Rethinking 5 Common Boardroom Norms

Directors are laser focused on sound processes. But are some of the long-held assumptions about directors' processes past their expiration dates?

Dawn Zier sat down with three experienced board members to discuss whether (and why) boards should rethink the conventional wisdom around the role of their directors.

Participants

Betsy Atkins, board member at Wynn Resorts, SolarEdge, and Google Cloud

Anna Catalano, board member at HF Sinclair, Frontdoor, Ecovyst, and Hexion

Dave Goebel, board member at Wingstop Restaurants, Murphy USA, and iOR Partners and independent chairman of the board for Jack in the Box/Del Taco

Moderator

Dawn Zier, former CEO of Nutrisystem, director at Hain Celestial Group, Prestige Consumer Healthcare, and Acorns

1. 'Noses In, Fingers Out'

DAWN ZIER: We have all heard the phrase "noses in, fingers out" with respect to how directors should think and act. Given all that has transpired over the last four years, is this perhaps antiquated thinking, and should directors be leaning in a bit more?

ANNA CATALANO: I've been on boards for over 20 years, and the director role has changed a lot. Generally speaking, the phrase "noses in and fingers out" can still apply, but there are a lot of degrees to that. Directors certainly have the capability of diving in because we've all had years of executive experience. When there are situations where that's required—and there's been more of them lately—we should do it. But the default needs to be to go back up.

If you picture an eagle flying very high, it's able to dive down. But the first thing it does after it accomplishes its mission is to go right back up. From a governance standpoint, directors should default back to a higher altitude when those things that needed the deeper focus are done. Preserving the distinction between director and leadership roles is important.

BETSY ATKINS: It's fair to say that boards are more engaged now than they typically have been, and perhaps that's the result of going through the extreme COVID-19 situation, where we all had to rethink the way work gets done. However, the level of engagement required of directors is situational. If there is something very significant going on in the company—for example, an acquisition, divestiture, restructuring, major business disruption, or succession change—there is naturally going to be a much higher level of board input.

Also, with the advent of large language models, we will see an acceleration in the rate of business model change, which will also drive engagement. With that being said, "noses in and fingers out" is still a good mantra, with the board asking the thought-provoking questions that influence and challenge management's thinking.

DAVE GOEBEL: I don't think there's necessarily a list of macro topics that would suggest directors should be leaning in more. I think it can get very confusing when that happens. As new topics come across the transom, the CEO should bring those topics forward, and sometimes the board will need to go down the ladder a little bit. But for the most part, boards should stay out of the soup.

One exception to this is during a CEO transition. There's no question when a new CEO steps into the role that the board chair is going to lean in more, drive onboarding, and help coach until the training wheels are ready to come off.

2. Unanimous Votes

ZIER: Given the push for diverse perspectives in the boardroom, coupled with the complexities that corporations are facing, does it surprise you that unanimous consent and unanimous votes are still the norm?

ATKINS: It's a matter of litigation avoidance. If you vote "no," you go on the record and you create a vulnerability, a wedge, for an external class-action or derivative suit. That's why we see so much unity. If it's clear that alignment can't be reached during the lead-up discussions, most often the topic will get tabled before a vote takes place.

GOEBEL: Debate can and should take place in the boardroom and if someone has a dissenting point of view, it should be heard. What I don't want to see are pocket vetoes. Have the conversation, and if a director is not comfortable, they can abstain, or the board can decide not to move forward if they feel they need complete consensus. I see the importance of certain votes being unanimous, but I don't think all need to be.

CATALANO: A unanimous vote is an endpoint. It's hopefully a result of a very fulsome conversation before the vote that actually gives all directors a chance to voice their views. I've been involved in many situations where the initial dialogue has not been unanimous, but really good conversations take place, dissenting opinions are heard, the issues are worked through, and alignment is reached. We can disagree as directors, but at some point, a decision has to be made. And once that decision is made, we need to move forward with it in a unified fashion and support it. Boards should not be giving conflicting messages to management.

