

The Four Constituencies of the Chairperson of the Board

A Perspective by Intrabond Partner, Donley Townsend

Context or Confusion

What exactly is the Chairperson of the Board supposed to do? Adrian Cadbury, one of the most respected voices on corporate governance, invoked Cicero to describe a good chairperson as one “who sits quietly at the stern and scarce is seen to stir.” But this is a more oblique definition than most want. America’s former Secretary of State George Shultz, himself an experienced independent director, may have described a chairperson’s situation well in writing about his years as a Dean at the University of Chicago. “Here I was with a variety of constituencies, none of which was under my control. I had the responsibility for the health of the organization, but my only real authority came from my persuasive powers. I learned early on that I must be able to persuade if I was going to be effective.”

Chairpersons provide leadership for increasingly independent boards under conditions of increasing scrutiny from shareholders with divergent interests, regulators with changing rules, and managers with more granular knowledge. It is a challenging role. The summer of 2010 brought this into stark relief as we watched the non-executive Chairperson of British Petroleum face a plethora of demands from many directions in the aftermath of the drilling platform explosion and the ensuing oil spill in the Gulf of Mexico. A little later the board of HP found itself embroiled once again in conflict with its CEO and faced public criticism from a number of quarters not least from shareholders who found themselves out about \$10 billion. These and many other situations provide ample support for the view of Peter Gourevitch and James Shinn in their book *Political Power & Corporate Control* that “corporate governance – the authority structure of a firm – lays at the heart of the most important issues of society... It is no wonder then that corporate governance provokes conflict.”

So, set aside the calls for splitting into two a role mostly one. Set aside the idea of an independent, non-executive Chairperson as a best practice. Forget the notion of a separate Chairperson as a marker of “more transparent”. What is the role and what are the responsibilities of the Chairperson of the Board?

The Idea of Constituencies

Our laws in the United States do not require Chairpersons. So, they have no statutory authority. Chairpersons have one vote on the board, the same as each of the other directors. Whatever powers they have are granted by the board or by the shareholders directly. Effective Chairpersons are effective because of their ability to gain and keep the respect of four constituencies: shareholders, the board itself, relevant outsiders (sometimes called *gatekeepers* or *reputational intermediaries*) and the CEO. Each constituency makes demands on the

Chairperson and fulfilling the needs of all four constituencies is what makes a Chairperson effective.

Constituency One: Shareholders

The shareholders claim on the attention of the chairperson and the whole board is perhaps the clearest and most easily understood. It has a long history and is established in law as well as custom. Jonathan Macey, in the introduction to his book, *Corporate Governance: Promises Kept, Promises Broken*, says “the purpose of corporate governance is to persuade, induce, compel and otherwise motivate corporate managers to keep the promises they make to investors.” The Chairperson ensures the board discharges its responsibilities to shareholders largely by and through controlling the agenda of the board meetings.

Custom and long usage prescribe the Chairperson’s responsibility to insure the right matters are put before the board and the right information is provided by management. Now, this is a very easy responsibility to describe but a very difficult one to execute. Shareholders vary widely in both their expectations and demands. An individual shareholder with a tiny stake in the company may want nothing more than to follow the rational ignorance path and manage risk through diversification. Other shareholders may be activists with a cause that defines their relationship and expectations. Still others may be material shareholders who rely on the dividends and therefore value continuity above everything. And, in most firms today, managers and employees are shareholders as well. If the Chairperson is to produce the value the many advocates of the independent Chairperson desire, then he or she must begin by leading the board in representing the interests, however complex they may be, of shareholders. To do this the Chairperson must know who the major shareholders are and why they own the stock. He also needs to be aware of how much of the stock is simply being rented by traders for a few minutes or days. Understanding who the shareholders are and what their various expectations are will inform everything the successful non-executive Chairperson does and does not do.

