

# Directors & Boards

A close-up portrait of an elderly man with white hair, wearing a dark blue pinstriped suit, white shirt, and dark tie. He is smiling slightly and looking towards the camera. The background is softly blurred, showing what appears to be a window and some indoor plants.

THOUGHT LEADERSHIP IN GOVERNANCE SINCE 1972

SECOND QUARTER 2008

## Board tenure: How long is too long?

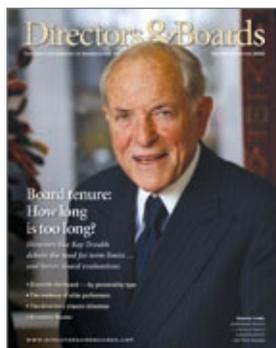
*Directors like Ray Troubh  
debate the need for term limits ...  
and better board evaluations*

- Diversify the board — by personality type
- The makeup of elite performers
- The director's classic dilemma
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**Raymond Troubh**,  
professional director  
— a strong presence  
in boardrooms for  
over three decades

## COVER STORY



# Director term limits come up for review

*Our panel participants tackle some thorny topics concerning board tenure: How long before directors get stale or too complacent? Are term limits a necessity or a hindrance to board performance? How useful (or useless) are director evaluations? What should be done about ‘duds’ on the board? ... and other dynamics that determine a board’s effectiveness.*

**T**HE DIRECTOR AS POTTED PLANT? Not a welcome image in thinking about effective board governance — i.e., a director of longstanding service who reaches an inflection point, drifting from engaged oversight into listless and lifeless complacency. Yet it is just such a possibility that provided impetus for the following discussion about the pros and cons of board tenure and term limits.

The panelists represent an inclusive spectrum: CEO, board member, academic, investor, and legal. Moderating the discussion is **Charles Elson**, Edgar S. Woolard Jr. Chair in Corporate Governance and director of the Weinberg Center for Corporate Governance at the University of Delaware. He is also a member of the *Directors & Boards* editorial advisory board. A bio note on each of the participants:

— **Sanjai Bhagat**, professor of finance at the Leeds School of Business, University of Colorado at Boulder, whose “empirical work on director independence, director ownership, and director equity is unsurpassed,” says Elson.

— **Kenneth Daly**, president and CEO of the National Association of Corporate Directors since 2007; he was a KPMG partner from 1978 to 2005 when he retired to assume the role of executive director of KPMG’s Audit Committee Institute.

— **Lawrence Dickinson**, corporate secretary of Barclays PLC



**‘The difficulty that I found with board evaluations has been the reluctance to pull the trigger on a nonperforming director.’**

— *Charles Elson*

and “*the corporate governance person*,” as Elson says of him, at the major British banking institution; he offers a singular perspective on board tenure policies and director independence based on the U.K. governance model.

— **Jon Hanson**, founder and chairman of the Hampshire Real Estate Companies, whose board service includes lead director at Prudential Insurance and chairman of HealthSouth Corp. following the leadership crisis that the health care provider faced with the ouster of former CEO Richard Scrusby.

— **Ann McLaughlin Korologos**, former U.S. Secretary of Labor in the Reagan administration, is chairman of the RAND Corporation and a veteran director currently serving on the boards of Kellogg Corp., AMR Corp. and American Airlines, Host Marriott Corp., and Vulcan Materials Co.

— **Robert P. May**, chief executive officer of energy company Calpine Corp., who has served in leadership positions with several companies over a 30-year career, including Charter Communications, Cablevision Systems, and HealthSouth (serving as an interim CEO and

on the board with Jon Hanson and Charles Elson during its turnaround).

— **John W. Noble**, vice chancellor of the Delaware Court of Chancery since November 2000; he practiced law with the firm Parkowski, Noble & Guerke P.A. in Dover, Del., before

joining the Court of Chancery.

— **Raymond Troubh**, a professional director who has served with distinction on some 30 boards over a three-decade career in the boardroom, including chairing the board of Enron Corp. in its post-bankruptcy workout; his current directorships include Diamond Offshore Drilling Inc., Gentiva Health Services Inc., General American Investors Co., and Triarc Companies.

