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Is Your Board Ready For Peer Evaluations?

Gaining the benefits of performance evaluation without pointing fingers.

by Karen Bohn and Sandra Davis, Ph.D.

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Is Your Board Ready For Peer Evaluations?

by Karen Bohn and Sandra Davis, Ph.D.

While almost all public companies today conduct some form of board evaluation, individual evaluation of directors by their peers lags. A sound peer evaluation program can prove invaluable for board members, helping nurture their strengths, and further develop their oversight talents.

Imagine if companies shed all performance feedback mechanisms and instead solely used age and tenure to determine employee retention. Sounds far-fetched? Actually, those are precisely the criteria many boards use to re-elect their directors, as opposed to regularly evaluating and determining individual director performance.

Unlike with most employees, senior executives and CEOs, relatively few board directors are individually evaluated on performance. Now, though, a growing number of boards are reaching beyond typical (and often-perfunctory) check-the-box board evaluation surveys. More are taking a closer look at individual director performance through peer evaluations.

For boards with significant evaluation experience that are committed to collective improvement, peer evaluation often yields the most productive results of any type of review.

The 29th annual (2014) Spencer Stuart Board Index (SSBI) shows that annual evaluations of individual directors as well as the full board and its committees, now happens on 34 percent of boards, double the 17 percent of just five years ago.

We believe two critical factors are contributing to increased board interest in director peer evaluations. First, director turnover has substantially increased. In a 2015 NACD survey of 1,034 public company directors, 72 percent of respondents said their boards have appointed a new director, up from 41 percent three years ago. Greater director turnover means more directors unfamiliar with the knowledge and attributes of their peers. This requires added time and diligence for a board to exhibit "robust, effective social systems" that display "a virtuous cycle of respect, trust and candor," as Jeffrey A. Sonnenfeld described exemplary boards in his seminal 2002 *Harvard Business Review* article, "What Makes Great Boards Great."

Second, in our data-rich, time-scarce culture, boards are more keenly focused than ever on maximizing the contributions of directors and ensuring they perform as a strategic asset. The challenge, of course, is reaching peak board effectiveness and efficiency. Boards struggling to comply with even minimal full board evaluation standards may not be in a position to make that leap. For mature boards with significant evaluation experience that are committed to collective improvement, however, peer evaluations can often yield the most productive results of any type of review.

While more than 98 percent of the boards of public companies in the United States conduct some form of an annual board evaluation, according to the SSBI, considerably fewer boards currently conduct annual peer evaluations. What are the potential consequences of not individually evaluating your directors?

For starters, consider what your silence about individual director contributions might mean. In a recent PricewaterhouseCoopers survey of public company directors, 40 percent said at least one of their fellow directors should be replaced, up from 31 percent just three years ago. Less-tenured directors were more critical of their peers' performance than those with 10 or more years of experience. The survey

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respondents cited diminished director performance, unpreparedness for meetings and lack of expertise as the most common reasons for director removal.

A 2013 McKinsey survey of 772 directors, on improving board governance, illustrates why many directors may be frustrated with their peers. Just 34 percent of respondents agreed that their boards fully comprehend their companies' strategies, 22 percent said their boards knew how their firms created value, and only 16 percent indicated their boards understood the industry dynamics of their companies. Clearly, directors are seeking an individual accountability mechanism.

Who is in a better position to review your board, collectively and individually, than board members themselves? We have found that board leaders (especially the chair and head of the governance or nominating committees) appreciate peer evaluations because they take the onus off these leaders to be the sole source and bearers of individual director feedback. Instead, feedback with peer evaluations is based on the collective (and typically anonymous) input of other board members.

Peer evaluations are not right for all boards. Boards most ideally suited to peer evaluation are those that want to go deeper than the typical general board evaluation survey. Most importantly, they have worked together long enough to have rich feedback for each other.

A peer evaluation means that the board will need consensus on the process and tool(s) to be used. A peer evaluation is ready to implement when the board has a solid process, tools and plans for follow-up feedback in place. Practically speaking, it should not take board members much time to properly evaluate one another, particularly if the process and tools are sound, likely just one to two hours per director evaluated.

Boards less likely to conduct peer evaluations are often newer. They first need to "find their footing" and concentrate on their core requirements before delving into individual director performance. Additionally, boards unwilling to commit the time needed to review peer evaluation and put action plans in place for improvement are better off not even getting into the process. The greatest complaints we hear about board evaluation processes are those that end without using evaluation data for improvement.

When starting with peer evaluations, you want directors to first feel comfortable with the concept before attaching any significant consequences to it.

