Forecasting the Trump Governance “Windstorm”

Description

What boards should focus on—and ignore—in an uncertain regulatory environment.

Since President Trump took office, boards have been bracing for a weather change in corporate governance.

While many directors believe potential changes will be generally positive for Corporate America, the lack of certainty on what those changes will be is the biggest issue for board members. The first months of the administration, says one board member, have been “like a windstorm, and its direction is uncertain.”

The political maelstrom has many on edge and unclear on what to expect as far as tax reform, trade, regulations, immigration, healthcare, and infrastructure spending, explains James Cox, the Brainerd Currie Professor of Law at Duke University, who specializes in corporate and securities law.

“Regardless of whether you’re in a red, blue or purple state, your business is going to be operating in an even more dynamic, hard-to-predict environment,” he adds. “It’s going to test the elasticity of the board when it comes to oversight.”

Boards are opting to be patient.

“I think most of us are still in a ‘wait-and-see’ mode,” says Jill Kanin-Lovers, who sits on the boards of Heidrick & Struggles and the Homeownership Preservation Foundation. “Every day seems to bring a surprise but nothing tangible yet to help with business planning.”

Indeed, the much-anticipated repeal of the Affordable Care Act surprisingly failed amidst political wrangling; and promises to gut Dodd-Frank may also fall short.

The Trump administration’s moves, while sometimes unpredictable, are partly informed by business leaders.

A host of CEOs for some of the largest global companies, including The Walt Disney Company, PepsiCo, Walmart and General Motors, among others, sits on Trump’s business advisory panel along
with other top business leaders, and the administration appears to be listening.

“I do believe they have open minds,” says Steve Klemash, a partner at the firm who directs the EY Center for Board Matters, about the new administration. (EY’s chairman and chief executive officer Mark Weinberger has a seat on the president’s business advisory panel.)

Klemash adds, however, “I have no idea where they will go. It’s complex; a lot of different variables.”

The general feeling has been “be alert and be aware, but don’t stop doing anything you’re doing,” says Elaine Eisenman, who sits on the compensation committee for shoe retailer DSW Inc. and is a member of the advisory board for Women Corporate Directors Foundation.

While there has been talk of doing away with regulations such as the disclosure of CEO pay ratios, it’s still unclear what will happen, she explains.

“For the boards I’m on, everyone is acting like the world is moving in the direction we thought it would before the election, but we are aware about other actions that can occur,” she notes. “No one knows what’s going to happen in changing regulations, reporting requirements. There are so many unknowns. We need to be nimble.”

The key is being vigilant and identifying what’s actually real, she stresses. But she notes, “How much action do you take for something that may not actually occur?”

A February survey by the National Association of Corporate Directors found:
“Fifty-one percent of companies are now reassessing core assumptions about the impact of new and proposed policies on their strategic growth plans.”

By most accounts, the Trump transition has been unlike any previous turnover of a political party.

“The difference between this and previous administrations is you have a high factor of unpredictability, even though the market sees this as positive for the economy,” maintains Andrea Bonime-Blanc, author of The Reputation Risk Handbook: Surviving and Thriving in the Age of Hyper-Transparency and chief executive officer of GEC Risk Advisory LLC.

And it’s all happening as the world at large is facing unpredictability, adds Bonime-Blanc.

“The geopolitical risk is much more of a factor with the world changing in ways that boards aren’t prepared to deal with,” she says. “There’s a lot of swirling allegations and political intrigue we haven’t seen since Watergate, and we have geopolitical risk at home that board rooms haven’t had to worry about.”

It’s unclear when or if that will improve, but the unpredictability of the Trump administration isn’t helping. Bonime-Blanc stresses that this is “nerve-racking for board members.”

Indeed, many board members declined to comment for this article, in part, because the topic is seen as volatile given how polarized the nation has become and the president’s unpredictable Twitter behavior.
“A lot of the reason you don’t hear from board members is they don’t want their companies to become targets” of a potential Trump backlash, explains Bonime-Blanc.

Early in his presidency, Trump went after Boeing over the price tag for a new Air Force One. He later derided Nordstrom following the retailer’s decision to drop his daughter Ivanka’s apparel line. Online websites such as TheHill.com have been keeping a running tally of the companies the president talks about on social media, including Ford, Carrier and Lockheed Martin, just to name a few.

Aside from the president’s temperament, members of his own party are increasingly pushing back on some proposals, and could derail many of the administration’s plans, including the alternative to the Affordable Care Act. This just adds to the uncertainty, she says.

Where to put board energy?

The most highly ranked policy issues that board respondents to NACD’s survey are talking about include: “corporate tax reform, deregulation, and trade protectionism.”

Taxes. Promises of tax reform and tax reductions are garnering cautious optimism from the business world, and talk from Trump that he’s going to cut the corporate tax rate by 15% has many on the edge of their seats in anticipation.

That kind of reduction could give corporations more capital to invest, says Angela Brock-Kyle, the audit chair and a member of the nominating and governance committee for Infinity Property and Casualty Corp. Boards may want to start thinking about strategies for such a reduction. But depending on the industry, she cautions, the gains could be offset by trade tariffs.

“For global businesses, tax policies become less of a determining factor,” says Brock-Kyle, who is also founder and CEO of B.O.A.R.D.S., a privately held governance, strategy and risk advisory firm.

