# Board Director Evaluation

**Board Qualifications**
Successful boards are self-aware and will *"… monitor the mix of skills and experience of its directors in order to assess, at each stage in the life of the corporation, whether the board has the necessary tools to perform its oversight function effectively."*

Mutual boards must each decide what mix of abilities, attributes and motivations are necessary for a director to be effective in their organization. The specific tasks or competencies expected of directors help companies identify qualified candidates. These tasks include overseeing accounting and finance practices, reviewing management practices, responding to potential crises, approving strategic plans, and empowering and motivating the chief executive. Having directors with general business or insurance industry experience can be helpful in addressing and meeting these obligations competently.

But insurance knowledge is not a requirement. In selecting any new director the question should be: *How can this individual most contribute to the success of our mutual company through decision-making or counsel to our board and management?*

A variety of factors will influence the selection of a director, including:

**Company situation**
- Company size: Is this person familiar with a company of this size and structure?
- Stage of growth: Is this person familiar with a company with these growth expectations?
- Financial condition: Would special financial knowledge or experience be helpful?
- Competition: Would a specific industry background be helpful?
- Technological change: Would technology experience or knowledge be helpful?

**Personal Experience**
- Demonstrated track record in a specific area of needed expertise.
- Knowledge of the insurance industry or a specific customer market.
- Successful experience as a corporate director elsewhere.
- Experience or expertise in long-range/strategic planning.
- Experience or expertise in finance/accounting (perhaps specifically insurance accounting/finance).
- Experience or expertise in technology/systems.

**Personal characteristics**
- Integrity: A high ethical standard in their personal and professional life.
- Accountability: The willingness to commit the time required for the work of the board and to be responsible, both in taking warranted action and in being held accountable for it.
- Engagement: The ability to honestly discuss and evaluate management and corporate performance.
- Judgment: Informed and intelligent decision-making and the potential for good counsel on the range of likely business issues.

- Financial literacy: Knowing how to read financial statements and how to use financial ratios in an insurance company context (see section on financial literacy later in this section).
- Maturity: A willingness to listen, to be open to the opinions of others, to communicate both persuasively and tactfully.
- High performance standards: Personal or professional achievements.

Personal characteristics can be very important since most boards try to create a collegial culture that has been linked in a positive way to overall company performance. On the other hand, *collegial* should mean professionally compatible and collaborative, not *clubby*.

In an effort to improve board performance, boards may wish to formally establish certain expectations that come with service on their boards. This can be addressed in a written "position description" for directors, and several models exist that incorporate much of what is presented in this section.

Recently, companies have also begun to limit the number of boards on which a current director can serve. As the demands on board members increase, service on several boards can interfere with the commitments of time and attention expected of effective directors on any specific board. This must be balanced against the helpful experience that having directors serving on other boards can provide to mutual companies.

Finally, director motivation is a critical element of effective board service. Mutual company directors must be committed to the company, its mission and vision (including the "mutual" concept), its business plan, and the pursuit of policyholder value over the long term. Directors should be motivated enough to ask good questions and the persistence to insist on accurate, honest answers from management.

**Board Evaluation**

One of the areas of board governance that has received a lot of attention is that of board and director evaluation. The Business Roundtable and similar organizations suggest that a "… *board should conduct periodic – generally annual – self-evaluations to determine whether it and its committees are following the procedures necessary to function effectively.*" These recommendations are based on the premise that any person, organization or process can be enhanced by evaluation of performance and dedication toward necessary change.

Board evaluation is, however, a relatively new idea in corporate governance practice and it is not widespread among companies. Recently, 63 percent of CEO's serving as outside directors of public companies reported that they had never been part of a board evaluation. Of these same CEO's, 42 percent had never participated in a board evaluation for their own boards.3 Despite these numbers, 91 percent of public company board members support regular board evaluations. This suggests that CEO's and other key board members are willing for meaningful board evaluations to take place. Only 15 percent of NAMIC mutual member companies surveyed conduct board self-evaluations.

The recognized advantages of board evaluations include:

- Strengthening overall board and individual member performance.

