Rules of Engagement

Improving Communication Between the Board and CEO

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Senior management and the board need clear communication to work effectively with one another. Too often, however, these groups repeat that famous scene from Steve McQueen's movie, Cool Hand Luke: "What we have here is a failure to communicate."

This need for open and effective communication may go without saying. But a corporation faces challenges when it appoints the same person as CEO and chairman of the board. This is true even when the decision was made to attain a unified vision and voice at the top.

The following suggestions will foster productive communication between the board and senior management when the unified structure is present:

1. **Increase the influence of the outside directors on the board's agenda.**

   A subtle but substantial shift occurs in the mind of an outside director who is chosen to lead the board's deliberations. This shift should lead to greater care in the preparation of the board's agenda, in the solicitation and use of views of other independent directors, in the care given to the content and timing of the board agenda, and to the handling of follow-up questions and assignments. Other independent directors will also find a new voice.

2. **Add regular formal sessions for the non-affiliated directors — with both fixed and flexible agenda items.**

   Directors should be careful to avoid setting up a two-tiered board. Insiders know more about the company and may be better informed about the industry, so meetings called without the presence of all directors should be regular but occasional, and should deal with specific matters that deal with performance of the insiders (including the CEO or other officers who also sit on the board). Such items may include succession planning, establishment of hard and soft performance targets for senior management, and the content and conduct of board meetings.

3. **Arrange for communication between the board and key members of senior management.**

   Much of this should be formal, to familiarize the board with the style and skills of other senior management people. Succession planning is thereby improved and the potential that the CEO might exercise too much control over the information presented to the board is lessened. Informal communication should not be used to isolate the CEO or to "triangulate" expressions of concern, but such informal communications will give the board insight into the health of the executive suite and may produce information that prompts the board to drill deeper on certain matters.

4. **Periodically measure the board's performance against negotiated standards and resolve to replace or improve less effective directors.**

   The chairman should seek professional support when measuring the board's performance. The chairman should be light-handed here, because board members may be ill-advised to record written comments about perceived failures of individuals or the board as a whole. Good advice is, "Don't write it down if you don't want to explain it to the judge." But seasoned corporate counsel is accustomed to advising in this area and can help the chairman structure this self-assessment in a way that improves performance without exposing the company or the directors to unneeded risk. (In the mutual fund area, the SEC has offered some guidance and such companies, registered with the SEC under the 1940 Investment Company Act, are now required to conduct an annual self-assessment.) In any event, evaluation models are now widely available and have been around for a season for operating companies.

5. **Clarify rules governing board access to external and internal professional services in the areas of legal, audit, and executive compensation.**

   Boards frequently use legal guidance in matters of public disclosure documents on which directors' signatures are required. The chairman should discuss with the board expectations about use of inside counsel and/or outside counsel for this exercise. Again, in the area of executive compensation, the board might utilize professionals in the corporation's human resources department and/or from outside consultants. In doing so, clear rules of engagement should be established. The board may wish to engage its own consultants. But if inside professionals are to be removed from the drill, then the rationale should be explained to the insiders from whom much of the data may be requested and by whom the decisions must be implemented. Career expectations of insiders may be impacted by these decisions and the CEO should understand these implications and convey them to the board for its consideration as decisions are reached.

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