☐ ***Step 1: Determine objectives, format and criteria.*** Like any important board-led endeavor, peer evaluations should start with clear, mutually agreed-upon objectives among directors. In fact, the mere process of having your board collaboratively discuss and determine its peer evaluation objectives is often just as valuable as the reviews themselves. It frequently reveals sometimes unspoken expectations that directors have for each other. By talking about the process, even skeptics become a constructive part of the plan.

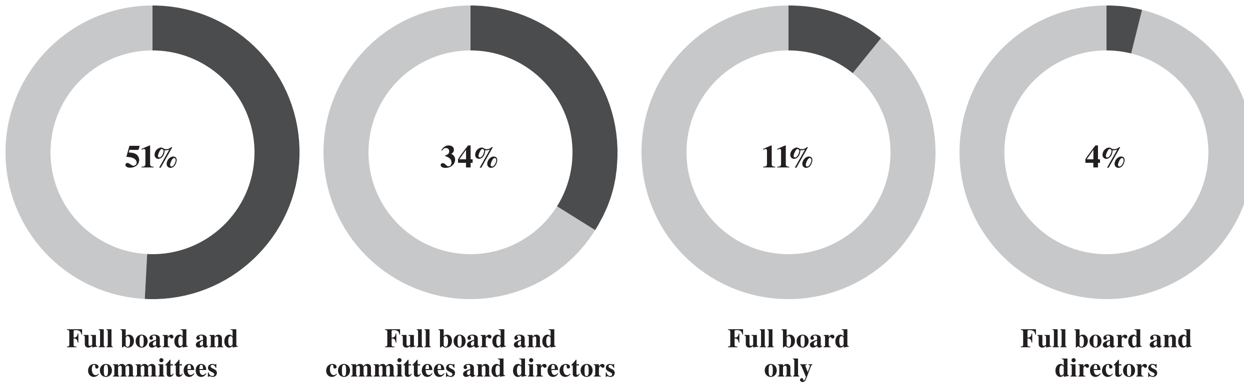
For a board choosing its first foray into peer evaluations, make it clear that the process is to be used for director development, only. While it may be tempting to use peer evaluations to factor into the re-nomination process, starting there could squash initial director interest in peer evaluation. When just starting with peer evaluations, you want directors to first feel comfortable with the concept before attaching any significant consequences to it. You may even wish to specify that the evaluation results will not be shared with members of the nominating committee and/or governance committee.

Each board needs to determine who will oversee and conduct the peer evaluation process, as well as deliver critical feedback. This varies depending on the board's size, interests and the time availability of its members. While the board chair may oversee the process on some boards, on others this role may be filled by the lead director or the chair of the nominating or governance committees. If the board chair and CEO are the same person, it is likely that the evaluation process will be led by someone other than the chair.

Determine how many directors are to be evalu-

Digging Deeper

Prevalence Of Board, Committee And Director Evaluation



Sample = 483 companies

Source: Spencer Stuart 2014 Board Index

ated each year, and the planned frequency of your evaluations, such as once every two or three years. If your board has eight or fewer members, you can likely do peer evaluations for each member in one year. With larger boards, such as 18 members, you may conduct only a certain number of peer evaluations per year, spread out over a multi-year period. For example, a board of 18 might do only six peer evaluations annually over three years. If there is significant turnover on your board within those three years, it will make year-to-year comparisons of the evaluations challenging.

Consider the value of engaging an external consultant to help oversee and manage the evaluation process, ensuring that it is both confidential and consequential. Besides likely having direct board advisory experience, an external consultant offers the dual advantages of discretion and objectivity, and likely access to the latest quantitative and/or qualitative assessment tools to facilitate the evaluation process.

Another decision point is choosing a suitable format for the process. Your evaluations could be based primarily on a written or online survey (with room for both quantitative and qualitative input), an interview with an external consultant, or a combination of both. There is no single "right" process for every board, although qualitative interviews add immeasurably to the impact of individual feedback.

☐ ***Step 2: Conducting your peer evaluation.*** Begin by making sure that all directors realize that the overarching purpose of the peer evaluation is to help members become more effective. Thus, this is not just about average scores or ratings, but about having a chance to provide evidence to support the ratings given. Numbers do not tell a complete story about what others think.

Conducting one-on-one interviews with directors during the peer evaluation allows them to "open up" far more than they might on paper. It also gives the interviewer the chance to ask follow-up questions, such as: "Can you give me an example?" "Help me understand what you mean by that." "What was the context of this decision?"

Whether conducted by phone or in-person, personal interviews are typically much more engaging, collegial and productive than a staid pen-and-paper (or trackpad-and-screen) process.

Interviews have the added advantage of being especially helpful during the private debrief. If the same person who conducted the director interviews also provides one-on-one feedback to the evaluated

The Right Director For The Job

Peer Evaluation Categories And Questions

When conducting peer evaluations, it is vital that your information-gathering questions be consistent, objective and professional, and asked in a collegial, constructive way. Potential subject categories and questions to include in a peer evaluation include:

☐ *Industry knowledge.* How familiar is this director with our particular company/industry? How does this director remain current about industry news?

