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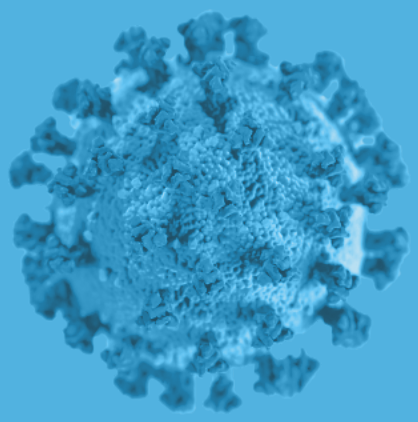

Future focused: governance developments on the COVID-19 journey

Directors in Australia, the UK and the US shared with us the experience of their boards during the past 6 months of the COVID-19 pandemic. We outline some positive developments for corporate and not-for-profit governance.

by

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When you are learning to ride a bike, you quickly learn that it takes a fair bit of wobbling and falling off. Success requires building skill and being persistent.

The next challenge is riding in unfamiliar conditions. If the brakes fail when you are going downhill, you quickly discover that you have to stop worrying about the brakes. Steering is all important. You need to look ahead.

These are appropriate analogies for the situation that boards have experienced in 2020. The situation is unfamiliar to everyone, but well-prepared organisations have been able to maintain their momentum and strategic focus.

Structural rigour in their governance and the broad expertise of individual directors have helped see them through to this point. It has helped them work across the detail, rather than becoming trapped within it. Shared experiences from other boards has improved decision making. Looking ahead is helping them to steer towards the future.

We spoke with directors of major organisations listed on the ASX, NYSE and LSE, as well as those on the boards of private groups, government organisations and not-for-profit entities. We wanted to understand the impact of COVID-19 on their organisations' governance. Particularly, we wanted to understand the impact of COVID-19 on the behaviour of boards and directors.

We sought US and UK perspectives in order to understand the experience in countries under far greater strain from COVID-19 than has been Australia's experience to date.

Our interviews took place in June and July 2020. As a result, our findings come from directors experiencing the pandemic at various stages. Some organisations were relatively stable, with their countries having experienced a first wave. Others were operating bereavement call lines to support staff through the loss of family, friends and colleagues. We thank each of our participants for their generous and open approach in sharing their perspectives.

The international experience

Pamela Packard, President of the National Association of Corporate Directors New York Chapter, discussed with us the stark reality faced by boards in the United States during COVID-19.

Some companies with "long-tenured" directors have recognised that they are in a high risk situation. They identified age diversity as a specific succession requirement.

"The whole board is in a high risk category."

The priority has been the health of employees and staff, followed by "cash as king".

Yet, in this environment, boards are also placing a greater focus on corporate purpose, taking the lead from the US Business Roundtable's August 2019 Statement on the Purpose of the Corporation.

Boards are testing the validity of their organisation's purpose - should they deliberately pursue it or revisit it completely? How is that purpose communicated to stakeholders?

Similar themes came from our discussions with Gordon Hardie, a non-executive director of Owens Glass Inc., a global manufacturer of glass packaging for the beverage and food industry, listed on NYSE. He has also joined LSE-listed Greencore Group PLC, a leading convenience food manufacturer (including ambient, chilled and ready-meals).

The pandemic brought to the fore the importance of purpose in both companies in galvanizing all stakeholders to fight the pandemic in a cohesive and aligned way. This sense of purpose allowed for extraordinary agility across the supply chain in both companies in the face of the pandemic, delivering significant changes in days or weeks that otherwise might have taken months or longer to deliver.

For Greencore, its focus was "keeping our people safe and feeding the UK". Its priorities were to look after its people while keeping its food plants functioning for the sake of communities.

"Both boards and management teams had as their top priority keeping our people and our customers safe and went to extraordinary lengths to do so."

His explanation of the scale and scope of the impacts of the COVID-19 in the UK and the US were the most direct and affecting of all our interviewees. He spoke of the depth of what was required to support staff, from the strains of management to bereavement support lines for those losing family, friends and work colleagues. A salutary reminder of what our lives could look like.

Our key findings

Our key findings related to:

- **governance structures**, including the importance of purpose and values as a governance tool, new perspectives on risk and disciplined information flows to support decision-making;
- **people**, including the bench strength and resilience of both boards and managers, with impacts on concepts of succession planning; and
- **governance of operational settings**, including how relationships with management have been re-set and a greater confidence in the acceleration of execution pace.

We discuss these findings on the following pages, and offer some questions the board can ask to test and adjust its organisation's approach.

The key developments are extracted below.

Key developments for governance structures

The importance of corporate purpose

Clearly articulated values and well-defined corporate purpose have been critical to effective decision-making, particularly for large organisations with many stakeholders.

