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The Anatomy of Board of Director Culture

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The Anatomy of Board of Director Culture

By Patrick R. Dailey

Culture matters more than before. Unless the right board culture is in place, nothing very special is likely to happen.

Talented directors sit shoulder to shoulder around a board table, razor-focused on their company's strategic imperatives guided by a superb Chairman at the helm, but unless the right board culture is in place, nothing very special is likely to happen.

Today, culture is a more critical determinant of board effectiveness than during the bygone era of ceremonial board service. Why? Because contemporary boards function as deliberative, working teams rather than simply preside. The cultural ground rules which dictate director attention, behavior, risk appetite, and decision-making processes are simply more critical to a board's effectiveness because boards are more *at work* than before.

It is a mistake to fail to understand the strength and focus of your board's culture. Constructive culture foster constructive working dynamics; dysfunctional cultures are no longer benign annoyances; they are often destructive to shareholder value as can be seen from the impact of boards including AIG, News Corp., Hewlett-Packard, Yahoo, and recently Avon.

The aim of this article is to explain board culture in simple language. The article describes the implications of board culture on director selection, board dynamics, decision-making, and board development. It is argued that increased knowledge of culture along with greater attention and better tools for board evaluation/renewal will improve board dynamics and decision processes. Ultimately, shareholders benefit from more astute, unified board leadership.

Culture defined

While culture most often operates in the background, it is unmistakably present. It is the body of accumulated beliefs, assumptions, attitudes, values, and experiences of a board's directors that collectively manifest in decorum, protocol, norms, prevailing decision processes, and the concentration of power and privilege. Culture functions as an ever present rudder that sorts issues, priorities, and can exert profound influence over individual behavior.

Culture can provide *lift* as well as cause *drag* on board effectiveness and director satisfaction. Cultural rules can be gleaned from rituals, protocols, rules, physical layout, as well as organizational stories that are often filled with cultural messaging. Culture teaches the dos and the don'ts and can rise up to penalize those who fail to abide by its norms and unwritten rules.

Colloquially, culture is "*how we do things around here.*"

Why focus on board culture?

Culture is the building block of group behavior.

Cultures have been shown to have a direct impact on the performance and competitiveness of businesses. Early on, the impact of culture on sustainable corporate performance was brought forward by Deal and Kennedy in their important book, *Corporate Cultures* [1982]. Daniel Denison made the irrefutable connection between culture and financial outcomes in *Corporate Culture and Organizational Effectiveness* [1997]. David Nadler in *Building Better Boards* [2006] offered a compelling view that *board culture* remains an underappreciated factor in the effectiveness of boards providing strategic guidance and fulfilling their fiduciary responsibilities. Many companies reference culture as the key ingredient to building long-term shareholder value. In particular, GE states that culture begins with its board to shape vision, set the tone for work and interaction, drive learning and change, and open doors to volunteerism and philanthropy. And recently, Ram Charan has spoken about *indecisive cultures*, which are corrected not through SEC regulatory actions and structural best practices solutions but through cultural norms that engender intellectual honesty, robust dialogue, and feedback within boards to guide management teams. Charan offers powerful prescriptions regarding the increasing importance of board culture as a tool for enhanced board effectiveness.

> Increased knowledge of culture along with greater attention and better tools for board evaluation/renewal will improve board dynamics and decision processes.

Cultures teach. Cultures are self-reinforcing. Lessons are conveyed in topics ranging from crucial matters including values, decision rules, norms, work styles and practices down to informal matters of seemingly little real importance. Newly-appointed directors assimilate into a prevailing culture by deducing the board's norms, symbols, formality, assertiveness, director approachability, and the strength of the inner circle.

From this jumping off point, new directors "learn the ropes" of acceptable behavior whether they have been brought in as complementary members or change agents. And the cycle begins anew with these new directors learning and abiding by the culture, practicing the norms in their board service, and then modeling the culture to newly-appointed directors that come onto the board over time.