— **Ann Yerger**, executive director of the Council of Institutional Investors since 2005 (and with the organization since 1996); the Council includes more than 140 public, corporate, and union pension funds managing over \$3 trillion in assets.

The roundtable was held in October 2007 at the University of Delaware's Alfred Lerner College of Business. This is the third of the governance center's roundtables that *Directors & Boards* has featured in our pages. Previous panels addressed "Whose Company Is It Anyway?" in 2000, a roundtable that launched the center eight years ago, and "Handling Dissent in the Boardroom" in 2004.

Excerpts from the debate on board tenure follow.

— James Kristie

**Charles Elson:** Historically, once you got elected to a board, you were there for the duration as long as you wanted to stay. The only thing that would knock you off would be an age limit. A lot of boards did have age limits, typically between 68 and 72. For boards that didn't, you could stay as long as you wished, which meant people could be there for 20 years or more.

Starting a number of years ago, questions began to be raised as to whether this was a good idea. The arguments in favor of long-term directors were that they have experience, that it is hard to replace them, and that once you have been there a long time you have a good sense of the company and can be a better monitor. The argument against long tenure was the inclination to get stale in the job and that, after 10 years or so, there were concerns — raised by CalPERS, in particular — that you were not viewed as independent of management, i.e., lengthy tenure compromised your independence.

Another view, one a bit in between, was not that you were no longer independent after 10 years but that you got too comfortable. It becomes hard to innovate against yourself. The more accustomed you are to the procedures and approaches

the company takes to various issues, the more you lose your ability to be critical of what management is doing and to be aware of problems that develop, and you become a less active monitor than you should be.

All this started the call for term limits. The National Association of Corporate Directors, in its 1996 *Report on Director Professionalism*, was the first document to issue an affirmative call for some kind of term limit. The NACD suggested a term limit of between 10 and 15 years, after which the board would say to a director, "Thanks, but you need to do something else."

No one could stay on the board beyond 15 years. There was an alternative view that was proposed at the time that term limits really aren't necessary and that the key is having a director evaluation process. If everyone is evaluated on an annual basis, you can allow someone to stay as long as they are productive.

Let's have each of you state your initial opinion on the subject. Ray, lead us off on this notion of the term limit as a good thing or bad thing — a necessity or a hindrance to board performance.



**'We have got to do something about the evaluation processes. They have to be better. They have to be tougher.'**

— Raymond Troubh

you're going to stay." That's very awkward. You're better off having some automatic test that applies to everybody across the board.

**Ann McLaughlin Korologos:** I would be on the side of saying term limits are neither necessary nor a hindrance as long as you start with a nomination process of finding the best people, accompanied by an evaluation and renomination process. In today's culture, with policies on age limits, resignation on job loss, and other factors affecting individuals, it's a little more acceptable to go on and off boards without staying for 20 years. Twelve to 15 years is more often the reality. But even

then there are exceptions extended by nominating committees and boards.

I took a look at several of my own boards. Since I joined the board of Kellogg Co. over 17 years ago, we've had 19 people join the board and 21 leave. The average tenure is 8.8 years, and we've had five CEOs during that time. At Host Hotels, where I went on the board 15 years ago, six directors joined, six left, the average tenure is 10 years, and we've had three CEOs. At AMR and American Airlines, where I have been on the board for 15 years, we've had 10 new directors, 13 departed, a nine-year average tenure for the board, and three CEOs. On many of my boards I am what would be thought of as a seasoned director. I stay on a board if I can add value. I've also voluntarily left six or seven boards.

**Jon Hanson:** I am for having some term limit — 10 to 12 years. Directors do get stale. They do stop contributing. At HealthSouth we have instituted a 12-year term limit. The board is permitted under circumstances to invite someone to be extended beyond that. In general, after 10 or 12 years you probably contributed as much as you're going to contribute.

