blenheim partners
Executive Search & Board Advisory

MGSM
MACQUARIE UNIVERSITY
GRADUATE SCHOOL OF MANAGEMENT

The Challenges of Attaining Growth:

The Blenheim & MGSM Insight Series

Authors: Dr. Brett Wright, Mr Gregory W. Robinson & Professor Charles Areni

"Superhuman effort isn't worth a damn unless it achieves results"

Sir Ernest Shackleton

Chapter 2

The "Professional" Director: Multiple Agendas and Flawed Incentives

"The day we went to career politicians, it became a problem, and the same applies to Directors."

Directors can have the wrong motives and incentives for joining a Board in the first place. This makes it difficult to get the best out of them to support and drive growth in Australian companies. This may be the case with this new breed of younger Directors, many of whom have no or limited executive experience.

Chapter 2: The "Professional" Director: Multiple Agendas and Flawed Incentives

"No crime is so great as daring to excel"

Sir Winston Churchill

It is readily acknowledged as one Director said that ***"the gene pool of NEDs in Australia is not that deep".*** Perhaps this is the reason that has led to participants feeling that a new ***"professional class"*** of Directors are being appointed to Boards. The view was that this was occurring for all the wrong reasons. Directors fitting this profile were characterised as:

1. Lacking C-suite experience;
2. Lacking experience generally;
3. Appointed based on narrow, ***"demographic"*** notions of Board diversity; and,
4. Generally younger and less experienced than Board members have traditionally been.

A recent article in the Australian Financial Review titled ***"40 the new 60 for ASX Boards"***[16], supported the age trend, highlighting the younger and sometimes less experienced Director shift that is occurring. The article stated that the number of ASX 200 Directors under the age of 50 had doubled in the last 5 years.

One participant captured all of this and more in the following:

"There is a lack of C-level experience in the Boardroom. I am seeing the development of the professional young NED, and question what they necessarily bring to the table. Do they have industry experience? No or limited. Do they have C-level experience? No or limited. Do they have P&L experience? Perhaps. Have they had leadership experience of a large organisation? No or limited. Have they faced the challenges of reaching a particular set of numbers and managing the stakeholders? No. I am surprised by the lack of experienced C-level depth in most Australian Boardrooms."

Some participants even suggested that the drive for gender diversity might be contributing to a new class of young female professional Directors, represented on multiple Boards as a way of meeting implicit or explicit quotas.

However, it is broader than just gender diversity being the driver, as both men and women represent this emerging class of younger Directors. One participant was generally surprised with this development, ***"There is this professional Board member thing that I have not seen much evidence of in North America, or Europe even … this is the first time I've encountered this rather young group of people who don't have, for the large part, CEO level experience … find themselves in this role and they need multiple Board seats to fund an income."***

Since many of these new professional Directors may need the money and must sit on multiple Boards to make ends meet, perhaps they can't afford to do anything controversial that might lead to an incident where they might put in jeopardy their Board role or, worse still, future roles. This results in over-concern with personal reputation and risk aversion when it comes to pursuing growth opportunities.

"Directors lend their reputation to the Board and to the company. But there's more to be gained by taking less risk than by taking more risk, and this is when the issue becomes a concern, and that is their risk orientation. They have very little risk orientation because there's very little upside for them. The company significantly outperforms versus just performs well. I'm not sure whether they gain any more from that."

"I see some Board members view as a high priority compliance and their own personal risk more than other agendas."

The following highlights how this negativity might translate to restricting growth opportunities within companies:

"Business means risk, but calculated risk. We have become the greatest nanny state in the world. We defer decisions, we defer risk, and we do not support the bold. You sometimes wonder if we were presented the task of building the Sydney Harbour Bridge today would the risk committee allow it to pass. We are being hampered by governance and risk avoidance instead of risk acceptance."

"We aren't betting the farm, and yet we over examine the risk. Reputational concerns are really starting to hold back opportunities. Taking on the Board is not easy as Board members tend to hunt in packs so therefore bring them along the journey."

"You need to take risk to get success. You cannot create a culture of encouragement and empowerment if leaders and executive teams cannot make mistakes. "This whole issue is captured in the following quote: "Where as if you've ……… got three Boards on $150k and got a chance of an extra committee? How independent are they going to be when they are hanging on wanting to be on the Audit and Compliance Committee because it's another $50k?"

In this sense, Directorships may be becoming income-generating activities in and of themselves or as one participant put it, ***"seen as a nice little earner",*** being pursued by people with little or no executive experience. Supporting this view was the comment ***"certain members of the Board have "relied" upon Board fees and are risk averse – it drives the wrong behaviour".***

This was the basis for the quote ***"the day we went to career politicians, it became a problem, and the same applies to Directors".***

For this generation of Directors, aspiration may be more about earning a safe income as opposed to what participants felt was the more noble and appropriate purpose of making the organisation great and being rewarded on that basis.

These views could be contrasted with the characteristics and motives of ***"good"*** Directors. ***"My experience in the US is the … Board members tend to be professional bankers or investors who have been around and done some pretty exotic things and made enough money where they didn't need to work."***

Some Directors even went so far to as suggest that the personal wealth of potential Directors might be used as a ***"litmus test"*** for determining their motivations for joining a Board. From this perspective, only Directors with considerable personal wealth gained from their experiences as company executives, investors and the like would qualify as having the right incentives, the courage to take risks, and the capacity to handle the consequences of failure.

"One Chairman said to me just the other day, 'One of the things I look for when I look at Directors, is do they need the money, because if they really need the money, it's not the right job for them'."

Another put it far more bluntly with the gambling analogy: ***"Back self-interest, it's always trying"!***

But there were some dissenting views on whether all Board Directors should have executive experience, and whether this new breed of younger, professional Directors is necessarily a bad thing. For example it would be likely that the younger Director would be more knowledgeable of digital and social media than would be the older more traditional Director. Other counterarguments were couched in terms of the need for diversity, in viewpoints and gender, as seen in the quotes below from two participants.

"… if you're only going to have rich people as Directors…..the gene pool that you have available to actually then sit as Directors of the company doesn't reflect the communities that they service… So if you're running a Unilever and you've only got rich people sitting on the Board then no one has got any understanding of what it's like when you can't afford to buy a bar of soap."

"I think there's still a lot more of the former (traditional Directors) who made their money ……. and I think that's a break on diversity that's potentially a problem" (if the existing or traditional Director model is maintained).

Comment

The emergence of the ***"younger professional Director"*** was raised on enough occasions by participants to signal that it is a potential concern regarding the conscious or unconscious constraints in decision-making processes. These constraints will tend to be around willingness to embrace risk. If this is the case then risk aversion and conservatism may become a growing force on Boards as the ***"younger professional Director"*** numbers grow. The concern will be that inherently growth and risk are business partners in themselves and if the risk appetite of a Board is significantly impaired, so too will be the growth prospects considered and approved. This can very well result in investments in new ventures, M&A and R&D being reduced, pared back, deferred or not approved at all, leading to reduced competitiveness and retardation in the growth of Australian companies. The end result may very well be a question as to the ongoing viability of some of these Australian companies.

This does not mean that new or emerging Directors should be excluded from Boards. Far from it because how else do they become a Director to start their career. There is room for ***"learners"*** on Boards and Boards should have the capacity to bring on such a person young or otherwise. What is essential is that the appropriate due diligence is performed on the potential new Board members to ascertain drivers and motivations of the individual to join the Board. Such a process will reduce many of the risks and concerns highlighted above.