How to Transform an Outdated Board

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Creating a board of directors is not a one and done activity. As a business grows and the business environment evolves, boards often need to be revitalized and transformed to adjust to the new realities. This is especially true for larger, multigenerational family businesses who are trying to professionalize their family business governance. Landsberg (2022) found that “very few family companies have programs in place to develop, vet, select, and assess” family members on the board. As part of this professionalization, membership on the board will expand from family members to include nonfamily members.

These more independent and diverse boards can bring their expertise and objectivity to improving the decision making and to engage in succession planning. Combining outsiders with family members on a board can develop organically when times are good. However, when a family business’s performance is being challenged, the makeup of the board becomes more critical.

The renewal of a board of directors has been garnering research interest in terms of make-up, term limits, and size (Crittenden et al., 2017). For family businesses in particular, experts emphasize the importance for board members to understand their roles and responsibilities, to routinely evaluate the board’s effectiveness, and to “embrace necessary endings” when a board member is no longer contributing (Binz Astrachan, Astrachan & Kormann, 2021a; Binz Astrachan, Astrachan & Kormann, 2021b).

These issues are very important, but what has been less discussed are the challenges of getting a board of directors to make changes to itself: How can leadership get board members to vote for change that may not be in their self-interest but that would be better for the family business? This article deals with an issue that is becoming increasingly fundamental to the continued and future success of family businesses: how an existing board of directors can perform surgery on itself - transforming its structure and orientation as needed in response to competitive pressures, even at the expense of some of its most influential members.

As consultants, we have worked with several boards that needed to be restructured. The companies were focused on radically changing the size, structure, membership, and orientation of their boards of directors -- in other words, changing the composition and recruitment within the board’s governance framework. The boards were the fountainhead of strategic policy for the organizations and therefore a critical element in their success, so they needed to be strong and effective.

However, boards can be confronted with a number of issues beginning with the dominance of insiders. When this happens, there can be little if any diversity of thinking, skills, and perspectives about the marketplace, and as a result the family businesses can experience narrow decision making. Another common issue is that some board members are more concerned with self-interest as opposed to what is best for the family business. This inevitably generates conflicts that often dilute the board’s leadership capabilities.

To address these challenges meant setting in motion a process to:

- Assess the organization’s key problems.
- Analyze the board’s collective shortcomings.
- Evaluate the pluses and minuses of different options for overhauling the board to correct these shortcomings.
- Design a new structure for the board that would enable it to function more effectively.
- Convince enough members of the existing board to adopt the new structure.

The end results were smaller, more streamlined boards...
that were better positioned to provide the kind of leadership that the organizations needed and less subject to pressure from the private agendas of certain members. Needless to say, this was anything but a simple task, since members of the board had to approve the changes and many of these changes affected them directly. In short, the design of a new board may have been a necessary strategic condition, but it was by no means sufficient by itself. Equally important were the tactical actions to win support from enough existing board members to assure that the new board would, in fact, be approved and implemented.

How One Board Transformed Itself
The following is an example of how the board changed itself at one company. A financial crisis made this necessary, since revenues were not growing with expenses. In cutting the organization’s expenses, questions began to be raised about the effectiveness of the board. A consultant was engaged, and through interviews found that many people felt that the board was non-productive and non-focused, with many board members perceiving board service as something akin to a lifetime career. The consultant found strong consensus that the company needed to be revitalized. The board Chair knew he had to engineer the organization’s turnaround. His agenda included creating committees with accountability for specific tasks and insisting on firm delivery dates. He knew that this turnaround had to begin with the Board itself and would have to involve some significant changes. One of these involved creating a Finance Committee with someone who had a strong grasp of fiscal reality. Another was to establish a Strategic Committee of the Board. A third was to create a Special Committee on Ethics and Governance that was charged with drafting stronger conflict of interest regulations and disclosure forms for Board members. Working closely with the Board’s Strategic Committee to help assure that “structure followed strategy,” and drawing on the work of the consultant, they designed an “ideal” board that would eliminate the problems inherent in the existing board and be able to provide the kind of strategic leadership the company needed.

The newly designed board had three important features.

Smaller Size
Their ideal board had many fewer seats. This was consistent with the prevailing trend among similar organizations towards smaller and more focused boards whose actions were more transparent and accountable. Although research suggests that family business boards should be between 5 and 10 people (Peake, 2018), we have found that even boards within this range may be ineffective due to non-performing members.

Functional Orientation
Several senior managers asked a group of industry mavens to meet with the existing board and talk about the industry and the competitors and how the client requirements were changing. It was apparent to some of the board members that several other board members had no clue in how the business worked and brought no relevant experience to the board. They then started to work on developing new criteria for board membership. The focus was on senior management business experience and a unique understanding of the marketplace.