A more nuanced approach to risk frameworks

Organisations are revisiting risk, including risk correlation and risk lead indicators.

Board and management succession have been elevated as risks requiring mitigation.

Information flows

More can be done with less. The requirement for timely and targeted information and single-issue board meetings has led to tighter board papers, with more actionable insights.

Where more detail is required, there is a healthier dynamic when challenging information with management.

Key developments for people

Board strength and resilience, including succession planning

Boards need to give thought to their own bench strength.

Given the decreasing shelf-life for skills currency, non-executive directors may find that governance will evolve in response to the skills of today's executives. This heightens the need for age diversity on boards, and reverse-mentoring. It also highlights the value of director fit and agility, in working beyond their historical skills area.

There was appetite for experience from other board roles to be readily shared and given weight.

Management strength and resilience, including succession planning

Boards will need to actively monitor management fatigue and develop strategies to ensure management have opportunities to refresh and renew. This is both for the mental and physical health of management, as well as diminishing conduct risks for the organisation.

Succession planning for management has moved from the notion of a 'key person' to the concept of building resilience in teams. This was highlighted by the US and UK directors we spoke with, where operations were at risk of illness striking the management team.

In the not-for-profit sector, CEOs are being asked to develop and demonstrate sustainable business models, where there had previously been a reliance on limited sources of revenue.

Key developments for governance of operational settings

The re-setting of how the board and management interact

Board and individual director interactions with management have increased, resulting in a more open way of communicating and leveraging each other's skills and experience. Management is gaining a better understanding of directors' technical skills, experience from multiple directorships, and from managing through previous crises as senior executives.

Execution pace and quality

Internal barriers to development and innovation (at board and management level) have been reduced by necessity. This has taught boards and management to have the confidence to implement developments quickly and with a solid level of performance, perfecting them later.

Boards are testing risk settings for operations, with a focus on making them scaleable and modular.

We intend to follow up with our participants as time goes on, in order to monitor the ongoing impact and evolution of board processes in this new landscape.

See details of our findings and some suggested board questions on the following pages.

Governance structures

The importance of corporate purpose

Key developments

Clearly articulated values and well-defined corporate purpose have been critical to effective decision-making, particularly for large organisations with many stakeholders.

Global thinking about corporate purpose has heightened. The British Academy's project on the future of the corporation and the US Business Roundtable's August 2019 *Statement on the Purpose of the Corporation* are now being tested and lived.

Overall, we found that organisations considered themselves better able to cope with the unfamiliar where they had established frameworks for decision making and a clear concept of purpose.

This helped boards balance considerations such as how they would allocate their capital during this period. One chair described it as prioritising staff and community safety, cash demands, service levels and - expressly at the very end of the priorities - "will you make money?"

Where boards and organisations had undertaken significant work on their values and purpose, they were able to apply that work when making choices at a time of rapid change and high risk. There were ethical issues around balancing different elements of that purpose, dealt with as open discussions about that balance, rather than values being a sub-text.

> *"In the last 3 months I have had more thank yous [from clients] than in the past 5 years."*

This included broader ethical conversations about the impact of the pandemic on stakeholders. This ranged from the impact on retirees of lower dividends to the impact on the use of suppliers with workers in high-risk countries. Concerns were also expressed that organisations which were adapting well did not want to appear to profiteer from the environment.

Questions for boards on corporate purpose

Have you applied your organisation's values in your decision making? Are they streamlined enough to be applied? Do they need revisiting?

Have you been acting in accordance with your organisation's purpose? Consider if you have been in survival mode, stabilising, or planning for the future.

Is your corporate purpose still relevant? Are your values fit for purpose? What are the implications for your business model?

A more nuanced approach to risk frameworks

Key developments

Organisations are revisiting risk, including risk correlation and risk lead indicators.

Board and management succession have been elevated as risks requiring mitigation.

Boards are re-thinking risk in light of the many system failures during the first phase of the COVID-19 pandemic.

> *"What else of an existential nature could affect the organisation and how does that affect how we think about risk?"*

Although pandemics were not generally in boards' risk registers, mature approaches to business continuity planning permitted existing risk planning scenarios to be adapted. The critical factor became not how a risk was categorised but how quickly a team could be raised to respond.

> *"It's about how quickly you can spin up a team."*

Risk correlation will become a stronger theme. This relates to the impact of multiple risk events, as well as the need to better identify lead indicators for risk. Factors such as the incident volume of low-value risks can act as an early warning of trouble ahead. Individually and collectively directors are revisiting how they have interpreted past indicators of future issues. New models will emerge.

> *"We have to look at how risks are correlated. Some risks can be the canary in the coalmine (e.g. small bad debts going up) that can be an indicator, for that customer group, of things going wrong."*

Another common concern were risks related to people. Interviewees as a whole had the physical and mental welfare of employees front-of-mind, with management fatigue a major concern.