Cultures punish. Cultures are self-defending. They are not benign. Within boards, the inner circle is often the keeper of board culture. Violations of the unwritten and often unspoken cultural norms can result in being removed from the channel of communications, marginalized, and cutoff. Directors always have a vote but they may lose their voice or credibility as a result of transgression. Some boards put violators in the penalty box and directors earn their way back to full board membership. Other boards don't allow recovery. Marginalized members would be prudent to move on. It is prudent to be a good student of board culture.

Cultures are resistant to change. Resistant cultures are a force to be reckoned with as boards chart new heights for professionalism and governance. Navigating change requires a politically adroit Chair who perceives the need for change and has the courage to pursue a change agenda. This change agenda begins with a board's understanding of its current culture - which aspects provide *lift*; which aspects cause *drag* on the board's effectiveness. Then, the change agenda can be charted as the Chair facilitates consensus among the board about gaps that need closing, and the agreed-to tactics for change.

The message from a wide array of distinguished experts is consistent and clear. Understand culture. Abide by its rules.

Elements of board culture

Social and regulatory pressures on boards for fundamental change are substantial and well chronicled. Boards are transitioning from well-intentioned support *clubs* for a company's Chairman and Chief Executive Officer to astute review panels composed of independent professionals headed by a non-executive Chairman who more and more believe the CEO works for them. Directors serve for a handful of *primary* reasons including:

- Opportunity to shape a company's future and enable a CEO as his/her coach and advisor.
- Personal learning and ongoing professional preparation
- Serving community interests and furthering corporate social responsibility
- Holding an honorable and responsible role.

Talented women and men are also more and more aware of the burden and downsides of board service including:

- Exposure to scrutinous second guessing, personal liability, and reputational damage
- Low potential for making a measurable impact on a company's future

- Exaggerated work load and time demands acknowledged with rather meager remuneration
- Problematic dynamics among directors that divert attention and bruise feelings.

> Understanding culture, abiding by its rules, and striving to shape and harness board culture leads to positive reputation and financial outcomes.

These inducements and obstacles, taken together, make a compelling case for cultural fit to be a prominent issue during director selection when skills, experience, temperament, and candidate expectations are assessed. And, culture is an influence throughout a director's ongoing service as dynamics, strategic work focus and compatibility matters enable, or disable, constructive deliberation and decision making. When the dynamics function constructively, the *magic* of board participation is realized; in contrast, when the dynamics are allowed to deconstruct and derail, board service becomes a burden.
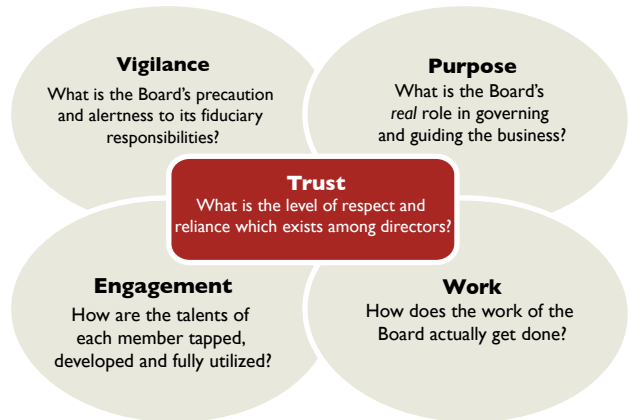
Figure 1. Board of Directors Culture Model®

Figure 1 presents the five primary factors of board culture - *how we do things on this board.* This model resulted from in-depth interviews and discussions with public and private board members and board chairs about board leadership, board work, the board's inner circle, plus decision influences and processes. These five factors summarize the most pivotal matters that directors consider when explaining *'what it feels like to serve on this board'*. These matters directly link to board effectiveness and director satisfaction.

Purpose. *Purpose* is the glue that binds directors in common pursuit. Their commitment to a long-term vision is a unifying force. It provides a sturdy foundation for decisions, evaluating achievements, and dealing with setbacks along the way. Purpose often becomes an inspiration factor that negates

Contemporary best practices expect directors to be double checkers: perform deep dives on management analysis and bring independently collected information to the table.

directional disagreements and serves as a rallying force for high performance. Clear purpose leaves no doubt regarding a board's fiduciary responsibilities - conflicting interests and other uncertainties that could confound and detour board focus and deliberation are removed.