But, with 70 being the new 50, I am not supportive of an age limit. I can give a good example where an age limit would have forced two directors off at a bad time. Prudential was converting from a mutual company to a publicly traded corporation, which is a very difficult process. We needed our two senior directors, Paul Volcker and Roy Vagelos, who just retired as CEO of Merck, to help us get through this. Both had turned 70. The board decided to extend their terms. That was a good example to me why you should not go off just because of age.

**Robert May:** I will take more of a management perspective. Like Ray, I am on balance in favor of term limits, but my balance is more like 55-45. Certainly, the argument for the board staying fresh and bringing new thinking into the board is the most compelling reason for why we should have term limits. But it does create additional work for the CEO, and some added complexity. It can be a couple-year process for the CEO to take on the additional work of getting used to a new director and getting a new director up to speed on the business. That takes time and takes away from the business. Those are some negatives, but overall I would be on the side of having term limits with the flexibility to modify them when circumstances warrant.

And, as Ann's information shows, the average shelf life of

CEOs these days is fairly brief. The notion of the board getting cozy with the CEO would be the rare case.

**Elson:** Ken, since you published that report on director professionalism, give us the NACD perspective.

**Kenneth Daly:** Let me share several themes from our research. While I initially thought that this was not that interesting an issue, the more I got into it, the more I realized that is not the case. In fact, in our 2007 survey, 41 percent of respondents consider the issue "critical," and another 47 percent consider it "important." So nine out of 10 have it high on their radar screen. Boards use a variety of ways to keep board membership fresh. Term limits are actually the least popular. Only 8.3 percent of the respondents approve of term limits. An evaluation process is clearly the most popular, with 55 percent saying that is the way to go.

Typical tenure of directors is getting shorter — 7.6 years. I would have never guessed that without looking at the data. Nearly half the boards (49 percent) replaced board members in the past year — and of those, 46 percent replaced more than one member. That's something you do not hear a lot about. Diversity of age is becoming an interesting new byword. It used to be that the preponderance of directors were 62-plus. But as I go around to different sessions where directors are present, I find that there are a lot of directors now in their 40s and 50s, which historically we have not seen. Another thing that plays into this is that directors are serving on fewer boards. In fact, 39 percent of respondents to our 2007 survey said their board has a policy restricting the number of boards the CEO can serve on, and 86 percent said the board *should* have such a policy!

The key to effective boards is to get the right skill set on the board. However that happens — and it ought to happen through nominating committee selection — the priority is getting the right skills on the board.

**Lawrence Dickinson:** The problem with rigidly imposed term limits is that they fail to take into account the different circumstances facing each board and the different characteristics and composition of boards from company to company. Having said that, in the U.K. we do have a system whereby under the Combined Code on Corporate Governance — which listed companies have to comply with or explain why they don't comply — nine years is the presumption of independence.



**'If a director got through the nomination process, he or she is usually not a total dud. If that is so, then shame on the rest of the board.'**

— Ann McLaughlin Korologos

You are allowed to keep directors on the board after nine years, but you have to justify why they remain independent.

At Barclays, where we have done quite a bit of board refreshing over the last few years, we have one nonexecutive director who has served nine years and who continues to add a lot of value. Good quality nonexecutive directors are hard to come by. If you have one who is still adding value you do not want to lose him or her because of some rigidly imposed limit. I do not think there is necessarily a link between tenure and independence. Quality nonexecutive directors live on their reputations, and will not let their independence fall away simply because they have been on the board a long time. In fact, for many individuals, the length of stay can affect their independence positively.

I do, however, think there is an issue about staleness that underlies the need for board refreshment. High-quality board evaluation procedures are an absolute key to making sure that the board is looking at its own processes and the quality of its own membership rigorously every year.

**Ann Yerger:** From an investor's prospective, the Council of Institutional Investors does not endorse mandatory retirement ages or tenure limits on directors. We have discussed both issues. We examined them well over five years ago — pre-Enron, pre-scandals — when there was more of a perception that some directors were potted plants and that certain individuals were sticking around perhaps longer than they needed to. But our

policies committee rejected the concept of the Council taking any kind of position on these issues. We agreed they were overly prescriptive and that what was most important was that companies and boards have robust independent nominating processes and independent nominating committees, and very robust director evaluations.