3. Shareholder Activism

ZIER: Many boards and management teams view shareholder activism as distracting and not necessarily maximizing value for all shareholders. Do you

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think this is a valid mindset? Or does constructive activism drive superior outcomes, and should boards be more welcoming?

GOEBEL: The best approach to avoiding an activist is, first and foremost, to stay ahead of them and be your own activist. Challenge yourself to ask: "If we were an activist looking in, where are our vulnerabilities? What things are we not paying enough attention to that we should?"

Secondly, never stiff-arm an activist. Have an open mind, and be willing to listen. We've seen situations where an activist can bring some fresh thinking that's not just short term or self-interest. But it's never fun, because it's always distracting. Sometimes there's value, and sometimes there's not.

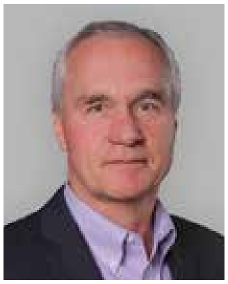
CATALANO: Generally speaking, the reason we're wary of activists is because they introduce ideas or timelines that boards and management teams are not comfortable with. I firmly believe that if an activist brings up a topic that the board hasn't already considered, you likely have the wrong group of people sitting around the table.

I've always been stunned at how much an activist knows about the business. They're outsiders, so they don't have all the context, but they know a lot. If you can engage with an activist around why they're coming in, walk them through the context of what they might be missing and why you may or may not want to pursue certain avenues, then that's a good start. You need to assess if their plan is to be constructive and add value to the long-term sustainability of the company or are they looking for an easy, short-term win. There's a big difference between those two positions.

One of the areas where activists often have success is in driving a change in board composition, especially if a board can be viewed as entrenched. Good boards are proactive in driving board refreshment and assessing any gaps they might have, long before an activist comes on the scene.

ATKINS: There's a continuum of activists, so it's important to know who you're speaking with.

Activists, as a general rule, tend to have a shorter-term time horizon. Some of them have very good ideas, while others are just looking for a quick way to pop the stock price—buybacks, for



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example, which might not be in the long-term best interest of the company.

There are also situations where activists can provide a needed mechanism for change that results in a healthy shake-up. An example of this is when a company is a long-time underperformer and the board fails to remove the CEO. There are many constructive activists, but there are also some abrasive and badly behaved activists who won't collaborate and aren't professional. Boards should always listen to their shareholders with an open mind. You can't refuse to do that just because they're labeled, but you need to do your homework to understand their playbook.

4. ESG and Diversity Initiatives

ZIER: ESG and diversity initiatives have been a focus in the boardroom over the past few years. Now, many corporations are facing pushback. How should boards be thinking through this as we move forward?

CATALANO: I grew up in the oil and gas industry, so I've been very familiar with environmental issues, even before ESG was a thing. Regardless of pushback or backlash, if it is the right thing to do for the business or for its people, then the board absolutely needs to make sure it's getting done—whether or not anyone's watching or measuring you.

Many boards have gotten caught up in "check the box" [with diversity]. Do we have a sustainability report? Are we measuring diversity? If you look at these things as an activity rather than a purpose for why you're doing something, it's a mistake. If a board is thinking that we may not need to do this anymore, then they've been doing it for the wrong reason.

GOEBEL: There will always be issues that are hot potatoes with proxy advisors and investors—often social or political in nature—and I always counsel the board to be thoughtful, introspective, and measured. Forget the acronyms and the labels for a moment and focus on what's underneath that. Having diverse thoughts and diverse opinions in the boardroom and within the leadership ranks will always be important.

We should ask ourselves: Did the pendulum swing too far, and how do we ensure that it doesn't swing too far back? I think investors and the like have every right to state their opinion and their preferences. But just like with any other topic, they should not try to force that right onto others. Instead, they should bring forward a balanced dialogue around "Here's what we think, and we'd ask you to open your mind and ask

The Hidden Costs of Disclosures

Because Betsy Atkins has spoken out on the increased number of required disclosures that companies have faced in recent years, we asked her to weigh in on the ramifications of these mandates.