Culture conveys the long-term intentions for the business and the intensity of commitment to achieve the vision.

Work. Decisions are the work products of boards. Culture largely dictates the way work gets divvied up, the hours required, the way that coordination and integration of work among individual directors occurs as well as among committees. While every director values an equal voice and vote, dynamics emerge around those who more heavily influence certain decisions and other directors who contribute and still others who withdraw. A characteristic work atmosphere results from the balance between harmony and conflict; collaboration and competition; full versus limited participation.

Sound board leadership is required to gather and sort through information provided by management and arriving from other channels. Leadership is also required to subdue director competition, bring disagreement into the open for constructive debate, and formulate sound decisions, which align with the agreed-to purpose all within an acceptable time frame.

Culture conveys the ground rules for the way board work is conducted - leadership style, decision processes, influencers, and intensity.

Vigilance. Ceremonial boards have been criticized for *just go-*

ing through the motions. The cultural rules for these boards prescribed this style of behavior and deemed it proper service. Inquisitive behavior, inquiry beyond that provided by management, and digging deep into stress test analyses and proposals presented by management was <u>not</u> expected. The culture was largely to approve management proposals.

Contemporary best practices exhort directors to be more vigilant. Perhaps these practices create expectations that directors be *double checkers* - perform deep dives on management analysis and bring independently collected information and analysis to the table. Business judgment standards are evolving to require greater expertise and deeper scrutiny.

Directors may also be expected to be sentinels. Sentinels *stake* out on the periphery of markets, product boundaries, or technologies where they read the faint signals of disruption or opportunity and bring this information to the company so strategy can be shaped and/or crises can be deftly handled or averted.

Contemporary directors must live comfortably with discomfort. Being vigilant in some ways means being always on the lookout for unraveling strategies and faltering operational pursuits, which might materially impact the enterprise. Arguably, *discomfort* differentiates board dynamics from operating unit dynamics. Effective boards embrace discomfort as a key raison d'être. The ineffective ones deny or insulate themselves from discomfort or succumb to negativism and chronic suspicion. So the culture of *effective* boards must encourage certain norms, beliefs, and behaviors regarding vigilance that may be deemed dysfunctional in operating organizations. Regrettably if mismanaged, these norms, beliefs and behaviors regarding vigilance that become dysfunctional elements within a board, thus giving rise to chronic negativism and second guessing management decisions.

Culture conveys how deep directors must dig - how alert they must be personally, and how rigorous their inspection is expected to be.

Board composition is important as directors are expected to bring special expertise that match the company's core competencies.

Engagement. Engagement is the *grease* that engages directors with their colleagues in collaborative service.

Today, boardrooms are places where each director must arrive prepped, prepared, and ready to contribute. This is even more challenging for newly-appointed directors because the learning curve is steep and the assimilation resources are often scarce. Board composition is of increasing importance as directors are expected to bring superb general business skills, cognitive, and temperament competencies which fit the needs of the board now and in the anticipated future. Nominating committees search for board candidates who can rapidly ramp and have immediate impact. These committees test for tem-

perament and *fit* that can be realized for directors who are complementary to the culture as well as those expected to be agents of change. Boards are becoming more diverse and international in their composition, which brings added challenges along with clear benefits.

Expectations are high. Directors expect competency, preparation, and contribution from their peers. Some seek safe haven while most seek full utilization, an equal voice at the table, and continuing education. All are sensitive to being marginalized.

Culture conveys the ways and means for directors to find their way into the center of the board coalition to fully contribute versus being isolated on its periphery.

Directors are more and more expected to be a *professional expert*, which is a level beyond the historic standard of *prudent professional*.