The board needs to change and adapt according to what the needs are for the organization. Who is to say what skill set is necessary or most appropriate for a board at any given time? It is the board's responsibility to think that through and make determinations about skills, backgrounds, and diversity — not just race and gender but also age. That evaluation is essential. That is why ultimately we did not take a position on the issue, and the market has shown that shareowners at large are not that supportive of these ideas. Every year there are a couple of shareowner proposals that call on companies to adopt either tenure limits or mandatory retirement ages, and they tend to not do very well — sometimes getting under 5 percent of the votes. It is interesting that the investor perspective is so different. Maybe it's because the dynamics in the boardroom have changed so significantly.

**Sanjai Bhagat:** I would not support a rigid board tenure restriction or age restriction. What I could support would be robust evaluation by the rest of the board of a member's tenure or age. If someone is adding value after 12 or 15 years, there is no reason to ask them to step off if they want to continue to

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serve. Data show that there is almost no evidence that companies doing poorly are those that have boards with ages on the high side or where tenure is on the high side. If anything, the data would suggest the opposite — that these companies are doing better. (*Ed. note:* See exhibit on page 23 showing about 1,500 U.S. companies sorted into four groups on the basis of their industry-adjusted return on assets.)

Board tenure restriction may even enhance independence of boards. But then the question is: Is independence such a good thing for shareholders? There is very strong evidence that companies that have more independent directors systematically have underperformed their peers. That is a well-documented result for almost all publicly listed U.S. corporations. So, if you are thinking about board tenure in the context of greater independence, that is probably not the right case to make. Maybe the right reason is the need for newer ideas, which come from new board members.

**Hon. John Noble:** When I think of independence, particularly in the context of a shareholder suit, I worry about how cozy the director has become with the chief executive officer and those who control the company in a *de facto* sense if not through pure voting power. I do not know that, as a legal matter, I would ever say a director has lost his independence simply because of time in grade. But where that director has other relationships with the company — as a supplier or other business connection — a long tenure would suggest that perhaps one of the reasons he is being kept around is that he has become compliant and willing to go along.

On the other hand, the lawyer in me forces me to say that although by numbers the panelists are in favor of term limits, let's recognize that being around for a while gives you the experience, the knowledge, the status — the *gravitas* — that makes you an effective counterweight to a CEO who may be running amuck. And there are a lot of little things that one picks up by having been on the board for a while, such as who you can trust and how you get the information that you need, which is important because so much of what contributes to how well a director does his or her job is how that information is provided to them.

### Optimal timing

**Elson:** All good points from the panel. Now that we know everyone's starting position, let's dig in a bit on some of the hard questions. What is the optimal time for board service? What is that optimal point where you know enough to be an

effective counterweight, but you begin to get stale and become too complacent and too cozy? Is it five years? Eight years? Ten years? There has to be a number somewhere in that realm. It's true that no individual is the same, that everyone reacts differently in different situations. There are times when someone who has been on a board for 20 years is more engaged and active than someone who has been on a board eight years. The problem is, how do you know?

**Yerger:** As investors, we don't know how a director is performing. We can't get behind boardroom doors. We like to try sometimes, but we can't. It is tough getting rid of underperforming employees. But that's the board's duty. We are counting on the directors to do the right things, and to make the hard decisions.



**'I'm more in favor of term limits because of the freshness issue, not as a way to deal with performance issues.'**

— Robert May

**Dickinson:** What we do at Barclays is that the chairman and I will meet with our top 20 institutional shareholders at least once a year to talk about purely corporate governance issues. We talk about the composition of the board and our views on the independence of the nonexecutive directors. That helps to get some shareholder feedback. Under U.K. regulations, directors who have served more than nine years have to be re-elected by the shareholders every year. So at our annual shareholder meeting, it goes for a vote. I fully accept that it is difficult for shareholders to know how specific individuals are performing, but we know as a company we have to justify to our shareholders that it is worthwhile keeping individuals on the board. That is quite a useful discipline to have in place for directors who have served over nine years.

