

The Future of the Board: Information will help it sink or swim

“Knowledge is power” goes the old Roman saying, and this still rings true today -particularly in the corporate world. Around the world, the effects of past corporate scandals have left their mark in the form of new legislation--with a greater onus on the company’s board of directors to provide sound governance systems. The “right” information at the “right” time is crucial for a board to be effective. But are company boards equipped to succeed in their new, more powerful role?

IMD Professor Ulrich Steger - Director of the Building High Performance Boards program - and Research Associates Jochen Brellochs and Wolfgang Amann set about finding out. As part of a comprehensive IMD study that took place between December 2004 and March 2005, they interviewed and send questionnaires to 4,700 board level executives from every major economic region worldwide. This is what they found out...

The effects of past corporate scandals, e.g. WorldCom in the US and Parmalat in Europe, were significant and appear lasting: investor, consumer, and employee confidence in corporate behavior were shaken to the core. Most countries reacted with fundamental new legislation targeting corporate organizational structures, disclosure requirements, or directors’ and officers’ liabilities. The board’s role has changed and become even more crucial for companies’ government systems. Clearly, boards today play the predominant role in modern corporate governance. As a result, board members’ responsibilities and tasks are broader and the complexities and dynamics surrounding the board’s work have increased tenfold. But with global corporate governance activism fading, the bad taste of past scandals remains: Will the “new corporate governance” work out and will the board succeed in its crucial, more powerful role?

Cause for concern?

Businesses spend millions on organizational development, but how much do companies invest in educating and updating their boards? “Knowledge is power” according to the old Roman saying and it seems more

important than ever. The availability of information, sources and knowledge determines how the board can influence and monitor management and its decisions, and how involved the board is in the company in general. Information supplied to the board indicates what is expected from its members, and whether it meets the standards the board needs to fulfil its expected tasks. Information-flows and sources are significantly representative of how powerful the board is. Also the timeliness of information is essential. Overall, information gives the board either a strong and influential role, but if it is missing it can equally put the board out of action.

General aspects

Our research indicates that 50% of boards meet between 4 and 6 times a year. However, another 44% meet more than 6 times a year. For the large majority of board members (>60%), only a very small part of the information they receive during the course of their full-time jobs is relevant to their board work. The board book of documents provided for every board meeting is usually kept small, and for 80% of boards, it does not exceed 50 pages. Surprisingly, 44% of board members also receive less than 10% of the information for every board meeting electronically.

Content of board information

When asked whether or not board members felt well informed about several fields relevant to their business, considerable differences showed up. About 90% claimed they were well informed about corporate and business strategy and financials. For organizational and human resources, it was still more than 70%. In topics “external” to the company, boards have different roles and influence. More than two-thirds are well informed about the company’s markets and the political, legal and societal issues related to the business. However, about one-third of the board members felt uninformed about direct competitors, market dynamics and developments and industry trends. It remains questionable whether this is sufficient to describe the “bigger picture” about the company’s business. In several