Trust. Board service is personal. The first issue many directors grapple with is not the strategy of the business; it is the personal risk level they face. Director trust is rarely discussed but always top of mind.
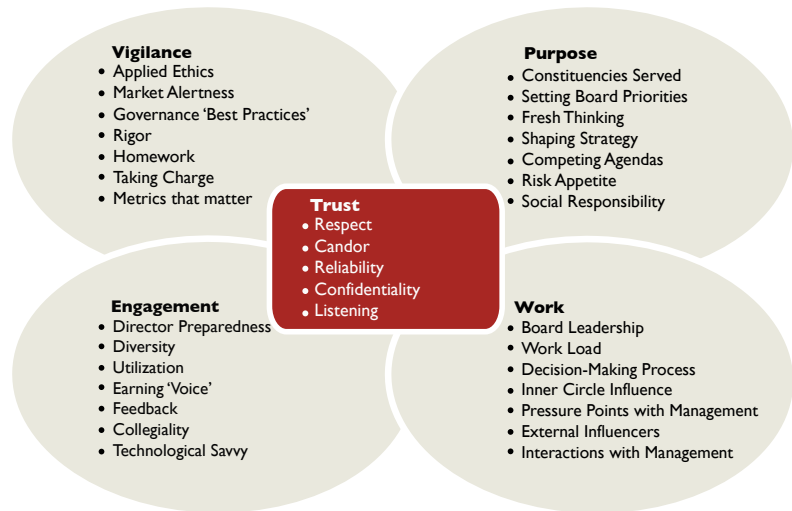
Decision-making requires directors to rely upon peers for full disclosure, accuracy, and candor. Without trust, mutual influence does not emerge, reliability is a chronic concern, and the board never matures beyond individual contributors brought together by a powerful Chairman for tacit approval of management's recommendations. The board deconstructs into a procedural body that fails to innovate lead, or serve shareholders particularly well.

With a solid foundation of trust, problematic ripple effects caused by misunderstanding or disagreement fail to dent or derail decision processes. Candor emerges. Interpersonal risking taking occurs. Constructive conflict plays out. Innovation happens. Shareholders are well served.

Culture conveys the standards for trust. Culture conveys the penalties for breaches, also.

Within each of the five factors are di-

Figure 2. Dimensions of Board Culture®

Vigilance
- Applied Ethics
- Market Alertness
- Governance 'Best Practices'
- Rigor
- Homework
- Taking Charge
- Metrics that matter

Purpose
- Constituencies Served
- Setting Board Priorities
- Fresh Thinking
- Shaping Strategy
- Competing Agendas
- Risk Appetite
- Social Responsibility

Trust
- Respect
- Candor
- Reliability
- Confidentiality
- Listening

Engagement
- Director Preparedness
- Diversity
- Utilization
- Earning 'Voice'
- Feedback
- Collegiality
- Technological Savvy

Work
- Board Leadership
- Work Load
- Decision-Making Process
- Inner Circle Influence
- Pressure Points with Management
- External Influencers
- Interactions with Management

mensions that provide further detail about each factor. These dimensions reflect matters that are prominently discussed by directors and Chairs as areas of heightened concern for the effectiveness of board process and the satisfaction and retention of directors. Each dimension is behaviorally defined and discussed in depth but due to space limitations, this further discussion could not be included in this article.

Problems with culture

Too Strong cultures. Strong cultures are canonized in *operating* organizations. Strength refers to the intensity, sanctity, and depth that members of a group honor and abide by its norms, values, rules and rituals. Those famous companies identified by Deal and Kennedy and other cultural historians were built around obsessively strong cultures. Tight, uncompromising, assertive norms and behaviors were deployed against objectives for strategy implementation, maintaining alignment, and staying the course. Strong cultures do function as control devices to set the tone, coordinate work, guide operational decision-making, and oft times function as a surrogate for actual supervisory direction. Evidence is conclusive that strong operating cultures out-pace, out-hustle, and out-last their competition. In contrast, weak cultures are liabilities that boards and operating executives attempt to remediate.