**Elson:** You should have evaluations to remove the dud if you can. The difficulty that I found with board evaluations has been the reluctance to pull the trigger on a nonperforming director. When the NACD report was in development, there was a conflict within the commission between those for evaluation and those for term limits. My argument at the time was not against evaluation, but relying *too heavily* on evaluations. Theoretically, evaluations are a terrific tool, but practically speaking it is hard, even with an evaluation, to move someone off the board. The term limit and/or age limit, as unpleasant and draconian as it may be, does make it a lot easier to rotate someone off because you don't have to embarrass them through a poor evaluation or have to say to someone, "You are at an age where you are just not contributing anymore." No one wants to say that to someone. Boards aren't theoretical institutions. They are collections of people — people you get to know and work with. So I was one of those on the NACD commission who favored the term limit. I thought 15 years was plenty of time to contribute your optimal value to the corporation.

### Evaluations — all they could be?

**Troubh:** Evaluations are becoming better, but my experience on a lot of boards is that evaluations are ineffective overall. They don't go deep enough.

**Daly:** Some of the board evaluations I've seen don't even rise to the level of awful. Essentially, they don't even evaluate the board member. Because of collegiality, you don't want to go to somebody and say, "Look, you're no longer productive. You're a dud." So what happens is you evaluate the whole board. I don't know what good that does for figuring out problems with particular individuals.

**Korologos:** I am trying to look at the practical side of the problem that we are supposed to be solving with term limits and I am having trouble seeing the problem solved. Keep in mind that there is a natural progression of board turnover — through retirements, resignations, adding people with new skill sets, all of those reasons. This accomplishes much of what term limits would do. With the addition of one, two, three new people every year or every other year, the board is getting fresh insights.

I'm a big proponent of stepping up to the plate to do evaluations. When you are standing outside the room for your evaluation, as happens with the Kellogg board, your self-examination does

more than any evaluation by any other board member. That's point one. Second, I have been on boards where we have asked people to leave. The evaluation process itself as a process does good. It's not an either/or — you stay on or get off. We have had directors who had issues that affected their performance which the evaluation process was used to remedy.

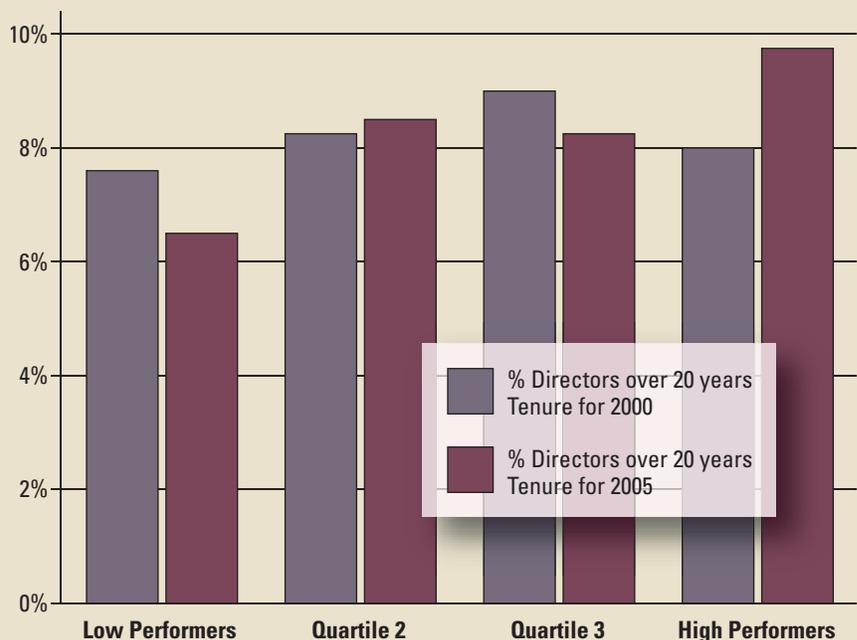
**Elson:** You're right. There is an informal term limit just through natural processes. The concern is when you have that 20-year person on the board who is not always there, who doesn't recognize that he is going stale and not contributing anymore. Does it make sense to have a hard and fast rule to take care of that kind of outlier on the board?