- Its effectiveness as an audit of current performance and of possible areas of improvement.
- A means for measuring progress and an aid to prioritizing improvement efforts.
- Raising individual board member performance issues in an objective manner.
- Regularly reviewing governance as a critical process for peak performance in a business environment of rapid change.
- Serving as a model/example to all in the company regarding performance evaluation and demonstrating the importance of organizational development based on feedback.
- Reinforcing the corporate governance responsibilities and objectives of the board and each member.
- Providing an opportunity for each member to reflect on both overall board and individual director contributions and providing explicit recognition of board success and important contributions from individuals.
- Answering critics who are expecting or demanding more accountability from the board.
- Minimizing errors or weaknesses in the governance process that might create public relations or legal issues later.

There is no better group to evaluate the effectiveness of the company's governance efforts than the board itself as directors appear to be very familiar with their areas of strength or weakness.

Recent studies indicate that boards believe they are most effective in areas of board-management relations, corporate governance, compliance, executive compensation, and director recruitment/nominations. Boards believe they are less effective however, in such key areas as risk management/control, strategic planning, and CEO succession.

Boards choosing to conduct self evaluations will first want to decide what kind of evaluations to conduct: the overall board; director evaluations, board leadership. The board will also want to select the method of evaluation: self-evaluations or peer evaluations.

Overall board performance evaluations generally include the following topics in an attempt to evaluate board "effectiveness":

- Board responsibilities.
- Adequacy and timeliness of information.
- Appropriateness of meeting agendas and time.
- Team work of directors, level of discussion, decision-making.
- Trust, candor, mutual respect, cooperation.
- Independence of thought and decision-making.

Individual directors' evaluations generally include the following topics in an effort to evaluate individual director "contribution":

- Meeting attendance.
- Degree of preparation.
- Active participation in meetings.
- Ability to communicate and express viewpoint.
- Willingness to listen, openness to ideas.
- Understanding of company and industry.

- Independence of thought and decision-making.
- Ability to work well with directors and management.

Mutual companies that commit to a board evaluation process should be prepared to respond to likely anticipated negative reactions by some board members.  Evaluations are a considerable challenge for any work group –especially one composed of high-level managers, executives, business owners or professionals. Directors may be reluctant to engage in what is a new, challenging and un-bargained for evaluation process.

As a result, proponents of evaluation should plan to address some of the following process issues:
- How to ensure board agreement on and commitment to evaluations.
- How to establish goals for board and board member performance to use in the evaluation.
- How to measure or evaluate progress or success.
- How to address issues of candor, confidentiality, and objectivity.
- How to formalize the process going forward.
- How to address any issues or areas of improvement opportunities.
- How to follow-up to ensure this is a helpful process.

Since board evaluation is a new area for most directors, it should be handled carefully and the process developed cautiously. This often means that boards will begin with just an overall board evaluation and/or individual board member *self-evaluations*. Eventually, if the board desires to move further in the area of evaluation, board leadership evaluations and individual director peer reviews might be implemented. Such an approach allows the board time to evaluate the progress and results of the evaluation process before committing to further and potentially more involved evaluation efforts.

It can be helpful for a board to assign responsibility for the board evaluation process to a single board member, or a group of board members, or a committee. This delegation and accountability helps ensure that the evaluation process actually takes place and that it receives the planning and follow-up that it deserves. The chairman (if he is an independent director) or the lead director is a likely candidate for the responsibility if a single individual is selected to manage the evaluation effort. The chairman of a nomination/governance committee is also a good choice. If a group is assigned the responsibility, a nomination/governance committee, an executive committee or a board task force is likely the most appropriate selections. As an alternative, the board could hire an outside consultant to initially help the board through this challenging process. In making any of these choices, considerable thought should be given to the tact, integrity, confidentiality and other qualities deemed important for the evaluation to work well.

**How to implement**

First, of course, identify or confirm individual director performance expectations. Any existing board director "job descriptions" or delineation of functions (some spelled out in the bylaws) should be used. These can help identify and clarify expectations in an orderly and non-controversial fashion and help give a framework to the process.  Perhaps this can be done by the chairman or a small group of directors, or the governance or nominating committee.