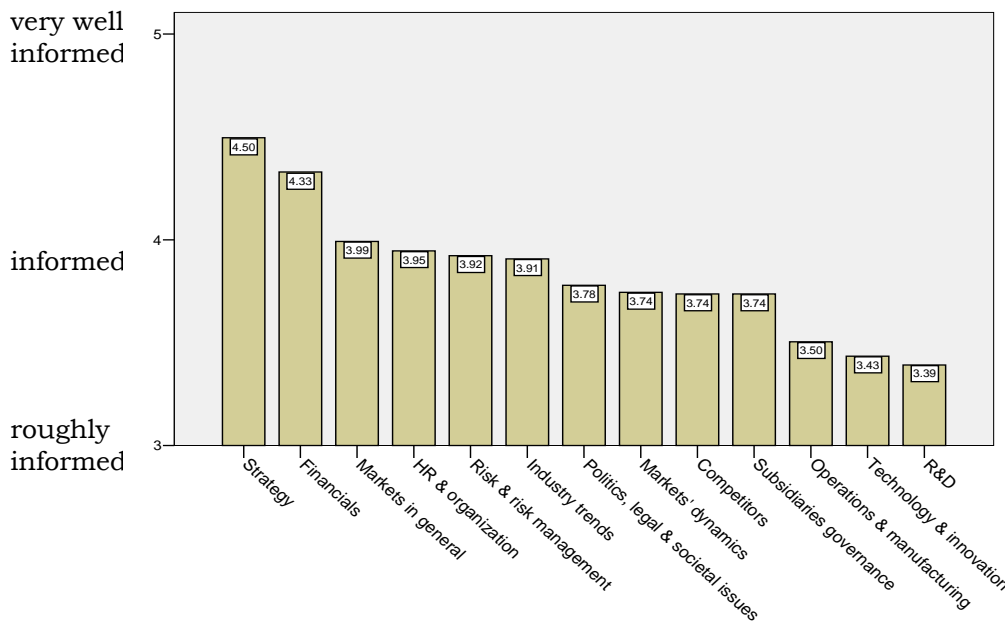
The information provided to the board is still mainly focused on the past. Less knowledge of the fields important to the company’s future and strategic success predicts severe difficulties for board members in anticipating the future development of the company. New fields of information seem to be rather slowly integrated into the board’s information systems: Though past crises had a huge impact on the board’s role, more than 30% of board members only have vague knowledge or less about the company’s risks, risk management efforts or the main activities of the company’s subsidiaries.

Different board positions, different information?

Roles and information inside boards also vary: Different board members have different functions and are supplied with different information. Corporate strategy and financials are core information fields for every position. However, for both fields, board chairmen showed slight informational advantages compared to ordinary board members. This trend grew stronger for the company’s markets, market dynamics and industry trends: In all of the fields mentioned, board chairmen had significant informational advantages compared to ordinary board members.

Concerning risks and risk management, both CEOs and chairmen were on a comparable knowledge level, whereas ordinary board members stood apart. On the subject of technology and innovation, operations and manufacturing, an apparent chain of information could be perceived: CEOs know the most, then other officers, chairmen of the board and then ordinary board members. Again, research & development turned out to be the field with the biggest information asymmetry with both chairmen and ordinary board members indicating much less expertise than CEOs and other officers.

Figure 1: Satisfaction of board members by field of information



strategic, forward-looking fields, the results should ring warning bells: In the case of technology and innovation and the company’s operations and manufacturing, more than 50% have only rough knowledge or no knowledge at all. Moreover, regarding strategic research and development, more than 50% of board members said they were poorly informed.

Quality of board information

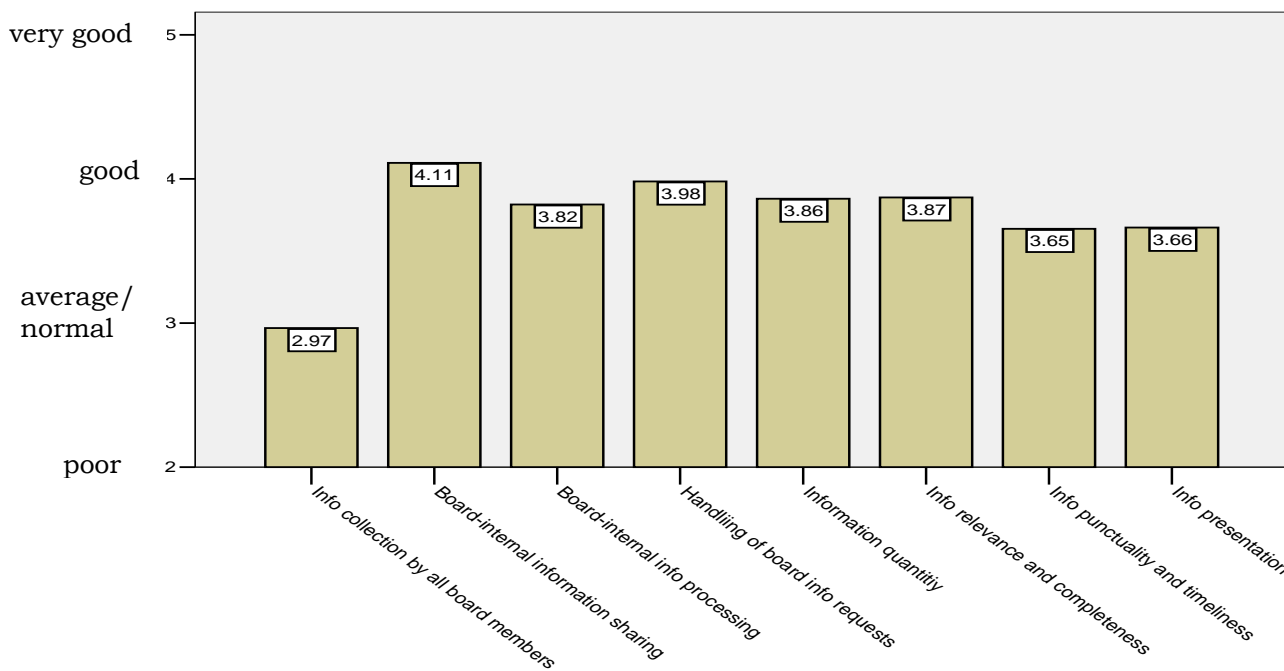
As assumed, about 40% of board members feel overloaded with information. This does not seem to be a problem of badly structured information. Regarding fields of information, the result is different: 63% stated the information supplied was too general and did not highlight specific key issues. Thus, most board members (>60%) would prefer to receive more information external to the company, e.g. about markets and competitors. 67% would prefer less detailed financial figures for their board work. Also, for nearly 80% the information provided is not forward-looking enough and deals too much with the past. Consequently, a large majority of 80% agreed that given current informational practices, board members could not get the “bigger picture” of the company.