“You can’t just take one of these issues separately,” stresses EY’s Klemash, adding that boards have to look at their operations and which changes could potentially hit their supply chain. “Make sure management is going through some form of modeling [for different scenarios], stress testing them, and updating them regularly.”

Regulations. President Trump signed an executive order requiring the elimination of two regulations for every one new regulation that’s introduced. But governance experts believe what ends up happening will be a bit more nuanced.

Legislators are meeting with management at major corporations to look at all areas of regulation—which are the most cumbersome and the most costly and causing companies not to grow and not to hire, Klemash explains. “There are a lot of conversations on how to make regulations smarter.”

When it comes to financial regulations, the approach may be measured. Trump’s pick to head the Securities and Exchange Commission, Jay Clayton, said during Senate confirmation hearings that:

“Dodd-Frank should be looked at, in particular rules that have been in place as to whether they are achieving their objectives effectively. But, I have no specific plans to” attack the legislation, according
to an article in Bloomberg in late March.

Duke University’s Cox doesn’t expect laws such as Dodd-Frank to be eviscerated, but there will be changes to the regulatory environment that will create “winners and losers.” The key is figuring out how they impact your organization, he adds.

“The cost of compliance with increasing multiple regulations has skyrocketed, along with risks associated with not being in compliance. So, to the extent those things are simplified, that’s great,” says Brock-Kyle. “But it’s important to remain mindful of what regulations are trying to accomplish.”

For example, President Trump signed an executive order to halt the Department of Labor’s fiduciary rule, which would have required financial advisers who handle retirement accounts to work in the best interest of their clients. The rule, she explains, was “designed to keep advisers honest, put their customers first. That should be a critical goal of businesses.”

Trade. In a February press briefing, White House Press Secretary Sean Spicer made it clear: “The president is looking at tax policy that encourages manufacturing and job creation in the United States.”

The critical question is whether a tax on goods coming in and out of the country will be implemented, says Klemash, and if so how much and when.

Given the potential impact on the cost of goods, he suggests, “boards should be thinking about what the overall trade balance of their organizations is,” especially retailers.

It’s something DSW’s Eisenman has her eye on. The focus, she adds, has been on “what to do in terms of the ability to keep prices low and remain profitable.”

The National Retail Federation, she continues, has taken a strong stand on the issue. As a board, she says, you have to make sure you’re being “proactive and quickly reactive, while you keep looking for opportunities.”

Other policy issues that are also on the table include healthcare reform, infrastructure investment, and immigration, a pressing issue for many corporations.

With the administration’s travel bans and a swelling of anti-immigrant sentiment, global companies should also be thinking about human resources. In March, the administration announced the suspension of fast-tracked H-B1visas, which allow companies to hire foreign workers for certain skilled jobs.

“We believe borders should be secure,” says Klemash, but depending on the industry, companies could face talent issues.

Brock-Kyle says beyond employee impact, there could also be an impact on customers. Boards, she advises, should be asking themselves: Are our products or services used by individuals who may be forced to leave the country, or relocate? Do we operate in sanctuary cities?

No matter the potential policy changes, Klemash offers three action steps for boards right now:

• Make sure your points of view are being heard. It’s important to reach out to legislators federally and...
in your state, give your views on these areas, work with various trade associations, and enlist the help of lobbyists if you use those.

- Think about spending capital. Your stock valuation could be at an all-time high, so consider potential new acquisitions, new technology and enhance your position relative to digital.
- Be strategic based on potential developments. You have to have a plan and adjust accordingly, but at the same time you have to run your business.

In order to make sure business is running well during turbulent times, governance experts urge directors to look within the boardroom.

“This is absolutely a time to increase attention on board effectiveness, and thinking through board diversity as well,” advises Constantine Alexandrakis, head of U.S. business for Russell Reynolds Associates.

“If you have a board with directors who have largely been out of active management of a business for more than five years, that could be a recipe for disaster unless directors are able to keep current in other ways,” he explains. “Be a lot more systematic on how to think about board effectiveness, constantly refreshing the board to make sure the right minds and approaches are sitting around the table. The way boards have run over the last 20 years is not the way they need to run in this environment.”

Boards, he adds, have to have “an increasing ability to pivot.”

In a Trump era, there needs to be a shift in how boards think, but at the same time they can’t lose sight of what ultimately drives their work, according to governance experts.

“The administration is such a paradox,” explains David Wise, Sales Leader, North America for Korn Ferry Hay Group. “On the one hand President Trump emerged as a populist candidate, but on the other hand he’s clearly anti-regulation. There’s a clear and dynamic tension between those two things.”

The paradox, he says, makes reading the political tea leaves even harder.

What is a constant, however, is that the power still lies with shareholders, he notes. “They have more impact than we have ever seen in the modern era.”

As a result, he continues, “I wouldn’t focus too much on regulations but on shareholders who are going to hold boards accountable irrespective of what may happen. They are the ones who vote directors in or out. Congress doesn’t do that and the White House doesn’t do that.”

And boards, Duke’s Cox adds, are going to have to change where they spend their valuable time. “At the board level, someone’s got to be paying attention to how the business is going to be impacted by challenges going forward — the new dynamic.”

While there is indeed a new dynamic in Washington, company boards have faced powerful windstorms before.

In every significant political reorder, DSW’s Eisenman says, changes are going to occur so “you have to be agnostic about the source of change and the way it’s happening, and just try and understand what’s going on in the marketplace.”

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