

PROFESSIONAL INSIGHT

**SolonGroup**<sup>TM</sup>  
*Restoring Possibility*<sup>TM</sup>

# INDEPENDENT DIRECTORS: DEAD, OR ALIVE?



REPRINTED FROM:  
MAY 2010 ISSUE

© 2010 Financier Worldwide Limited.  
Permission to use this reprint has been granted by the publisher.

[www.financierworldwide.com](http://www.financierworldwide.com)



**FINANCIER**  
WORLDWIDE corporatefinanceintelligence



PROFESSIONAL  
INSIGHT

CORPORATE GOVERNANCE

Independent directors: dead, or alive? | BY DEBORAH HICKS MIDANEK

Independent corporate directors today – those directors the public counts on to provide impartial and seasoned judgment on their behalf to corporate decision making – are behind the eight ball. No amount of exhortation, self examination, or regulation will fix the basic problems they face in executing their jobs well.

First, the nature of the decisions they are required to make has radically changed over the course of the last 30 years of technological and financial innovation. The complexity of the issues at hand and the required speed of analysis, understanding, and action have increased exponentially during that time, while the tools available to directors have expanded slowly.

Second, the role of the independent director is inherently ambiguous. Does the director represent the shareholder, and if so, does that responsibility run directly to the shareholder, or does it run through the corporation? Does the independent director have the authority to hold management accountable, or is the goal to be collaborative and advance management's agenda for the company? Can these roles be reconciled effectively and clearly? Where does the director's formal authority come from, and to whom is he in turn accountable?

Third, who sets the agenda of the board? Who sets the agenda that determines what items the board considers, and how they are presented? How freely is the director encouraged to explore the issues he or she is most concerned about?

Fourth, who interprets the corporation's position to the board? Typically, information about strategy and competitive position is filtered through the lens of the CEO, with assistance as needed from the CFO. The board sees and hears and interprets information as the CEO sees fit.

Fifth, in the boardroom certain views of the company's advantages and disadvantages take root and become held as firmly as fact. Repetition often takes the place of verification, and the link between being, for example, 'the low cost producer' and having a competitive advantage in serving the customer is assumed, not investigated. Being the low cost producer may not be an advantage if, for example, customers are not sensitive to price, or if transportation cost to market wipes out the difference.

Sixth, often the culture of the board itself makes it impossible for a single director to be effective. Despite progress in recent years in use of the executive session, how freely can and do directors talk to each other? It is very difficult to be the sole questioner, the only holdout, the constant challenger, and still have credibility within the group to sway the group's process.

Seventh, board composition has a huge impact on effectiveness of the group. Individual directors vary widely in their interpretation of the board's role in key areas such as strategy and risk management. There are many directors still in place who believe they serve at the pleasure of the CEO, and that their job is to support the CEO until and unless the CEO does something so egregious action must be taken, or he retires. Other directors, more eager to challenge the CEO's assumptions and actively participate in strategy formulation and identification of risk are drowned out, or face a tough road avoiding being dismissed as boat rockers who want to micro manage.

Eighth, CEO's as a rule do not consider themselves accountable to their boards, so don't speak clearly and plainly to them about the range of risks and rewards related to particular actions. Talking to the board is often seen as a burden, an afterthought, or a necessary but somewhat irrelevant evil.

Ninth, communication between board and shareholders is generally seriously constrained by fear of improperly divulging information, creating multiple and possibly conflicting voices for the company, or undermining the CEO. So the board is insulated from the concerns of shareholders, lenders, employees, suppliers, and customers alike.

Given all of the above, it is hard to imagine how boards can ever be effective in steering the affairs of the corporations for which they are responsible. No wonder boards are often regarded as impotent.

And yet, when the going gets tough, who is responsible? The board. As the perpetual body responsible for the survival of the corporation, the board in the end has a very clear role. And remarkably, boards often rise to the occasion and handle themselves and the demands of the particular source of distress well. What makes the difference, and how can boards functioning in good times learn from boards managing in

distress?

First, the board suddenly has advice and counsel directed to and by it. Those advisers (lawyers, investment bankers, accountants) who in good times are typically chosen by and see themselves as working for management, realise that their real audience is in fact the board, as management may or may not last. Time is taken to explain prospective transactions and structures, to unbundle them and be sure that the board, beneficiary of the business judgment rule, has a real basis on which to make a decision.

Second, the role of the board is not only much clearer, but gets respect as the guardian of the enterprise's very existence. Time and effort is spent on considering the issue of who it is the board must serve, and why various actions will or will not help the board to carry out that mission.

Third, often independent board leadership and voices emerge that demand the ability to set the agenda of the board, as directors no longer passively accept that someone will tell them if something important happens.

Fourth, the CEO's voice is no longer the only voice interpreting what is going on. The board learns to listen to the CEO, and provide support, while also evaluating information from other sources. A healthy scepticism develops, and the board looks carefully at whether the CEO is up to the task at hand, or in fact is responsible for the creation of the difficulty. The board naturally seeks data from beyond the C Suite, inside and outside of the company.

Fifth, corporate myths can suddenly be examined and challenged, as the board often seeks independent reviews of key assumptions about the

company's position. Often a more complete picture emerges; one upon which a realistic plan of action can be based.

Sixth, the non management members of the board, once leery of sending negative signals to the CEO by talking amongst themselves, now realise they must talk regularly and speak plainly, to be sure they are seeing the situation and the CEO clearly, and are prepared to act, either in support of the incumbent, or in choosing another direction. Dysfunctional politeness goes, leaving candour and a sense of shared responsibility in its place.

Seventh, the credibility of those directors who see their main job as supporting the CEO is undermined, and those who bring a more independent view to the table are more clearly heard.

Eighth, CEOs who once shunned the board now speak openly, in an effort to build support from the board and to spread accountability for outcomes.

Ninth, the board is now actively involved in communication strategy, and often participates in meetings with various constituents to listen and learn what is on their minds.

What, in the end, is the difference between the behaviours in the two scenarios? In one, the board allows itself to be lulled into a comfortable dream state, in the complacent belief that if there is a problem, management will tell them. In the second, the board has been awakened from its drowsy reverie, and understands that it had better get its act together and breathe life into the job it and no one else is charged with doing. Which is the more desirable scenario, and how can a crisis atmosphere become the status quo, setting the scene for board best practice? ■



**Deborah Hicks Midanek** is president at Solon Group, Inc. She can be contacted on +1 (917) 853 3598 or by email: [dhmidanek@solongroup.com](mailto:dhmidanek@solongroup.com).

Deborah Midanek counsels imperilled companies and their constituents and has led various businesses through strategic, operating and financial challenges. She enjoys a reputation for thinking creatively, and contributing to realising unusually strong results. Ms Midanek holds an MBA from Wharton and an AB from Bryn Mawr College.