Feature

Evaluation and development of 'non-PLC' boards

David Archer argues that other boards can now benefit from the wealth of experience that exists on how to conduct effective PLC board evaluations and to get real change from the results.

There was a time when the language of the boardroom and board governance was a rarefied thing spoken by distant people who ran banks or other major corporations somewhere in the City. But today boards are all around us and more are being set up every week as new organisations are being created to deliver public services away from direct Whitehall control. Francis Maude has recently said that he wants to see one million public service workers being employed in Public Service Mutuals or other employee-owned organisations by 2015 and all of these require boards to govern their operations and to hold their management teams accountable to stakeholders. Then there are the Foundation Schools, Hospitals, Housing Associations which again need a well-functioning board to be effective. Charities have somewhat different governance rules, but a trustee of a charity that is delivering significant operational services to the public has many of the same responsibilities and concerns of a non-executive director (non-exec).

In this scenario, understanding what makes a board work well, how to measure board effectiveness and how to develop board performance becomes a necessity for large areas of our public service delivery landscape.

In a previous edition of *Governance*, my colleague Alex Cameron wrote about a framework for PLC board evaluation (based on the UK Corporate Governance Code) and how to get beyond a tick box approach in order to give board members real insight into what drives effective collaboration in the boardroom. In this article I want to look at what lessons this Code and its application might have for the evaluation and development of other boards.

Being 'not-for-profit' doesn't make you immune from boardroom problems

Failures of governance can happen in any organisation. The headlines over the last few months about the failings of the Co-op Group have posed many questions about the experience and capability of the chairman and members of that board. In a very different sector the so called 'Trojan Horse' report[1] into Birmingham schools talks of 'behaviours by governors and governing bodies that do not appear to be in the best interests of the schools which they should serve' and says 'there is still an issue of competence' for governors. It's easy to pin the blame for failure on a lack of individual competence and there has been lots of good retrospective analysis of fatal flaws in board structures[2] but the question has to be asked – why weren't stakeholders and indeed members aware of these failings long before.

These failures may ultimately point to a failure of external regulators to hold the boards of these institutions to account – but also to underlying failure of internal mechanisms for board self-assessment and improvement. And in much less extreme cases than these, how do members of a board know where their strengths and weaknesses lie – and how do the public to whom they are delivering their services know what plans the board has in place to address those issues?

How can the FRC governance code help?

Other frameworks exist for board evaluation, the NVCO produces a board self-appraisal toolkit[3] and the Charity Commission has some useful guidance on what makes an effective trustee board. But studying the FRC Code can bring some additional benefits. This Code has been honed over many years and its principles have evolved from painful lessons of past failures of PLC governance. Whilst this might not seem an auspicious place to start I think other boards can now benefit from the wealth of experience that exists on how to conduct effective PLC board evaluations and to get real change from the results.

At the heart of the FRC Code are the concepts of '*Comply or Explain*' and of *transparent external evaluation*. A board needn't follow the detail of each provision to the letter – but if it doesn't *comply* it must *explain* to its external evaluators and through them to its stakeholders how it meets the principle behind that provision in some other way. The board then needs to go through an external evaluation process on a three-year cycle and these explanations, along with board development priorities, are publicised to shareholders and customers via the annual report.

The discipline of regular and repeated external evaluation against a consistent framework is a benefit to any group that wants to improve its performance – and that applies to boards across charities, mutuals, and public bodies as much as it does to PLCs.

The principles of the FRC Code as applied to non-PLC boards

Leadership

- *The role of the board* – every board needs to be clear about its collective purpose, the leadership it brings and its responsibility for the long-term success of the organisation.

- *Division of responsibilities (Chair & CEO)* – there should be a clear division of responsibilities between the Chair's responsibility for the running of the board and the CEO's responsibility for the running of the organisation's business. No one individual should have unfettered powers of decision.

- *Non-executive members* – as members of a unitary board, non-execs should constructively challenge and help develop proposals on strategy. But the development of strategy is a collaborative effort between all members, executive and non-executive.