Second, present the results for review and endorsement by the full board ahead of the process. When this step is carried out properly, board acceptance of the expectations usually comes rapidly. The criteria should be hard to dispute, being logical conclusions produced by an objective process. Of course, disagreement on specific criteria can be expected, but this is healthy since it brings to the surface differences of opinion which may have been the cause of past problems or simply help refine the expectations.

Third, consider a trial run to test the clarity and completeness of your standards. Testing can be accomplished by conducting a trial ***evaluation*** by or for board members who were not part of the development process. Feedback should avoid disproportionate debate on whether the plan is "good" or "bad." Rather it should concentrate on specific modifications and refinements which will make it better. It is best to avoid voting on whether board members "like" the process. Some board members may resist any ***evaluation*** process because they fear being rated poorly. Either ego or self deception can provoke a negative reaction. It also is for this reason that the self test should be limited to a representative group of board members whose opinions can be expected to be constructive.

Fourth, prepare written guidelines and procedures.  For any ***evaluation*** program to remain workable, the details of how it is carried out should be put into writing, and an individual or committee assigned to keep it current.  It avoids misunderstandings, and brings new members up to speed sooner.  As the board turns over, the guidelines should be used for orientation of new board members as well as ensuring the system is maintained.  Details should include frequency of ***evaluations***, the directors responsible for sending out and collecting the appraisal material, etc. Obviously, as experience is gained and business conditions change performance standards also should be changed.

Finally, audit the process periodically. An important part of any performance review process is periodic auditing. The *evaluation* methodology should be included in the written guidelines and include recommendations to the board based on the board's hands-on experience. Are the ***evaluation*** instructions adequate? Is there sufficient lead time to complete scoring? Were standards clear and complete? Is it helping directors become better contributors?

**Evaluation oversight options**

Individuals themselves, peers, the board's governance committee, or the chair and/or senior executives are in a position to review an individual board members' performance. We list these options below.

**Peer review.**  The chair and each member of the board could complete an anonymous performance evaluation of one another. Results would be collated, averaged and returned privately to individual directors. Overall board performance scores would be discussed at a board meeting.

**Corporate Governance Committee**.  Members of the board's corporate governance committee (or nominating committee) could evaluate the performance of individual directors. This would be based on a common understanding of the directors' responsibilities, as well as other stakeholder expectations. Feedback would be confidential and directed to the individual.

**Self Evaluation.** Individual board members could assess their own performance, guided by the criteria of an evaluation instrument. These assessments could be discussed with the chair and/or peers.

**Top Management Team.** The CEO and the executive team could also assess the performance of individual board members, facilitated by a performance evaluation form. ***Keep in mind that "upward" criticisms are problematic.***

**Chairman only.** The chair could provide confidential feedback to each director, based on personal observation and may include aggregated comments solicited from other board members and senior management.

Most authorities agree that the most effective way to measure and improve performance is by peer and/or individual self-assessment. Both should be done privately and facilitated by the chair. Many experts prefer self-assessment facilitated by the chair because criteria vary according to the type of enterprise, the ownership pattern and the reason each director was appointed. Here, mutual organizations may have an advantage over stock companies in that mutuals do not experience pressure from institutional investors and shareholders' rights campaigners for other (even public) forms of assessments.

**Use of Results**

Finally, there is a very practical issue to address: How can anyone actually use the results of a performance appraisal? Of course, no one can force a board member to perform. A board does not have the same supervisory powers as management does in other typical performance evaluations situations. Assigning blame and fixing consequences are not a board's traditional responsibilities.

The primary, some say exclusive, reason for evaluating board members is to identify non-contributing directors. Others contend that any evaluation process that is focused on singling out an individual director for "counseling" or removal will be met with significant resistance. Rather, the focus should be placed on improving the overall effectiveness of the board through individual self or peer assessment. There are several reasons for that: board members are peers, criteria are subjective and each member brings unique assets to the board. As a result, ***evaluation*** is a difficult process on an individual director level – so difficult in fact that some experts believe that only the nominating or corporate governance committees in cooperation with the board chair should do it (or at least facilitate or coordinate the process).