**Troubh:** Because it's so difficult to get rid of board members, what you tend to do is ignore the laggards. With 10, 12, 15 people on the board, the feeling is you can afford to have a 10 percent or 20 percent error rate. You know who the good people are, the cream always rises to the top, and those are the ones whose opinions you listen to.

As Ken Daly said, the present effectiveness of the evaluation system is terrible. But that's our fault. We get these standardized forms — 10 or 12 pages, and you check, check, check and off it goes to an independent agency to be counted. They come back and say, "The board is OK on these six points." Then you

## Board tenure and corporate performance

1,500 U.S. companies sorted into four groups on the basis of their industry-adjusted return on assets



Source: Sanjai Bhagat, University of Colorado at Boulder

destroy the documents because you are worried about lawsuits — you don't want anyone to see what you really wrote. There are a few comments, which are anonymous. You may say, "He's a jerk," but you don't sign it.

We have got to do something about the evaluation processes. They have to be better. They have to be tougher. That's going to take a long while.

**Daly:** The companies that have the most aggressive evaluations might also have the biggest shredders. You can imagine how difficult it is to do a thorough evaluation when you are holding in your hand something that could create quite a mushroom cloud.

**Korologos:** I think of evaluations as a tool for board effectiveness as opposed to a report card about how you did that semester. As a tool, you are going to use it for whatever purposes. It's up to a nominating or governance committee or an executive session of the board to use the results of that tool well.

**Dickinson:** We actually do disclose some of the outcomes of the evaluation process, but not individual director evaluations. If we say, "Well, the board decided that it wasn't spending sufficient time on such and such topic," we would be prepared to disclose that, to give some sense of what happened as a result of the evaluation process.

### When a dud is a dud

**Elson:** Let's consider this: Sometimes a dud may look like a dud but might be much better than you think. I know of a situation where a board thought they had a dud who should not have been there. Then the company ran into a crisis, and the dud started to talk. And the dud, as it turned out, was a lot smarter than the other directors thought. In fact, he was extremely smart, and became vice chairman of the board because he helped them out of the problem.

The point is that the evaluation of the dud was incorrect. Sometimes people get called duds because they are dissenters. They express a different opinion, which can lead to them getting ganged up on.

**Korologos:** If a director got through the nomination process, he or she is usually not a total dud, or a dud that has potential to be "rediscovered." If that is so, then shame on the rest of the board. If we are not using all of the tools we already have — the executive session, the lead director, building a collab-

orative team, and tolerating differences of opinion — then we are not doing our job. Term limits becomes an excuse to not address a problem when it should be addressed.

**May:** I, too, am a little troubled with trying to solve a performance issue with term limits. If you have a board, a chairman, or a lead director who doesn't have the mettle to deal with the performance issue of a director — having the tough face-to-face conversation — then you have to wonder what other issues they are ducking in the boardroom. I'm more in favor of term limits simply because of the freshness issue, not as a way to deal with performance issues. Term limits means you push out dealing with the performance issues for some specified period of time.

**Hanson:** On the boards I have served on, after every board meeting, and sometimes before the board meeting, we have an executive session without the CEO. There you will find directors speaking who may never speak at a board meeting. The "duds" come to the surface, and you find they are not duds.

There are people who are shy, who won't speak at a large board meeting, especially in front of management, but will when you get them in an executive session. The lead director, which I am on one board, gets the opportunity both in those types of sessions, and in the sidebar conversations, to really pick up what is on a director's mind. That is dramatically changing how boards function.

