Board Refreshment Beyond Term and Age Limits

Description

The role of the board is more important — and complex — than ever. In many ways, the board is the tip of the spear in the battle against the disruptive forces that impact business more broadly — increased competitive risk, the rise of emerging technologies, and social and demographic shifts that impact everything from our customer base to brand identity to how we retain talent.

In this environment, it is critical that the board be fit for purpose.

“Whether it’s technology, global politics or a pandemic, the world is constantly changing and evolving,” says Ellen Richstone, who serves on the boards of Superior Industries Inc., Orion Energy Systems Inc., eMagin and Cognition Therapeutics. “If a company is not constantly changing and evolving, they’re not going to be around for very long.”

The board is only as strong as the people sitting around the table. In this new environment, companies must adopt a proactive and thoughtful approach to board refreshment, one that ensures board members’ expertise aligns with company strategy and long-term value creation.

“The focus and needs of the board are going to change as the marketplace changes and the company’s strategic vision evolves,” says Susan Ness, who served on the board of TEGNA. “As a consequence, the board needs new ideas and new people coming in to ask questions about board assumptions and practices.”

Vada Manager, who serves on the boards of Valvoline and Helios Education Foundation, agrees. “We understand that boards don’t need to be comprised solely of CFOs and CEOs. Given a changing demographic base, a changing country, a changing operating environment, and a focus on a broader range of stakeholders and shareholders, boards are looking at a broader plethora of issues, which means you need to have a more diverse set of skills and perspectives on the board.”

Ensuring your board is prepared to address future challenges requires two things: thinking critically about who is sitting around the table and ensuring that experience and skill sets map to the company’s long-term strategy. “Every year, a board should be looking closely at its makeup,” says Richstone. “You start with, ‘What are the needs of the company for the next three or so years? What is the
makeup of the board? Do you have any big gaps? Is everyone pulling their own weight?’ And I think that’s an exercise that every board should go through every year.”

Ness agrees. “Boards should be asking, ‘Do we have the right expertise around the table? Do we have a board that reflects our changing customer base?’ For example, if you are doing a lot of business with China, do you have a board that really understands how business is done in China?”

**Elements of Board Refreshment**

A solid board refreshment plan can be the linchpin to unlocking the board’s true value because it forces the board to take a hard look at its own strengths and operating environment. To ensure the right composition, the board must be rooted in a future-focused view of the company, says Manager. “It’s almost like multilevel chess to figure out what your board composition is like now and what it may look like after, for example, an acquisition takes place. Are the current board members old-world with regard to what the company used to be, or will they still be relevant when you map the strategy going forward? It’s imperative that the board not just look at what that company’s doing today, but forecast what it may be doing in two to three years and look ahead even further.”

Cheemin Bo-Linn, who has served on 13 corporate boards and is currently a director for Flux Power, KORE Wireless and Blackline Safety Corp., sees several critical benefits to a thoughtful board refreshment process. “First, it helps the board create the right mindset. What do we need to change to be more effective, and is that aligned with our fiduciary duties and corporate strategy? Second is a focus on continuous improvement. A good board refreshment process resets expectations because the individual board members focus on their own metrics around contribution or competency. Third, a good board refreshment process centers a future-ready set of optics and board deliverables. I have noticed that on my boards with a thoughtful refreshment process, we have keener market insights, we have improved board judgment and we talk more about competitive advantage. By looking at the composition of the board on an annual basis, we have a deeper awareness of changing market dynamics and we’ve become more agile.”
Age and Term Limits

Despite the role refreshment can play in enhancing the overall performance of the board, there are still many that don’t prioritize it. According to 2022 benchmarking data by The Conference Board, about one-third of board members had a tenure of 12 years or longer, while 16% of then-seated Russell 3000 directors and 16% of S&P 500 directors had served for at least 16 years. “There are so many boards where there’s been no change in board membership for years,” says Ness. “That’s not good leadership.”

The slower pace of board refreshment has led to increasing calls for standards and best practices to govern the ways that boards make space for new talent. One way to create more openings is to increase the size of the board, but this can present its own challenges — if the board is too large, it can be more difficult to manage discussions or gain consensus on critical topics. Richstone sees value in expanding your board — if it’s done thoughtfully. “There are times where, even if you have the skill sets you need and the mix is good, but you still aren’t bringing new people on the board, I think you need to consider expanding the board even just by one person, because a new person with new ideas is very important. And I don’t think you should go more than a couple years without that happening.”

In addition to increasing board size, more governance and diversity advocates are calling for triggering mechanisms to force board refreshment, namely age and term limits.

Term limits dictate that a board member must retire after a set number of years, most commonly 12 or 15. Age limits govern the point at which older directors are forced to retire. While there has been more call for such limits as a part of driving board diversity and effectiveness, very few U.S. companies use them. As of July 2022, only 6% of S&P 500 companies and 4% of Russell 3000 companies disclosed a mandatory retirement policy based on tenure. While age limits have been by far the more popular choice, more companies are moving away from rather than toward them. For example, the share of S&P 500 companies with age limits declined from 70% in 2018 to 67% as of July 2022, and from 40% to 36% in the Russell 3000. In many cases where they do exist, a company will raise the age limit for retirement once directors are within striking distance of the target, or they make an exception to their policy to keep a valued director in place, rendering those limits moot.

