

# TOUGHER BOARDS FOR TOUGH TIMES

This special feature by *Elizabeth Judd* is sponsored by *Georgeson*.

It's no secret that signing up directors has become far more onerous recently. And with financial markets in unprecedented turmoil, the growing consensus that CEOs and other top executives should focus their attention at home – rather than jetting around, opining in other companies' boardrooms – is making it harder to recruit top talent.

'CEOs are being limited by their own boards in the number of outside boards they may sit on,' observes Rhonda Brauer, senior managing director of corporate governance at Georgeson. 'In the past, a CEO could sit on two or three boards, maybe more. Now it's one or two, possibly even none.'

One reason CEOs are limiting their directorships is time. 'CEOs are being squeezed,' explains Jeff Neuberth, president of Manhattan-based director search firm Topmark Advisors. 'If serving on a board takes 200 hours per year, that's a big chunk of time away from normal business and family.' Geography has also become a concern, with air travel more burdensome 'and the use of corporate assets like jets under increasing scrutiny.'

Yet another challenge is public perception. Georgeson president

David Drake points out that 'overboarding' – the catchy term for directors spreading themselves too thinly – can earn a company black marks from proxy advisory and governance rating firms. RiskMetrics and some other corporate governance watchdogs are recommending withhold votes and negative ratings for sitting CEOs who have three other directorships.

All in all, these new constraints are making life tougher for companies trying to build a bench of top-notch directors.

Ever since the Enron debacle and the advent of Sarbanes-Oxley (SOX), director independence has become a cause célèbre. Today, says Brauer, 'it's considered good practice to have

at least two thirds of the board deemed 'independent' by stock exchange rules.'

Rajeev Kumar, Georgeson's senior managing director of corporate governance research, says a new proposal requesting an independent lead director has popped up on proxies this year and won strong support at companies including AT&T and Boeing. RiskMetrics' data also show independent chairman proposals receiving record support at more than 20 companies this year.

## BALANCING ACT

Although director independence is widely considered a virtue, companies need to balance it with more practical considerations. There's a tension, asserts Drake, between 'bringing in independent directors with a fresh perspective and bringing in someone with more relevant industry experience.'

SOX also triggered the demand for more financial experts. Drake says the trend is still strong. 'In the past you had directors on audit committees who were rubber-stamping the independent audit firm's work and not asking the right questions about the company's accounting policies. Now you're finding more



Rhonda Brauer, Georgeson

active directors,' he says.

The need for independence, diversity and financial expertise comes at a time when sitting CEOs are scarce. As a result, companies are casting a wider net. Brauer suggests tapping lower-level executives: 'You're seeing younger directors because you're looking at individuals with the potential to be CEOs down the line.' Drake points out that CFOs and COOs are appearing in boardrooms with increasing regularity.

Older individuals are also a more common sight in boardrooms now. Brauer says some companies are reconsidering their mandatory retirement age because they'd like to attract retirees who have significant business expertise to share.

Yet the idea of eliminating a mandatory retirement age may be approached with trepidation because it's an automatic mechanism for getting rid of directors who aren't pulling their weight. Brauer suggests retirement ages are often instituted or retained because it's awkward for a company chairman, lead or presiding director, or chair of the nominating committee to approach a director who isn't performing well and recommend that he or she either take steps to improve his/her board contributions or resign from the board. 'If you could have more of those open and honest conversations, you might be able to do away with retirement ages altogether,' she says.

Finally, Rachel Posner, senior managing director and general counsel at Georgeson, says board candidates should be evaluated based

on their commitment to the role. She also suggests testing prospects' chemistry with the existing board. 'Invite them to meet the directors and see how it works,' she advises.

### AN ACTIVIST TWIST

At some firms, boards are being pressured to appoint representatives of activist shareholders to their membership. Brauer, who until this spring served as corporate secretary and corporate governance officer at the New York Times Company, notes that in April two nominees from a hedge fund were elected to the newspaper giant's board to settle a potential proxy fight.

'The board agreed on two of the four names that had been proposed initially so management and the board could end the proxy fight and continue focusing on the company's long-term strategy,' she says. In cases like this, adds Brauer, 'one question is: how will the additions affect the collegiality in the boardroom?'

Director elections have become an outlet for shareholder disillusionment on other fronts. 'We're seeing more withhold-the-vote campaigns,' says Brauer. 'If shareholders have the right to vote on the compensation of top executives, there will likely be more withhold votes against compensation committee members.'

Of course, the intense scrutiny and charged atmosphere can be a turn-off for prospective directors. 'For someone at CEO level, the director compensation – which is generally much lower than executive compensation – may not be worth

the additional potential liability and additional publicity,' says Brauer.


### WHAT TO EXPECT

Given the new board landscape, director searches might take longer than before. Neuberth estimates that a quick search might last 10 to 12 weeks, while a protracted one could take three to six months.

One positive, says Brauer, is that some companies have started soliciting input from their shareholders about qualities they desire in new directors. Boards or nominating committees can also authorize search firms to approach a company's largest institutional shareholders and get an idea of what characteristics a future director would ideally possess.

Ultimately, many of these changes should result in stronger, better-equipped boards. As companies seek more independence, expertise and diversity in their directors, change will come – but it's likely to be gradual. 'Remember,' concludes Neuberth, 'this is like a big super-tanker slowly turning.' ■

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