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Measuring the Performance of Corporate Boards

Duties and Responsibilities

The standards of conduct that directors must meet in fulfilling their responsibilities to their organizations are defined in the corporation's bylaws, in various statutes and regulations, and in court precedents. These duties can be summarized as:

- *Duty of care* – Directors must exercise diligence in making decisions as stewards of the corporation.
- *Duty of loyalty* – Directors must place the interests of the company above their own personal interests, avoiding conflict of interests.
- *Duty of obedience* – Directors must both obey the law and ensure that the company itself complies with the law.

The executive management of the corporation has the responsibility for the day to day management of the company, whereas the Board has a fiduciary duty to represent shareholders' interests in protecting and creating shareholder value, and to oversee the actions of management to ensure that the company is being managed to achieve long-term success.

In this regard, the Board assumes three core responsibilities:

1. Oversight of strategic direction & risk management thereof;
2. Ensuring fiscal and management accountability, including appointing the executive team, monitoring their performance, and succession planning;
3. Assuring the ethical, fair and equitable treatment of all stakeholders (including all classes of investors, minority shareholders, employees, and the communities most affected by the corporation's operations).

Implicit in these responsibilities is the self-management of the Board itself. Long gone are the days when the performance of the Board was the sole concern of the Chairman, acting in accordance with the wishes of the majority investors. The standard for corporate governance has, and continues to, escalate. Boards need more than statutory, regulatory, and other external measures of performance to keep pace with modern expectations.

Boards need to be continuously self-improving.

Continuous Improvement

For Boards to be continuously self-improving, they need both a process for self-improvement and a yardstick by which they can measure their improvement initiatives. Many forward-thinking Boards have organized themselves to focus on self-improvement and are implementing processes for continuous improvement. Unfortunately, despite a tremendous amount of literature, guidelines, and recommendations on specific practices for improved governance, there are few benchmarks that can be used to measuring progress.

Most of the self-assessment materials available for Boards are one-sided: over-emphasizing important characteristics such as director independence, or company disclosure practices, at the expense of other, equally critical but less topical attributes of Board performance, such as strategic direction and risk management. Incredibly, very little of the material available addresses the different needs of non-public Boards -- even though they represent the vast majority of corporations.

Our approach redresses those issues by design. It is based on a balanced scorecard framework, equally measuring each of the major dimensions of Board performance. It is available in both public and private company versions such that the scorecard can be self-applied by all corporate Boards. It also provides a consistent scoring mechanism that can be used by both companies and researchers to benchmark and compare Board performance across companies and to enable the longitudinal correlation of dimensional scores with corporate performance.

Scorecard Framework

Our framework is multidimensional, consisting of three dimensions along each of two major axes. The first major axis represents the core responsibilities of the Board and contains the familiar three dimensions of:

1. Strategic direction,
2. Fiduciary responsibility, and
3. Equitable accountability.

However, accurate key performance metrics in each of these dimensions require a context that measures the full scope of Board operation. This context is supplied by our second major axis that represents the scope of Board operation using systems theory (i.e. any system can be characterized by its inputs, its systems and structure, and its outputs). The three dimensions along this axis are:

1. Individual competency and Board composition ("inputs")
2. Board processes and committees ("systems and structure")
3. Outcome effectiveness ("outputs")

By measuring key performance indicators found at the intersection of these six dimensions, we have achieved a balanced scorecard using a reasonably minimal number of measurement points. In fact, both the private and public versions of the scorecard have approximately 50 metrics and require less than 20 minutes to evaluate.

The following figure illustrates the multi-dimensional structure of our framework:

Board Operations	Board Responsibilities: Strategic Direction	Fiduciary Responsibility	Equitable Accountability
Competency / Composition	KPIs	KPIs	KPIs
Processes / Committees	KPIs	KPIs	KPIs
Outcome Effectiveness	KPIs	KPIs	KPIs

To ensure that the scoring of each metric can be aggregated without skewing the resulting scorecard result, a consistent set of criteria is used to assign scores based on a 5-point process evaluation of each key performance indicator (KPI):

- The highest score (5 points) is assigned to the best practice recognized for that KPI;
- The lowest score (zero points) is assigned to the most common worst practice for that KPI;
- Intermediate scores are assigned to the practices that represent stages of process maturity between the worst to the best practice.

The selection of "best practice" for each KPI is based on the experience of The Lanigan Group and the University of Ottawa's Centre on Governance and has been guided by a comprehensive review of literature and research published to-date by legislative committees (congressional and royal commission), professional associations (legal, and accounting associations), industry associations (directors, chief executives), securities regulators, securities exchanges (blue ribbon committees), academic researchers, management consultants, and industry publications in Canada, the USA, the UK, and in Asia.

We have anticipated that, over time, the identification of best practice may change and that some KPIs may be dropped and others added as the result of evolving international experience and research into corporate governance. By using a consistent, process-based scoring mechanism and by using an enduring framework for the scorecard itself, these changes can be accommodated over time without invalidating the comparability of results obtained in prior uses of the scorecard.

OCRI

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About The Lanigan Group

Founded in 1998 by Paul Renaud, The Lanigan Group has developed a reputation for its high-impact executive consulting services to the technology industry in both the USA and Canada. The Lanigan Group is dedicated to helping technology companies implement sustainable innovation and business growth by improving strategic governance, business strategy, product strategy, customer value creation, and in assisting in business process and capability improvement.

More information regarding The Lanigan Group may be found at www.lanigangroup.ca.

About The University of Ottawa Centre on Governance

Located in the heart of the nation's capital, The University of Ottawa is one of Canada's top research universities and is unique in offering a comprehensive range of programs in both of Canada's official languages. The Centre on Governance is an interdisciplinary research and teaching unit at the University of Ottawa that was created to examine the changing patterns of organizational and social coordination. Launched in the Spring of 1998, the Centre brings together leading academics from different university faculties and a number of first-rate practitioners from the private, public and civic spheres. Focusing on research and educational programs like Corporate Governance, Innovation, E-Business, Distributed Governance and Social Learning, the Centre pursues solutions to governance issues that are consistent with guiding organizations through the challenges of today's socio-economy.

More information about the Centre on Governance may be found at http://www.governance.uottawa.ca.

About The Ottawa Centre for Research & Innovation

The Ottawa Centre for Research and Innovation (OCRI) is Ottawa's economic development corporation. OCRI is the rallying point to bring business, education and research together to create the winning economic conditions that allow Ottawa's technology companies to thrive locally and compete globally. At OCRI we promote sustainable economic development to maintain our high quality of life.

More information on OCRI may be found at www.ocri.ca, and more information on the Ottawa Region may be found at www.ottawaregion.com.