Term Limits
Board service for each member would be limited to two consecutive terms, which put a limit on the number of consecutive terms one could serve. This would ensure the necessary turnover in ideas and experience as new members became part of the board on a regular basis. This staggered the departure of board members so as to minimize disruptions and maintain some continuity.

Getting the Board to Adopt the Plan
An ideal board could become real only if it were formally adopted by the existing board. And adoption required yes votes from a two-thirds majority of existing board members. So, the issue of implementation became all-important. When the board restructuring was first presented at a board meeting, it was met with resistance. To gain enough votes, the following steps were taken.

Reducing Through Attrition
The Strategic Committee agreed among themselves that the implementation plan should be built around the fact that board member terms overlapped. If seats that became vacant were not filled (and then eliminated), most of the reduction in the size of the board could be accomplished without forcing any existing members to resign before their terms had expired. This user-friendly approach became an important selling point among the full board and greatly eased the plan’s acceptance.
Lobbying the Swing Voters
The next task for the committee’s core members was to mount an intensive sales campaign to assure the necessary two-thirds majority for board restructuring at the next meeting. In the interests of efficiency, this campaign focused on swing-vote board members and made extensive use of one-on-one contacts through phone calls, emails, and face-to-face meetings.

To be efficient, the committee knew that they had to focus on existing board members who were most likely to oppose restructuring. The committee knew that certain members had the most to lose personally from a board restructuring. If enough of them recognized this danger and chose to band together in a voting bloc, they could prevent the board from adopting the committee’s restructuring proposals. Therefore, the committee realized that a key tactical approach to win enough votes for its proposals would be to prevent such a bloc from forming. They sought to do this by giving their proposals a “good guy” image of doing what was best for the company, which would make voting against them seem obstructive and self-serving; and by diluting the “common cause” attraction of the voting bloc through strong one-on-one emphasis to relevant Board members about how a revitalized company could enhance the benefits for all of the board’s members. The change agents also had to be willing to “lead by example” in that they were subject to removal by term limits.

Conflict-of-Interest Disclosures: The Secret Weapon
Perhaps the most potent tactical weapon that the committee had was its control over the Conflict-of-Interest process. In order to enhance transparency, the new disclosure form that each board member had to fill out annually required each member to clearly specify any employment or financial interest that they or a member of their family had in the company’s operations that could lead to conflicts of interest. Ethics regulations required board members to recuse themselves from voting on any actions in which their disclosure forms revealed significant conflicts of interests.

Clearly, no board member could refuse to fill out a disclosure form even if its contents revealed so many conflicts as to preclude them from voting on most board actions. For a number of board members, this was obvious “handwriting on the wall” that their ability to promote business for their firms within the board environment would be materially curtailed. Yet it became increasingly apparent to most of these members that they could not vote against the Committee’s proposals with a straight face. So from the Committee’s perspective, the desirable became the inevitable.

The "Father Confessor"
Another important influencer for changing the board structure was the President and CEO. Unlike what had become the norm in so many private corporations, the company’s CEO did not dominate the board. Because of this, the CEO found opportunities to become something like a personal “father confessor” for individual board members – someone who always had time to listen to them in private conversations and help them find solutions to the problems they discussed with him. It was therefore inevitable that a number of board members who were initially undecided about board restructuring turned to the CEO as a trusted sounding board for their personal concerns about the pros and cons. While he made no secret of his personal support for board restructuring, he went out of his way to avoid coming across as a “salesman” for the concept in these conversations. Instead, by asking the right questions at the right time, he helped many board members reach their own conclusions about the necessity for board restructuring if the company was to turn itself around.

The board did vote to restructure itself and this specific example, among several experiences, indicates that it is entirely possible for an existing board of directors to remake itself in significant ways. But this is more likely to occur if the following conditions are in place:

- The organization in question is experiencing problems severe enough (preferably some of which involve fiscal issues) for many of its stakeholders to regard it as constituting a “crisis.”
- The design of a restructured board is formally made the responsibility of an appropriate board committee (such as its Strategic Committee), which may have to be created to take on the task. The design of the ‘ideal’ board is the all-important first step since there has to be something positive and radical to sell to the rest of the board.
- The need for effective collaboration among all participants has to be treated as more than a vague abstraction. This means constant
emphasis on maintaining trust and open communication, establishing a common vision among people with diverse backgrounds and agendas, and keeping everyone’s eye focused on the goal. Strong, pragmatic leadership in an atmosphere of candor and flexibility is essential if this is to happen. This group behavior is important and requires constant feedback.

- The tactical issues of gaining support for a restructured board are at least as important as the strategic issues relating to its design.
- The board chair should take the lead in pushing for change and be committed to bringing it about.

Because family businesses deal with changing environments, as all businesses do, and because younger family members are looking to take over the business, family business boards are not static. They need to change. In our experience, effecting a change in a board’s structure is more challenging than creating the original board. But it is doable with the right strategy and a lot of hard work.

References