If director non-performance ever becomes an issue, the evaluation process may be of some assistance. If done through a committee and/or under the authority of the chair, it is possible that a non-performing board member could be "counseled" and or asked to resign. However, this option already exists and the process leads to great discomfort. In fact, in a somewhat dated survey of 546 companies, only 13 cases were reported where directors were forced to resign [J.P. Dunlan, Evaluating the Board: The Next Dimension, Sept. 1995].

An somewhat easier option, if non-performance is considered to be a current or prospective issue, is to set term limits for board appointments/elections. This could challenge a sacred principle of "appointed for life," but may be more palatable to the board going forward as part an overall board governance improvement effort.  It also provides the opportunity for governance or nominating committee involvement in the process of director evaluation – a recommended practice.  The committee could then assess individual director contribution at the time of re-nominating the director.

**Evaluation factors – Differences between Board and Individual Director Criteria**

**Board Performance – "Effectiveness"**

- Whether key responsibilities in the charter were carried out.
- Adequacy and timeliness of information received.
- Appropriateness of meeting agendas and meeting time allowed.
- How well directors worked together.
- Appropriateness of discussion/communication.
- Degree of consensus on key issues.
- Degree of compliance with expectations/qualifications.

**Director Performance – "Contribution"**

- Meeting attendance rates.
- Degree of preparation.
- Active participation during meetings.
- Ability to communicate and express ideas.
- Willingness to listen and acknowledge the views of others.
- Understanding of company and industry.
- Ability to work with directors and management.
- What the director does well.
- What the director should do differently.

**Sample 1: Director Expectations/Evaluation Criteria**

- Fulfilling the legal requirements for board membership and governance, including the duties of due care, loyalty and disclosure;

- Becoming familiar with the governing structure and documents (articles, bylaws) of the company;

- Representing the interests of the entire policyholders in board discussions, decisions and actions; developing an increasing awareness of their needs and views;

- Participating with other directors in establishing policies for the company and in monitoring performance and compliance with such policies;

- Attending regularly scheduled and special meetings of the board or policyholders – attendance at a minimum of three board meetings and all policyholder meetings;

- Preparing for each board meeting using the agenda and materials supplied and requesting additional information if necessary;

- Participating in the discussion, decisions and actions of the board, making your knowledge and experience available as appropriate; encouraging free and open discussion of the business of the company;

- Undertaking and fulfilling committee assignments and other tasks at the invitation of the Chairman or the board and participation in at least one board committees as requested;

- Supporting board actions publicly;

- Reporting all real and potential conflicts of interest to the board.

**Sample 2: Director Expectations/Evaluation Criteria**

**SERVICE**
- attends all meetings
- contributes to discussion
- contributions add value
- provides wise counsel
- appears to be well informed
- respects confidentiality
- is an effective team member
- demonstrates collegial good manners
- facilitates the movement to consensus
- understands the critical issue quickly
- influences corporate effectiveness
- actively participates in decisions
- provides counsel/advice to senior management between meetings
- builds staff-board partnership
- makes suggestion that produces an improvement
- is available for private consultation
- provides access to outside resources and constituencies
- lends credibility/legitimacy to organization

**CONTROL**
- understands and fulfills fiduciary responsibilities
- is familiar with by-laws and regulations governing the organization
- monitors programs and/or services
- asks the tough questions
- willing to rock board when believes strongly about an issue
- keeps on top of industry issues, in addition to information provided by CEO/management
- does not refrain from constructive criticism of senior management

**STRATEGY**
- participates actively in establishing corporate strategy
- influences corporate strategy
- understands mission and vision of organization
- uses the vision/mission as a standard to make decisions
- makes knowledgeable, prudent decisions
- is an advocate for the organization
- focuses on major issues
- questions focus on policy and strategy, not tactics and operations

**STAKEHOLDER INTERESTS**
- represents stakeholder interests to board and external bodies as well
- provides information and advice on how to optimize value
- challenges management on performance goals and results