ATKINS: People rarely go back and do the forensics around the costs of these requirements. It's sizable, and the culmination of all that we are required to do can impact profit margins considerably and reduce cash necessary for innovation and growth, especially for smaller companies.

When [the Sarbanes-Oxley Act] was put in place, the estimated cost of doing it was a modest $91,000 per company. The real costs turned out to be $4 million to $6 million, and IPOs dropped by 75%. Now, it's averaging around $2.8 million. That's a lot of money if you're a $100 million company making after-tax profits of $10 million. It's a 30% hit to profit that could have been invested in product or innovation to drive growth.

We had the same thing with [the Dodd-Frank Act] in 2008, and now we have this ratcheting up of regulations and reporting requirements that's further going to erode margins. The new SEC regulation on climate is estimated to cost $864,000 per company. At one of my companies, we've already spent close to $2 million on consultants. We're not even reporting yet, but we're $5 million to $6 million in.

This regulatory avalanche diverts so much time and resources away from the "business of the business," and nobody is speaking about it as a concern.

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yourself these important questions as to whether or not you should be leaning in the same direction." Organizations and companies should not be put in a situation where they feel everything is becoming a mandate.

ATKINS: What we really are looking for is diversity of thought and ideas, and I don't think it should just be based on gender or ethnicity. We need to expand the programmatic approach that focuses on some micro-identity segmentation algorithm and create a meritocracy that defines diversity more broadly.

For example, we should have more Gen Z- and Millennial-age cohorts in the boardroom. We should ask ourselves why we aren't bringing more international colleagues into the boardroom when most big companies do more than half of their business outside the United States. Where is the scrappy entrepreneur? The union member? The non-Ivy Leaguer? I don't care what their gender or ethnic background is, if directors are all from the same socioeconomic background, they're likely to think the same. Diversity has to be more broadly defined and should encompass many different experiences.

5. Director Feedback

ZIER: Boards tend to ensure their CEO and management teams go through a rigorous annual performance review process. Yet, on many boards, the annual board evaluation process is a fairly generalized survey where there is limited feedback on the individual directors. Should this change?

GOEBEL: The checkbox board evaluation process is something we need to leave behind. Good boards today are taking their evaluation process very seriously.

A process that I find to be effective is giving every director the opportunity to review all of their colleagues. The board chair or the chair of nominating/governance then aggregates that feedback and has a conversation with each director about what they do well and where they need to think about performing better.

Gone are the days of people sitting on boards that are not fully participative and adding value.

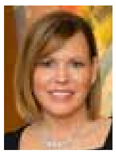
The board evaluation process should have a level of rigor to it similar to a management evaluation process.

ATKINS: Similar to Dave, I find that the traditional board survey doesn't add a lot of value because directors are careful about what they put in writing to avoid a smoking gun for a lawsuit. I believe the correct process is that the lead director, board chair, or governance chair should have a robust conversation with each board member to gather input on the performance of the board as a whole, the performance of the CEO, and the performance of individual directors.

CATALANO: Board evaluations should not be looked at as a separate activity. They should be part of overall governance where you assess board composition, skill sets, and gaps. We make a mistake when we bring people onto boards in allowing them to think that they can stay on in perpetuity until some artificial thing happens like a term or age limit is hit. One should stay on for as long as their skills are helpful to the organizational strategy and what that executive team needs in terms of advice. We need to do a much better job of setting that expectation.

Board evaluations need to be about the board in its entirety. Even if directors are evaluated individually, it should be done in the context of how they contribute as a group, not just as individuals. We should be asking: Do we have the right voices around the table? What are the things that each individual director is contributing to support the direction of the enterprise? What are the things we wish they would do more/less of? What new skills do we need?

The Directors Roundtable was hosted by



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