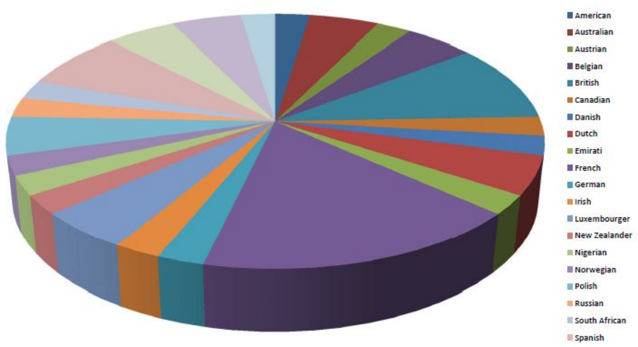
Improving European Board Effectiveness – insights from participants of the INSEAD International Directors Programme

A healthy capital system is an important ingredient for European competitiveness. Indeed, investors look for stability and predictability, which leads to the necessary flow of capital into our markets. Besides the key role government plays in creating confidence, there are three main actors in the capital system: "owners" who supply financial resources, managers who apply their expertise to build attractive returns on the owners' investments, and boards of directors that oversee the process. The entire system relies on each actor contributing such that economic value is created.

However, many recent media reports on corporate scandals and the financial crisis — which can then lead to sovereign crises — have placed much of the blame on boards saying they have not fulfilled their duties. It seems that boards of directors in many regions are the *achilles heel* of the capital system.

Efforts to increase European competitiveness should include plans to improve board effectiveness. The question is what improvements would be most beneficial? What changes are low-hanging fruit – relatively easy to implement, but have significant impact? These are questions we gave to 40 participants of theInternational Directors' Program at INSEAD. This program is designed to help directors hone their skills and identify best practices for overseeing organizations and managers. The participants represent most of the EU in addition to other regions of the globe (see chart below, IDP4 participants by nationality). They're in the governance trenches observing first-hand the good and bad of European boards. What do they think will improve board effectiveness?



We ask our participants to identify the practices and changes that would most significantly improve European governance. The suggestions included:

Participants of IDP 4:

Tips for Improving European Board Effectiveness

- More independent (from management) directors
- Diversity of thinking (not just board network)
- Higher quality board members
- Higher quality chairs
- Better information flowing to boards
- Restrict number of board appoints for individual directors
- Independent selection of board members (based on meritocracy)
- Improve transparency (better disclosure conflicts of interest)
- More involvement in strategic issues (new markets, acquisitions, etc.)
- Recognize/learn from failures
- Better organization of meetings and agenda
- Improved orientation and training plans for directors
- Less employee representation
- Directors spend more time on board work
- Ensure differentiated strategies
- Be more aggressive/tolerate failure
- Ensure differentiated strategies

Two improvements on the list were identified by nearly all IDP participants and interestingly were common across European countries.

Visit INSEAD Knowledge
http://knowledge.insead.edu

First, the most common response from the list was to ensure more **independent directors** on boards. Many IDP participants complained that managers tend to have too much control over the business investment process. "And many directors feel obligated to managers and thus are not willing to fully test their ideas and assumptions, too They were not suggesting that boards take over responsibilities from managers. Indeed, boards must keep their hands off the controls. However, they did suggest that boards must serve as more critical evaluators and engage in thorough debate even when managers are stubbornly defending a particular direction. In addition, independent directors are more capable of identifying and addressing conflicts of interests that may cloud the managerial decision-making process. For example, what happens when a CEO's compensation plan rewards growing revenues and the CEO continually suggests acquisitions? Independent directors are more likely to see and deal with these issues. Our group recommends directors are independent from managers, do not all come from the same informal networks, and do not represent specific shareholders only. The underlying principle is to attract independent thinkers who will fully apply their skills.

Second, **diversity** on European boards was cited by many IDP participants as a critical factor for improving effectiveness. Interestingly, this diversity was not particular to gender, which is forefront in the media and the focus of recent regulatory initiatives. Rather our group recommended many kinds of diversity – nationality, industry and functional background, age, culture, etc. It is interesting that many telecommunication (cell phone) companies attempting to capture the lucrative 15-25 year old market have boards where the average age is over 50. Boards continue to look like "old boys networks."

There are many opportunities to improve board effectiveness and we only list a few. Our IDP participants have enrolled in this program to improve their board effectiveness skills through discussions of best practices, case studies and expert insights. It is clear from their interactions that board effectiveness is complex. However, competitiveness relies on all of us making changes to move boards forward such that they are fully contributing to a healthy capital system.

–

Tim Rowley - Professor of Strategy and Organizations, Director of the Clarkson Centre for Board Effectiveness, Rotman School of Management, University of Toronto.

Visiting Professor, INSEAD and Co-Director of the INSEAD International Directors Programme.

Find article at
https://knowledge.insead.edu/blog/insead-blog/improving-european-board-effectiveness-insights-from-participants-of-the-insead-international-directors