But, there is a *dark side* to strong cultures. Directors should take note regarding their own boardroom dynamics to detect cultures that are *too strong*. These include:
- Reduced capacity for innovative thinking: *change is difficult to muster.*
- Sanctions against those who challenge the status quo: *probative inquiry is unappreciated.*
- Reliance upon a charismatic leader: *participative decision-making fails to materialize.*
- Evangelical belief in the organization's norms, practices, and destiny. *External threats are disbelieved and discounted.*

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Weak cultures. Uncertainty is at the core of any group with a weak culture. Weak board cultures often begin with an unclear purpose or direction, which engenders cliques and conflicted interests among directors, which lead to demoralizing missteps and fatiguing resets. These are not agile groups; these are confused groups with a limited sense of identity

or direction---groups that are not held strongly together by norms, values, mission, vision, or *battle-tested* experience. These are distrustful environments where cliques or a marquee director may hijack the board for self-interested agendas over or around a withdrawn Chairman. The board is unable to repudiate strong-arm tactics or rise up collectively for corrective action or renewal. Board *drama* may be played out in the open but more likely, behind the scenes. Nonetheless, political finger pointing is practiced; self-protective actions abound. Weak boards do make decisions but these are often decisions that result from deferral to *strong-arm* influencers on the board or external influencers.

Disconnected cultures. These cultures preach but fail to practice. Demonstrated behavior and choices made are inconsistent with stated values, philosophy and the mission. Resulting from the 'disconnect', these cultures fail to set a clear tone; they have little or no moral authority. Directors may be oblivious to the inconsistency or deny it has impact or relevance to other stakeholder groups. Boards earning this reputation are viewed suspiciously and director reputations can be tarnished.

Stale cultures. Curiosity and learning flattens out over time for any group - boards included. Status quo creeps in and the board slips into autopilot - perhaps, even high performing autopilot for a while. Over-reliance upon long-standing lessons of experience; overconfidence; and complacency can unconsciously render a board blind to threats or opportunities and rather mechanical in its inquiry and vigilance. There is

Let's review today's feedback from social media updates!

Boards need ways to re-examine their current perspectives and deficiencies, embark on closing schisms and performance gaps... to renew, boards must learn.

nothing in the culture that shakes things up a bit. Collectively, the board may continue to offer valuable historical perspective and wisdom but the effectiveness of directors as sentinels and change leaders may diminish. When the board gets stale, the board's field of vision narrows, and alertness diminishes, maybe even their zeal; enterprise risk elevates.

> The Board leader is most often the catalyst for self-examination. The Chair may skillfully nudge the board toward self-examination.

Boards need periodic renewal

Boards like other groups need ways to re-examine their current perspectives and deficiencies, embark on closing schisms and performance gaps, and reinvigorate their spirit - to renew, boards must learn. And, contemporary boards simply must learn more and learn faster.

Board learning is a group activity - it should be conducted face-to-face. Board learning is distinct from individual directors attending a board or committee educational event sponsored by a university or professional association - these are important for enhancing individual competency but are not substitutes for group learning. The essential ingredients for renewing a board include:

Catalytic leadership from the Chairman or inner circle. The leader is most often the catalyst for self-examination. The Chair may skillfully nudge the board toward self-examination. Generally, it is constructive when the leader is able to de-emphasize the power and influence differentials, which inherently exist on most every board and lead collaboratively.

Discovery. Confidential director surveys supplemented with in-depth interviews of directors by an independent board advisor are a constructive approach for discovery and critical self-examination. A diagnostic survey allows directors to confidentially voice their opinions. The scope of discovery taps director perception of board purpose, work process, director engagement, and vigilance. Boards can learn the strengths and vulnerabilities of their unique culture through the lens of the board culture model presented in Figure 2.

Candid discussion. Facilitator-led discussion of summary reports and summarized interview information reveals healthy, functional areas as well as the more extreme areas of board culture that might need enhancement or corrective action. Group discussion of summary feedback puts issues on the table regarding expectations, which operate within the five board culture factors. Summary feedback reports reveal gaps between current behavioral and decision-making practices [i.e., *is now*] and director beliefs about requirements for effective future culture [i.e., *should be*]. The differences between

'is now' and 'should be' perceptions stimulate discussion and re-calibration.