Additional influences on informational levels

Despite an increase in demands and responsibilities, the overall board information systems continue to remain unchanged. 80% of board information systems have been developed by management and then simply adapted over time. Only in one-third of the cases did the board define any criteria for how it should be informed. One in every three respondents clearly indicated that their board information system definitely does not apply best practice standards.

There is a significant relationship between the time someone spends on the board and the overall level of information, specifically knowledge of markets. Long-term board members see more easily through hidden agendas and benefit from easier information sharing with colleagues. Thus, tenure has its advantages. Also, information exchange

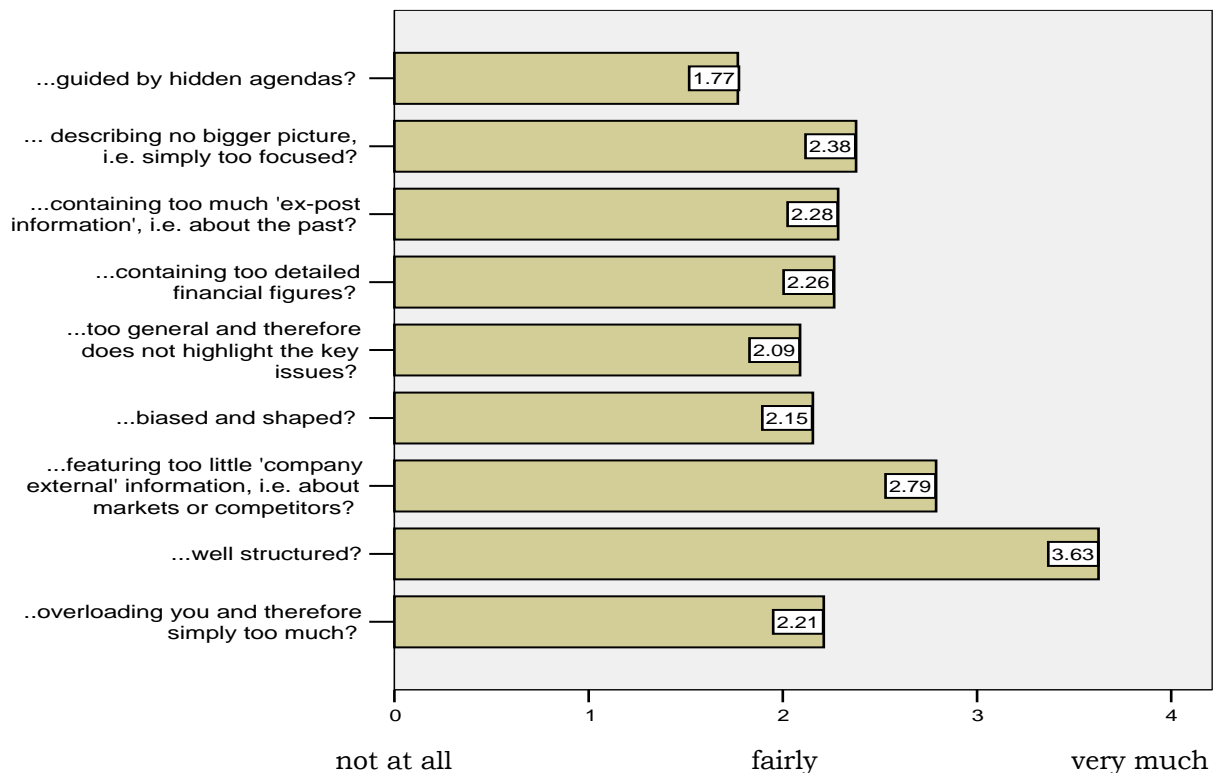
Figure 2: Satisfaction with board information characteristics