Those who favor age limits say that, at precisely the time when boards need fresh thinking, boards themselves are getting older. The data backs this up. According to a study by Corporate Counsel Business Journal, the average age of directors in the United States rose to 63.34 years in 2021, up from 62.64 the year before. A study of boardrooms worldwide reported that U.S. boards’ average age far outpaces that of their counterparts in Europe, Canada and Australia. The call for age limits is in part driven by a shift in the profile of who makes a good director. Increasingly, boards are looking for those with current, relevant skill sets forged in operating roles, something that is less likely to be true as directors get older. Richstone concedes the rationale behind the call for age limits, but says that, in practice, they can be counterproductive. “Age limits are so hard because you see people who are very current, very active, and they are 72 years old. And then you see people at age 60 who you think, ‘How quickly can we move them off the board?’”

Term limits, for their part, can play a critical role in not only bringing new voices to the board, but also ensuring adequate director independence. “In many European countries, after a decade or so, the
assumption is that a director is no longer independent. The director may be able to stay on as a nonindependent member of the board or overcome the presumption by reaffirming independence. It’s not a given,” says Ness. “And the reason is, you’ve become so comfortable dealing with the same corporate players that you relate more and more to where they are coming from and less and less to your function as an outside individual on the board representing shareholders and the community at large.” Richstone has seen this play out in her own network, where directors volunteer to step off the board after 10 or 12 years of service. “At some point they just become so invested, they don’t feel quite as independent anymore.”

But many key stakeholders are not convinced that rigid limits create the right kind of board refreshment. A recent analysis by professors at NYU Stern School of Business posits that board-wide term limits may be detrimental to the board, the company and the shareholders if they force valuable directors out. In addition to their own findings, the researchers cite Institutional Shareholder Services guidance from 2017, stating “Term and age limits, as they have been typically applied, may not be the solutions, because they force the arbitrary retirement of valuable directors.”

Bo-Linn sees another unintended consequence of both age and term limits: They can actually have the opposite of the intended effect, creating a scenario where underperforming directors stay longer than is good for the board. “Age and term limits are not responsive to strategic needs. Let’s say you have a director who is 57, he’s been on the board for nine years and he’s not performing. Your board’s age limit is 62 or you have a term limit that is 12 years. Are you going to wait five years until he hits the age limit, or even three more years until he hits the 12-year mark? That’s what I call ‘event-driven’ behavior, and it’s at the sacrifice of the company being agile and being competitive in the marketplace.”

**Good Governance or Conflict Avoidance?**

The larger point that can get lost in the debate over age and term limits is that how board refreshment happens reflects the health of the board itself. The whole point of board refreshment is to ensure the board is thinking strategically and proactively about its work. Relying solely on forcing mechanisms like tenure or age can provide what amounts to an easy way out, allowing boards to bypass the work of having challenging — but necessary — conversations about how they may need to change.

For example, there could be a board member who is not pulling their weight or someone who is a great contributor, but whose skill sets are no longer as relevant given where the company is headed. In an ideal scenario, engaged board members can see that the needs of the board are shifting and surface the conversations themselves. Notes Manager, “The better board members I’ve served with recognize, ‘Maybe I was appointed to the board when the company was X, but now the company is Y, so I won’t put my name up for reelection because I can see this is an opportunity for someone with a more relevant and current skill set.’ I think those are the kind of board members you need — people who are looking after the shareholder interests.”
That is the ideal scenario, but it’s not always practical to rely on that level of self-awareness. Board members are human beings, and human beings can be notoriously bad at seeing their own blind spots. And the hard truth is, even for seasoned professionals, it can be uncomfortable to tell a colleague that they are no longer the right fit. “It’s very hard for directors to say bad things about their fellow board members,” says Richstone, “because everybody in the boardroom has had great careers. They’ve gotten on the board because they’ve done wonderful things that are considered valuable for the company.”

While it can be hard to tell a valued colleague that they are no longer the right fit for the board, avoiding the conversation because it’s uncomfortable is an abdication of the board’s core responsibilities. If the board is avoiding a conversation about offboarding simply because it may be unpleasant, what other issues might they be avoiding? An underperforming CEO? An aggressive competitor? A stalled corporate turnaround? “A good board refreshment process can trigger candid conversations about board member effectiveness, and be a necessary catalyst for change,” says Bo-Linn.

Age and term limits are increasingly held up as a way to bring badly needed diversity to the board. On its face, that argument makes sense. Given historical power structures that made it difficult for diverse leaders to break into the C-suite, it is more likely that older or longer-tenured directors will also be less diverse. While age and tenure triggers can be a helpful tool, the more sustainable way to create diverse and relevant boards, says Bo-Linn, is to get curious, rigorous and specific about board effectiveness. “Instead of age or term limits, we should focus on: Do the board directors stay current? Are they active in the field? And do they know how to help the company stay competitive by asking the right questions?”

To Bo-Linn’s point, boards that think deeply about their optimal composition in the current business environment are prioritizing historically overlooked skill sets like digital transformation, people leadership and industry expertise. This widens the aperture of who should be sitting around the table and creates openings for more diverse talent. Boards that simply rely on triggers may never do the hard work of identifying those gaps or that emerging talent, and therefore may swap one director for a younger or less tenured version of the same.

Part of fulfilling fiduciary duties is doing the hard work of thinking critically about the company strategy, the emerging risk profile and how board composition must map to those factors in order to serve the company long-term.

“Remember, time is not in your favor in today’s marketplace. You can’t wait for an event-driven trigger like age or tenure,” says Bo-Linn. “It is tough to bid farewell to a director, especially if the person is a founder or has been on the board a long time. The board should look for recency and relevancy of experience to help the board be future-ready. With an annual board refresh, it gets done, and then those triggers may not be necessary.”

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