Constituency Two: The Board Itself

Boards of directors are at best episodic teams. Most boards contain a high-octane mix of intelligent, talented, and successful men and women who have evidence that their views and judgments are valuable. It is the Chairperson’s job to orchestrate this talented group to perform at a high level in advancing the cause of the organization. A critical first step for the Chairperson is to insure the best possible board composition. This means assessing the collective knowledge, skills, and abilities of the directors against the demands imposed by markets, technology, managers, regulators, etc. It requires a Chairperson who can tell a director when it is time to go and recruit men and women of uncommon ability and achievement to join.

Once the Chairperson has the best six or eight or twelve talented people, he or she must guide assignments to committees and insure the committees have the resources and information they need. He must also understand the unique competencies of each individual director and seek to draw out those competencies for the good of the board and the enterprise. The Chairperson must also establish and maintain standards of performance for board members beginning with the

recruitment and selection process. Everyone considered for directorships possesses a demonstrated capacity for hard work but the Chairperson sets the tone for what is expected from individual directors.

The Chairperson must also insure the board functions well as a group when it meets. And this is no easy task. A board too collegial will likely be ineffective in monitoring managers; a board insufficiently collegial will likely be unproductive. Knowing where the balance point lies requires a deep understanding of individual behavior and group dynamics, the wisdom to use this knowledge effectively and the courage to do so.

Beyond the growing burden of committee work (some of which the Chairperson must shoulder), he must also focus the whole board on strategy, risk management, leadership succession and other matters of governance.

And what tools are available to the Chairperson? While he ostensibly controls the agenda of the board meetings, these days his task is largely trying to squeeze everything to be done into the time the directors can reasonably be expected to devote to board work. The non-executive Chairperson of a major Midwest financial firm described the work involved for him in managing the board's meeting agendas. He meets with the CEO twice a month for lunch to make sure he has his views on the agenda. These face-to-face meetings are supplemented with phone calls and e-mails. In addition, the Chairperson speaks with the General Counsel once a month. He also has regular conversations with the CFO, the Treasurer, the Chief Risk Officer and the Chief Human Resource Officer. He describes the interactions as, "I call them for information but never manage them. This is how I make sure that the board has the information it needs, when it needs it. And, it how I make sure I have a sense of where the big issues are. Where we will need lots of time for dialogue and deliberation and where we can move rapidly." Another non-executive Chairperson described his discipline of speaking with each director one-on-one in preparation for each meeting. "These conversations, some in person, some by phone, enable me to understand where we might want more discussion. They're important to one of the essential jobs of a Chairperson, making sure the board meetings are valuable, well run. I owe it to the other directors to make sure our time is well spent."

Constituency Three: Relevant Outsiders

In his 2006 book *Gatekeepers: the Professions and Corporate Governance*, John Coffee warned, "no board of directors – no matter how able and well-intentioned its members – can outperform its professional advisors. Only if the board's agents properly advise and warn it, can the board function efficiently." Auditors, securities analysts, attorneys, compensation consultants, and investment bankers regularly advise boards on critical matters. Other outsiders including actuaries, public relations firms and executive search firms bring important information and advice to boards from time to time. The Chairperson bears the major responsibility for the selection, evaluation, and retention of the advisors the board will rely on. He must insure their capabilities are right and their performance sound. The Chairperson must strike the balance between reliance upon information from management and information from outsiders since no

board can deal with all the available data. So, as in the case of the board constituency, the Chairperson must be able to assess and select the best possible advisors for his firm. Then he must be capable of setting and maintaining high standards for their work. And, finally, he must understand the needs of each of the firm's gatekeepers and insure their voices and views are heard by the whole board and by top management appropriately.

Beyond the reputational intermediaries, key customers and suppliers may likewise have an occasional claim on a Chairperson's time. In fact, nothing provides the experienced business leader with a better pulse of an enterprise than regular, candid conversations with customers and suppliers.

Journalists, political leaders, regulators and shareholder services firms may also have occasion to reasonably seek some of a Chairperson's time. Crisis situations in particular can thrust a non-executive Chairperson into the role of speaking for the company to any number of publics.

Taken together, the Chairperson's relationships with the company's relevant outsiders are critical in establishing and maintaining an informed independence.