**Troubh:** The emergence of the lead director concept, which practically everyone is adopting now and which I very much favor, is going to make evaluations a better tool. The lead director has the responsibility to go amongst the board, coordinate opinions, and then talk to the individual and say, "You are good," or "You're not good" — without the shame and anger and antipathy of the past. The lead director is an extremely effective tool for board management and board self-governance.

**Korologos:** I don't think all board members contribute 100 percent at every meeting. It's all based on their skills, their background, their knowledge, their interests. What's important is that, over time, you all benefit by that director. You may go a couple of years and not know that old Sam knew as much as he did about something until the issue comes up, and then you marvel as he gets into it. That's great, as long as Sam is participating generally and knows the strategy and knows what's expected. We're not all wired for sound



**'Typical tenure of directors is getting shorter — 7.6 years. I would have never guessed that without looking at the data.'**

— *Kenneth Daly*

every meeting. Sometimes your interests pertain to different issues as they come before the board. What is important is building the team, where the diversity of talent, age, and perspective collectively enhances the shareholder value.

**Dickinson:** I couldn't agree more. It is incumbent upon boards to discuss what the ideal composition of the board should be, and what mix of skills and experiences you want on that board, particularly from your nonexecutive directors. In our case, we discuss geographic mix — we don't just want U.K. directors, we want people from the U.S. and continental Europe — and backgrounds. We might be looking for somebody to bring retail or brand experience, IT experience, or financial experience to the board. Boards are like a team, and you have to get that team working properly in order for it to be effective.

### Thumbs up for rotation

**Elson:** Ken, you were in the auditing field before you came to NACD. You effectively had term limits vis-à-vis your auditing work — rotating on and off client accounts. Does that influence the way you look at this?

**Daly:** It does. First of all, as a new person on the scene you're able to ask stupid questions, which sometimes turn out to be not that stupid. So that's good. A point that I would add in to this discussion is that a fundamental problem is the onboarding process. Most onboarding processes are, "The first meeting will be Thursday — be there." You've now been onboarded. It can take a long period of time for directors to get up to speed on what the issues are. Longtime directors have a huge amount of institutional knowledge that's easy to tap into. That's something you lose by rotating them. The onboarding processes have to work a lot better for the new directors to get up to speed.

**Elson:** That's been one of the arguments against the term limit — the notion of indispensability. "This person is the best audit committee chair we have ever had." Yes, that person may be terrific and you don't want to lose them, but what happens if they get hit by a bus? The world goes on. There is always a pool of people ready to come in and do good things. After a given point of time, a board needs to give someone else a try.

**Hanson:** One point that needs to be made is *where* a board member does most of his or her work. It's in the committee meetings. That's a good opportunity for fellow board mem-

bers to judge the contribution that's being made. In these smaller meetings you'll really see someone's productivity or lack of productivity.

**Troubh:** All of the arguments we cited about longevity would apply to committees. They should be mixed up constantly. You should have new people coming in who are "ignorant" in a sense that they ask all new questions, tough questions, that wake up the accountants and the specialists. And I would rotate the committee chairman every three years.

In the old days when I first went on boards, the audit committee was composed of rookies or people who were nearly dead. Nobody cared about the audit committee. Now the audit committee is the most important committee on the board. You can make a mistake in the compensation committee and cost the company a million bucks. You make a mistake in the audit committee and it can be 15 cents a share.



**'We have in the U.K. a system whereby nine years is the presumption of independence.'**

— Lawrence Dickinson

comes at different times, which may not be all that obvious to them or the other board members. A rigid rule cannot pick up that inflection point. It is just not easy to know when different people become less productive.

But why is it so difficult to evaluate peers? We do it routinely in a lot of professions. In accounting partnerships nowadays, partners have to take less compensation when they are not as productive. If we expect a CEO to make hard decisions about his staff, why would we not expect the board to make hard decisions among themselves? That is a legitimate expectation of the shareholders.

**Hanson:** I've been on about 10 public boards, and there are always laggards. Peer review is mandatory. You've got to bite the bullet if a director is not performing. We do represent the

**Korologos:** Depending on committee chairs and membership, I'm seeing on my boards a rotation of three to five years. You can have somebody on the board for 15 years and they take over a committee they have never been in charge of and you get a renewed energy and freshness there.