☐ *Meeting preparation and participation.* Does this director consistently come to meetings well-prepared? Is it clear that this director has (and devotes) the time necessary to be an effective board member?

☐ *The strategic value of the director's discussion insights.* Does this director regularly initiate dialogue with significant strategic value, or is a key contributor to such discussions? Can you cite specific examples?

☐ *Ability to handle conflict respectfully.* How does this director deal with inevitable disagreements and/or conflict within the board?

☐ *Ability to listen and consider others' views.* Based on the director's comments and follow-up questions, is it clear this director has carefully listened to and weighed the input of others?

☐ *Ability to pose challenging questions.* Asking challenging high-quality questions is more difficult than it may seem. Does this director artfully pose good questions, and if so, how? How spot-on and valuable are the director's follow-up questions?

☐ *How this person adds value to the board.* What tangible and/or intangible qualities does this director add to the board? How is this board better off (or worse off) through this director's contributions?

☐ *Ideas for becoming more effective.* Does this director offer constructive and realistic ways for the board to improve itself and become more effective?

directors, it becomes much easier to convey not only what was said, but also the nuances of what was meant.

Bear in mind that the ultimate goal of feedback is to ensure that the recipient clearly understands and is able to act on the information given. The more insight you can provide during feedback, the better.

Qualitative interviews also allow directors to talk confidentially about the process. Sometimes a director has had a bad experience with peer evaluations or simply has a negative reaction to the process itself. Having a chance to hear directors' concerns and reassure them about confidentiality helps them be candid and helpful. Even though someone might have concerns about the process, we have found that most directors want to be part of a board where all members are effective and valued.

When presenting directors with their individual evaluation results, expect some of the recipients to be surprised by the feedback.

☐ ***Step 3: Using the results.*** As noted earlier, board members become disenchanted with evaluations (if not outright disgruntled) if the evaluations are not used to improve the board's capabilities. Ideally, peer evaluation results should be delivered promptly, and eventually folded into the full-board evaluation. Handled properly, the combination of peer and full board evaluations should enable a board to noticeably improve its performance within 12 to 18 months.

When presenting directors with their individual evaluation results, expect some of the recipients to be surprised by the feedback. After all, this could be the first time in years that this director has received any individual performance input. The recipient may also be a new director.

In one example, peer evaluations revealed that a director who had been recruited for his specific expertise limited his meeting comments to that particular area. That is what he thought his peers wanted. Instead, his evaluation showed that his fellow directors wanted to hear from him in many other areas—a recommendation he took to heart.

In another example, a director had expressed interest in serving on her board's finance committee, but her evaluation revealed her peers believed she lacked sufficient financial experience for this role. This prompted the board member to pursue outside learning opportunities in finance, in order to better prepare her to potentially serve on the finance committee, and most importantly gain her peers' support for this assignment.

Board members charged with delivering evaluation results should be prepared to help recipients understand this information and balance relative strengths and weaknesses. Peer evaluation also reinforces the board's strong interest in director development, up to and including recommendations for external learning opportunities.

Especially for new directors, it can be helpful for them to learn about and be referred to high-quality external development resources. Boards would be wise to encourage directors to individually pursue development opportunities, as well as help make such resources available for directors.

☐ ***Step 4: Evaluating and fine tuning your evaluations.*** When establishing your peer evaluation objectives, create a game plan for how you will evaluate the overall process. Often, this is a baked-in component if you engage an external board consultant. If you elect to conduct peer evaluations on your own, you may simply wish to have the full board weigh in on the process after the fact in a "roundtable" type format.

If peer evaluations reveal operational issues with the board, the members should discuss and prioritize items to be addressed in the coming year, with responsibility for follow-up designated to the governance committee. Then, the following year, the board can review its progress.

For the benefit of individual directors, the board should support their efforts to act on the recommendations received in their evaluations. For example, if most directors feel too removed from the work of the business, you might arrange for the board to visit various remote locations, or hold a board meeting at an off-site company location.

Peer evaluations are very useful for new and newer board members, especially those who have not served on a board before. It gives them a straightforward way to gain insight into the views and expectations of their peers. What's appropriate with this board? What's not? How often should I speak up in a board meeting? All of these (and more) are common and valid questions among new board members.

Scottish poet Robert Burns wrote how wonderful it would be "to see ourselves as others see us." While directors are typically already at the top of their game (so to speak), they also universally wish to grow and maximize their contributions. Peer evaluations not only help each director grow, but also help boards reach a higher state of overall excellence. ■

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