tests the board's patience and creates little or no value."

Source: Building better boards, by B Behan

Board evaluations must be done right

In order to obtain the optimum benefit from conducting a board evaluation, it must be carried out diligently, intelligently and thoroughly. Undoubtedly, a level of 'maturity' is required amongst the members of the board and its sub-board committees if the evaluation is to be effective. The outcome of such evaluations may often result in some tough truths being revealed about the functioning and effectiveness of the board and its members. If done ineffectively, board evaluations may cause substantial harm to the board and its members, and possibly to the organisation as a whole.

The fact that a regular internal and external board evaluation is part of the organisation's culture and embedded within its Corporate Governance Framework®, indicates its commitment to sound governance and demonstrates its continued accountability to its stakeholders. Indeed, if a monetary value, or return on investment could be calculated to demonstrate the benefits of organisations conducting a meaningful board evaluation, it would be clear that in the pursuit of long-term sustainability and the legitimacy of an organisation, the process is in fact essential and its value incalculable.

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