**Yerger:** The Council endorses rotation on committees.

### What do you measure?

**Bhagat:** That the board member is not as effective in the beginning of their learning curve and that at some point during their tenure we start to see diminishing returns is, conceptually, a valid point. For different people that inflection point

shareholders. Therefore, it's no different from evaluating any other employee — if someone's not performing, it's our duty to find a way to remove that person.

**Elson:** A CEO is easily measured by metric — how the company performs. For a director, if someone isn't showing up for meetings, or doesn't own a requisite amount of stock, or has business relationships with a company, that's easy to evaluate. Going beyond that into subjective observations of performance gets a lot tougher. The director is almost a judge, a monitor. How do you determine the effectiveness of someone as a monitor? There is no body of knowledge that you specifically can test and master. When you get down to it, what you do as a director is evaluate management and what management is saying to you. How effective is this person? How effectively are they relating their vision, their strategy, to you? Do you feel they are competent and capable?

How do you evaluate how effective a director is at that? Ray, you have been around a lot of boards. How do you evaluate someone?

**Troubh:** I've tried to maintain high standards for evaluation of my fellow directors. They ought to be conscientious, smart, team-oriented, and work hard. I ask myself, are they trustworthy and industrious custodians of my investment as a shareholder?

**Korologos:** It is up to the director to have competence, character, common sense, business knowledge and industry knowledge, and a willingness to just go and do their job. The bottom line is the quality of that individual. I do not have time to waste, so if I do not add value to a board, I am out of there. It has nothing to do with my length of service. It has to do with whether I am intellectually engaged, curious enough to find out what is going on, mindful of what is happening in the external world, and committed to my fiduciary duties.

**Troubh:** I don't think it takes nuclear physicists to be great directors. What I mean by that is that it doesn't take a long time. You bring someone on the board, you show them a couple of plans, they go to a couple of meetings, and if they are halfway intelligent, which most of them are, they will pick up on the nuances of the business and an understanding of the industry, and within a short time, if they are any good, they will be a very effective director. The inflection point of effective contribution can be rather quick.

## Present state of play

**Hanson:** In the 30 years since I have been on boards, I've seen directors gaining more control of the company — not the day-to-day control but in the governance. In the old days, you lost your independence the longer you were on a board, because, as the vice chancellor said, you got co-opted by management. I do not feel today on the boards I serve on that we are being co-opted by management. In fact, management realizes that the tide has turned and the board is much more in control of governance of the corporation than even 10 years ago.

**May:** If you join the board as an independent director, you see the value of 'being independent' and you protect that fiercely, whereas in years past it may not have made a difference. In today's world, it does. In the beginning you are an uninformed independent director for some period of time, and then you get to be an informed independent director. Maybe at the end you become a bored independent director, which is when you need to leave the board.

**Troubh:** One of the things that makes me feel a bit better is that the nominating committees are improving. They are taking their job seriously. The chief executive no longer has a dominant role in the selection of director candidates. It is going to take time to build up a nucleus of really independent nominating committees. When that happens, you will see a better class of board membership.

— Jon Hanson

**Elson:** Let's turn to the vice chancellor for a concluding observation.

**Noble:** The question you leave with is the following. We have changed dramatically in the last five to 10 years in how boards operate, how directors view their jobs, and how board members are selected. Do those changes somehow obviate the good reasons that are cited for term limits? Will these curative measures achieve what the term limit notion is designed to achieve? Ultimately, this is the question that each company, each board, each set of shareholders will need to answer for themselves. My sense is that, net net, this issue is probably going to go the way of congressional term limits.

**Elson:** There was a U.S. senator from Georgia who was once asked about the seniority system. He said, "Well, when I first got here, I wasn't too big on it, but the longer I've been around, the more I like seniority." [Laughter]. Thank you, panelists. ■



**'It's in the smaller committee meetings where you'll really see someone's productivity or lack of productivity.'**