Constituency Four: the Chief Executive Officer

During the many years in which the norm was a combined Chairperson/CEO role and before the recent repeated calls for the separation of the roles, the question of the relationship between the two positions was moot. In recent years, much has been written and said about the wisdom of separating the roles but little about what would then characterize an optimal or even good working relationship between a part-time, non-executive Chairperson of the Board and the Chief Executive Officer (or between a Chairperson/CEO and a lead independent director). British, German or Japanese models of corporate governance might provide some useful perspectives. But no matter which vantage point you look from, the relationship between a Chairperson and a CEO is complex.

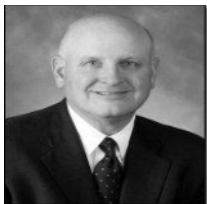
CEOs themselves are usually complex people. The complexity of the relationship with a Chairperson deepens since CEOs are almost always fellow board members. The demands of the relationship for the Chairperson can also vary greatly depending on the tenure and backgrounds of the two individuals. A long serving Chairperson and a new CEO will have a different relationship than a new Chairperson and a long serving CEO. The Chairperson of a young, high growth company with a young management team will have a much different relationship with the CEO than will the Chairperson of a Fortune 100 firm. Yet the board put the CEO in his job and the board can take him out. So Chairpersons have important work to do in managing the relationship with the board member who happens to be CEO. For many (probably most) Chairpersons this involves being a sounding board on some days and being the person who asks the hard questions in a soft way on other days. But whether sounding board or questioner, the Chairperson must take the lead in establishing and maintaining a productive relationship with the CEO. Carl Wick, the longtime Chairperson of the Federal Home Loan Bank of Cincinnati, says, "Make no mistake. In the relationships that work well, the Chairperson reaches out."

Chairpersons usually communicate the board's appraisal of the CEOs performance. Walt Higgins, former Chairperson of NV Energy noted, "Performance feedback is a very important role of the Chairperson. It cannot come from the whole board. The Chairperson must synthesize it so it can be constructive." Chairpersons are usually the source of informal feedback as well.

To carry out the work of building and maintaining a relationship, the best non-executive Chairpersons view the CEO as an important constituency. Whether in person, over the phone or via e-mail, Chairpersons and CEOs in companies where both view their relationship as both cordial and effective report frequent, open and wide ranging communication. Almost all talk or e-mail more than once a week. One experienced non-executive Chairperson who had also served as CEO of two public companies said, "The Chairperson must be available, must be proactive, must communicate what he sees. You can't be afraid to say, I think you need to look at x or y. At the same time, you must realize that the CEO has a lot to do every day."

Conclusion

Prescriptions for boards of directors are dangerous. Sometimes even so called best practices do not fit well with a company's needs at a particular juncture in the organization's development. Companies can swing from good performance to crisis in a short time. Markets and regulations change. New competitors emerge. Constituencies seem to form and fragment and multiply like the picture in a kaleidoscope. CEOs resign, some even die in office. And through all these changes, we want the Chairperson of the Board to provide just the right blend of magic to keep everything going well. No wonder Sir Adrian Cadbury turned to Cicero, one of the giants of the ancient world, when he sought a description for the role of the non-executive Chairperson.



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Don Townsend is an Intrabond Capital strategic partner. As an executive search consultant and coach for senior leaders new to their roles, Don has experience in the energy, computer, telecommunications, instrumentation, IT services, financial services and engineering/construction industries. He has conducted senior leadership and board of director assignments in Canada, France, Germany, Great Britain, Japan, Mexico, the Netherlands, Sweden, Switzerland and the United States. He is particularly skilled in finding European leadership for US firms and American leadership for the US operations of European firms.

Don assists Chairpersons and CEOs in recruiting directors for their boards. He has published articles on governance topics in *Directors Monthly* and *Strategy & Leadership*.

Don was a Vice President at A.T. Kearney, the global management consultancy, from 1997 to 2003. Prior to that, he held Human Resources positions with Hilti AG, Telex, Teradata, NCR and AT&T. During his industry years, Don also held leadership roles in Quality and Marketing. Don has bachelors and masters degrees from The University of Texas at Austin.