Trust. A safe-to-say environment enables candor and interpersonal risk taking.

Change agenda. As a result of robust and candid discussion, boards find consensus on the issues they want to tackle. Intensity emerges around the change agenda. Sound implementation will put mechanisms in place to achieve *should be* goals. Persistent attention to new behaviors, norms, and practices will consolidate the cultural change agenda and allow change to *stick*.

A Chairman leads a board through renewal----but renewal does not last forever. Over time, the board again can benefit from renewal and the astute Chairman nudges the board to repeat the process.

Concluding comments: Building the board you need

Realistically, every Chairman can aspire to build a strong coalition of talented and committed directors to guide management and serve the interests of long-term shareowners. Directors can expect to be part of a constructive and professional coalition, which periodically convenes in noble and conscientious service to shareholders and to the management team they shape, guide and monitor. Board culture reflects and reinforces the ever-present DNA of your board---to foster healthy boardroom dynamics, or alternatively, to allow dysfunctional dynamics to disrupt and retard board processes and disillusion exceptional directors.

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Recognizing the impact that board culture plays in attracting talented board candidates and a board's decision-making process is of growing importance to Chairmen as boards step-up to increasing workloads, increasing director independence, and accountability with sharper edges than ever before. The Board Culture model defines the dimensions and provides descriptive language for directors to use in exploring and understanding the impactful elements of board dynamics---some which are visible; others which are cloaked. Diagnostic work using culture surveys, board development interviews, and other board evaluation tools reveal what works and what does not work for your board. From this diagnostic work, a change agenda takes shape, which is intended to make your board more functional and attractive. In summary, the board you want and need has an underlying culture that moves…

Perfunctory Cordiality towards...... *Genuine Trust and Mutual Reliance*
Directors rely upon directors. Boardroom candor stimulates interpersonal risk-taking, and prudent risk-taking leads to both protection and innovation. With the ever-present concerns about liability and threats to personal reputation, boardroom trust is the *primary element* of healthy culture.

Competing Agendas towards...... *Collective Purpose*
The board knows its destination. Thoughtful deliberation has joined together the board, analytically and emotionally, in the durable pursuit of long term vision. The board's role in engaging and guiding operating management and managing risk is clear. The board accepts and fully understands its fiduciary responsibilities to shareowners.

Respectful Acquiescence towards...... *Consensual Decision-making*
Boards make decisions. Analytic and decision-making disciplines are in place; which taps expertise, experience and wisdom among directors, executive management, and professional advisors. While the board listens broadly and intently, attempts by external influencers to lobby or sway board decisions are repudiated. Board-level decision-making is the sole province of the board, not that of management, not external influencers, not just the inner circle.

Dutiful Attendance towards...... *Active Engagement*
Directors care. Deeply skilled directors arrive well prepared, and willing to work together to contribute. Chairman and inner circle sets a tone of collaboration and collegiality, which translates into director engagement and high performance. Directors honorably serve. Their board responsibilities are personal responsibilities.

Passive Monitoring towards..... *Proactive Vigilance*
Directors are alert. The culture you need is one that sets norms for directors to be alert and proactive in their awareness of emerging opportunity or threats. *First movers* win share and market dominance. *First protectors* survive and aggressively protect core assets and capabilities. Both capabilities help companies get to the future before their competitors.

About the author

Dr. Patrick R. Dailey is a founder of Board Quest, LLC, a board of director consultancy. Patrick has held senior level Human Resources positions in Fortune 100 firms…all undergoing significant strategic and cultural change. Dr. Dailey has worked in the technology sector for Hewlett-Packard and Lucent Technologies; consumer products for PepsiCo and Herbalife; chemicals and pharmaceuticals UK-based The BOC Group; and consulting for Korn/Ferry International and Chicago Change Partners, with the firm's founder, Dr. Charles Bishop. Patrick serves on the Board of the National Association of Corporate Directors-Atlanta Chapter. He also serves as a director for EIAbroad. He received a Ph.D. in Industrial and Organizational Psychology from the University of Houston, Texas, U.S.A.

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