Board members generally do not suspect the information supplied to be guided by hidden agendas. Yet, 31% still felt that it was at least a little biased and shaped by management’s opinion; 37% even said the information supplied was fairly or more biased and shaped. Figure 2 presents the respective overview.

among colleagues improves over time. On the other hand, this means that new board members need initial advice and help and a considerable amount of time on the board to reach full efficiency. In creating high performance boards, it is, therefore, a primary task to bridge these information gaps as soon as possible.

Figure 3: Given the current practices of your company, is your board information...



Regular and more frequent board meetings provide board members with significantly better levels of information, especially regarding the core corporate governance fields of risks and risk management and subsidiaries' governance but also general market and industry knowledge. A clear relationship links strategic influence of the board and the number of meetings. The bottom line is the more frequent the board meets, the more value-adding potential it has.

Overall understanding of board roles and tasks

Board members, by and large, have embraced their dominant role of adding value at the upper echelon of organizations. Boards emphasize strategic influence beyond monitoring and supervising. Controlling financial performance and providing checks-and-balances for the CEO and management continue to be highly essential tasks. Mere representational tasks or VIP status without actually tackling real issues do not take

centre stage. However, they need a certain basic level of information, and this can only be achieved through a minimum number of board meetings.

Information sources and potential implications

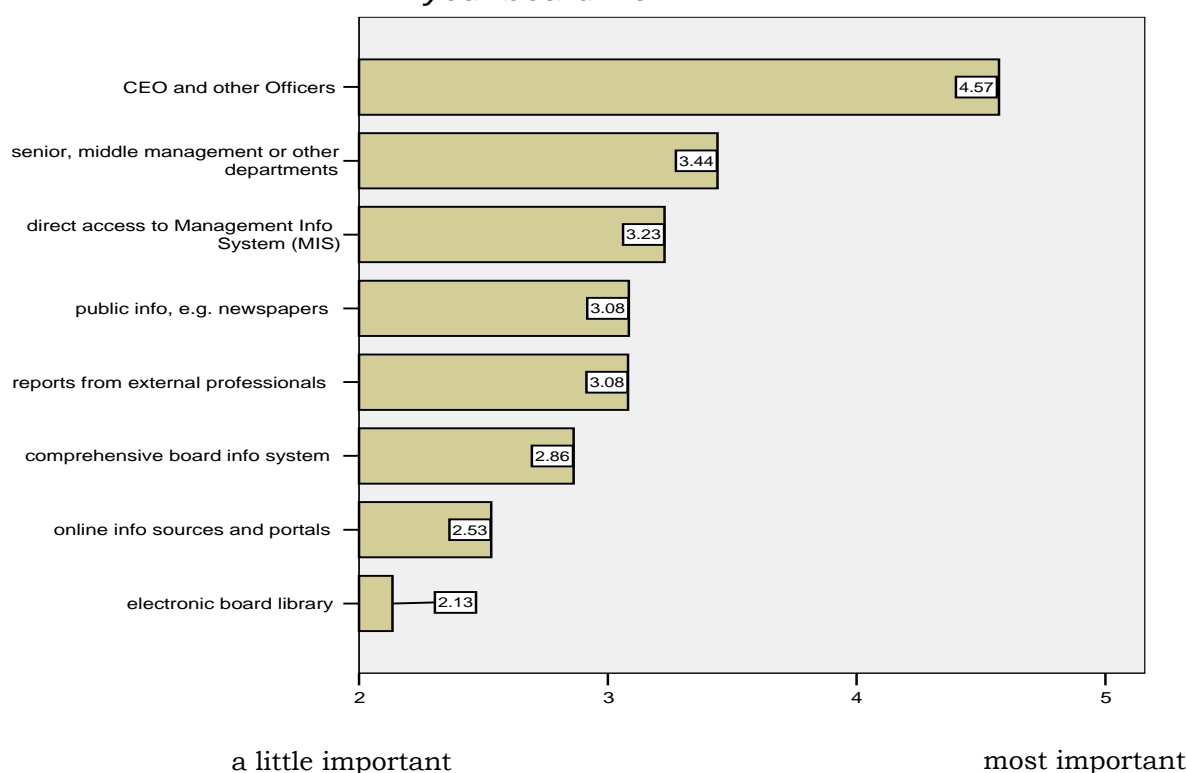
The results showed that there is considerable room for improvement regarding the information sources board members use for their daily work. For 54% of board members, more than 90% of the information for their board work came from the company; it was not sourced by themselves or externally.