Effectiveness

- *Board composition and appointments* – there should be a formal, rigorous and transparent procedure for the appointment of new members of a board based on an analysis of the appropriate balance of skills, experience, independence and knowledge required for the board to carry out its duties. All board members should be subject to a regular reappointment process and maximum terms should be clearly defined.

- *Commitment* – all board members must be able to allocate sufficient time to discharge their responsibilities effectively.

- *Development and support* – all board members should receive induction training and should regularly update their skills and knowledge. And the board should be supplied in a timely manner with information in a format and style that members can understand.

- *Evaluation* – all boards should undertake a formal and rigorous annual evaluation of its own performance and that of its committees and individual members. The result of this should feed in to a development plan which is available for stakeholders to view.

Accountability

- *Financial and operational reporting* – a board should present a balanced and understandable assessment of the organisation's current position and future plans.

- *Risk management and internal control* – a board is collectively responsible for determining the nature and extent of the significant risks it is willing to take in achieving its strategic objectives.

Remuneration

- *Executive remuneration* – there should be a formal and transparent procedure for developing policy on executive remuneration and for fixing the remuneration packages of individual directors. A board is responsible for determining levels of remuneration sufficient to attract, retain and motivate executives of the quality required to run the organisation successfully.

Relations with stakeholders

- *Dialogue with stakeholders* – the board as a whole has responsibility for ensuring that a satisfactory dialogue with stakeholders takes place. And the board should use the AGM and annual report to communicate formally with stakeholders including details of the board's own evaluation and development plans.

The different challenges of 'non-PLC' boards

Although I've argued that there are a lot of similarities in the governance challenges faced by PLC and non-PLC boards and therefore the type of evaluation that would benefit them – there are some significant differences too.

- *Lack of clear accountabilities between board and executive team* – this is a complaint of many not-for-profit board members, particularly when it comes to accountability for the definition of strategy. The standard way PLC's have developed to deal with this dilemma (in the UK at least) is the unitary board structure with effective non-executive and executive membership – and an environment that encourages robust debate and collaboration across the boardroom.

- *Board members acting as representatives of different interests* – in a PLC board the members are united in a joint responsibility to safeguard all shareholders' interests. In other boards, members may not have such a clear common purpose. And in many public sector and Public Service Mutual boards there are members who are specifically elected to represent the interests of specific constituencies such as staff or parents on a board of school governors. This feeling of being a representative can block effective collaboration in the boardroom and reduce the collective decision-making capacity of a board.

- *Many non-financial targets* – this is one of the biggest differences in the priorities of these other boards compared to a PLC. Of course PLC's have to hit many competing targets but they can trade-off under performance in one area with over performance in another and as long as the sum comes out with a good profit the shareholders and the board are probably going to be happy. Collaborative leaders on not-for-profit boards have to juggle resources and strategy to satisfy a range of stakeholders each with different objectives and desires. It's a struggle to trade one target off against another without a common currency to compute the relative benefits.

- *Shortages of skills and resources* – the UK Code talks at length about the importance of getting the right skills on a board and right resources to support it. But for other boards outside the PLC arena getting the necessary skills and resources can be a major barrier to effective functioning particularly if this involves unpaid non-exec posts.

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Conclusion

The explosion in the number of boards tasked with overseeing the delivery of large components of public services calls for a new focus on board appraisal and development across these organisations. The principles within the Code can help provide a basis for this. The principles are well known to those with experience of PLC boards and with many of these individuals also serving on not-for-profit boards this gives a sound knowledge base to work from. A Code designed for PLC's can't be applied blindly to other organisations, but by explicitly addressing any differences from the PLC world (like those four points outlined in the previous section) and writing them into a terms of reference, the Code and its provision for external evaluation can be a very valuable development tool for any organisation.

[1] Report into allegations concerning Birmingham schools arising from the 'Trojan Horse' letter
https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/340526/HC_576_accessible_-.pdf

[2] Report of the Independent Governance Review of the Coop Group
http://www.co-operative.coop/PageFiles/989348879/Report_of_the_Independent_Governance_Review.pdf

[3] http://knowhownonprofit.org/studyzone/board-appraisal-toolkit

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