Over 90% receive two-thirds of their relevant information for board meetings only from the company. Overall, board members mostly rely on the information that is sent to them, rather than looking for their own. Figure 4 depicts the results of the investigation of board members' most important information sources. For an overwhelming majority, the CEO and other officers represent the most

important information suppliers – far more important than any other source. Going directly to the company’s middle, department or line managers came in second, but did not have a significant lead compared to electronic information systems or other information sources. The board, therefore, should be aware that neutrality in content and information field selection is not guaranteed if the supervisors receive their information mainly from the body they are supervising, i.e. the top management.

management more intensively. As a result, almost half (46%) of the boards have succeeded in increasing the efficiency of board work and meetings. Board information significantly improved in almost 50% of cases. 60% of boards now exert more strategic and operative influence. Simultaneously, 56% of board members indicated that their tasks have become fundamentally more complex. For only 18%, scandals and regulations had no impact at all.

Figure 4: How important are the following information sources for your board work?



Impact of recent corporate governance scandals and new regulation

It is no surprise that the recent scandals and failures in corporate governance, along with the plethora of codes and regulatory adjustments, have had an impact on how boards work, perceive their role and tasks, and ensure they have the proper information to deliver. 43% indicated these scandals and regulatory adjustments fostered independence of boards from management. More than 50% of boards now monitor

Conclusion

The role of board members has changed since the wave of corporate scandals triggered new regulation. Much more far-reaching involvement of the board beyond monitoring and supervision altered the information demand fundamentally. However, board members clearly indicate they are not very well informed on several important issues. The key problems here are information fields that were most likely not considered core to the board's responsibilities in the "old days:" Board members lack information on markets and industry dynamics and competitors and therefore are unlikely to be able to, for example, evaluate the competitive position of the company. Other strategic holes in board information concern forward-looking fields such as research and development, which might be crucial to the company's future success. Though strategic involvement is considered a primary task of the board, the information supplied consists of mainly snapshots of the past and less on future outlooks. A large majority (80%) agreed that given the current informational practices they were not able to get the "bigger picture" of the company.

Next to the information content, the process of how board members are informed shows further room for improvement. Board members still tend to rely heavily on information supplied by management which strongly questions their independence and power within the company. Proactively defining clear criteria for board information systems is still a rarity. Position-wise a "chain of information" could be perceived, with the CEOs informed best, then board chairmen and finally ordinary board members. These results are also pointing towards the first groups receiving important information earlier than ordinary board members. This results in obvious information asymmetries within the board: Being an ordinary board member and newly appointed, means having significant difficulty in getting necessary information.

As board members see their role enhanced, new information demands regarding content, quality and tools must be met with supply. Information sharing and processing between management and the board and among the board members themselves remain unused sources for adding value. Here the chairman's relationship to other board members is often neglected. To create and maintain a high performance board, these informational gaps must be closed successfully.

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