Some raised the issue of a lack of age-diversity on the board, with the whole board in a high-risk category for COVID-19.

One organisation ensured that the chair, "stand-in chair", CEO and "stand-in CEO" met regularly, so that all were in the loop in the event that the chair or CEO fell ill.

Questions for boards on risk

Does your risk management framework handle risk correlation? Can you stress test it for multiple coinciding risk events?

Have you revisited your risk lead indicators? For example, are you considering incident volume for low-value risks?

Have you considered revising 'key person' risk to broader and deeper board and management succession planning? Are you actively using it as a risk mitigation strategy e.g. involving understudies in key meetings?

Information flows

Key developments

More can be done with less. The requirement for timely and targeted information and single-issue board meetings has led to tighter board papers, with more actionable insights.

Where more detail is required, there is a healthier dynamic when challenging information with management.

Inefficiencies in information flows have been highlighted, but the conversations around them have in some ways been easier than usual.

> *"I ask management: 'What are the actionable insights, so I can be more useful?'"*

Organisations have generally sought much shorter and simpler board papers (including 1-pagers) during this period. This has been necessary for speed of operation.

Boards have assisted with strategic settings, then left matters to management so that they could be fast and flexible in making operational decisions.

The exception to brevity appears to be in financial reporting, which has become more detailed as cash-flow forecasting and monitoring are more salient than ever. Some organisations with sophisticated financial reporting and monitoring did not have readily accessible cash-flow information - a sign of the sudden shift in economic conditions.

By contrast to the trends for more disciplined board papers, some new directors on-boarded during this period were given licence to be more active in their own induction and were given greater access to management and detailed information. This was especially so for new directors on audit committees.

Without the ability to "walk the floor" to pick up general information, or to have incidental discussions (or to review and reflect) during coffee breaks or meals, directors have been finding various ways to obtain and test information, while trying not to over-burden fatigued management teams. One chair described his increased role as an intermediary. He acted as the main contact point for directors' queries, to ensure that the management team was able to focus where necessary.

More interactions with management are also helping to re-set the tone for challenging management information. After the APRA inquiry into the Commonwealth Bank of Australia, the approach to challenging information from management has been dictated by "don't tell me, show me". In our experience, this has sometimes been perceived as a lack of trust, and has heightened tensions with management. It has also resulted in a greater volume of material being produced for the board, rather than greater insight being displayed in board papers. In contrast, the COVID-19 experience has created better engagement by management in information gathering and testing, within tight timeframes, resulting in a mutual focus on better-quality outcomes.

Questions for boards on information flows

Do your board papers contain actionable insights? Are they too long?

Are you being clear about your purpose for information, for board papers and in other interactions with management? Communicate the 'why' in order to focus and engage management. Are you challenging management openly and positively?

How are you gathering and testing information when you can't walk the floor? Have you identified critical lead (and lag) indicators in order to receive prompt information for non-financial risks (including conduct risks)?

Do you have sufficient lead indicators for culture? For example, in a dispersed workforce, absenteeism is not a lead indicator.

Will your lead indicators be sensitive to cultural changes in operating environments, as the organisation moves out of crisis and into stabilisation phase?

How has the COVID-19 experience been different for boards?

The speed with which the COVID-19 pandemic struck globally has been unlike other recent experiences of downturns.

The global impacts of the pandemic have challenged the just-in-time inventory and business processes that modern organisations rely on for costs efficiencies.

Government interventions in all countries have been unexpectedly quick and deep.

Where governments have been slower to act, organisations have been unable to influence the course of the pandemic on their staff and customers.

Boards cannot anticipate the end point of the pandemic or its economic after-effects. In the event of development of an effective vaccine or vaccines, the success of its implementation will be affected by the rationale to the vaccine or vaccines (e.g. immunity for the vaccinated individual, with or without neutralising their ability to be infectious), access to the vaccine and the public health settings of individual countries.

People

Board strength and resilience, including succession planning

Key developments

Boards need to give thought to their own bench strength.

Given the decreasing shelf-life for skills currency, non-executive directors may find that governance will evolve in response to the skills of today's executives. This heightens the need for age diversity on boards, and reverse-mentoring. It also highlights the value of director fit and agility, in working beyond their historical skills area.

There was appetite for experience from other board roles to be readily shared and given weight.

The quality of individual directors has been similarly highlighted by this crisis. Interviewees said they soon saw who could do what on the board, and changed their operating style in order to effectively execute their oversight role while supporting management. Capable directors included those who were able to deal quickly and assuredly with matters, yet also pause and test situations when required. Other directors did not step up as well to the challenges.

> *"You need people who can catch and throw. They can resist the flow of the river when they need to, and go with the flow when it is required."*

Our research suggested that boards are now looking for more texture in their consideration of board skills, compared to their existing method for identifying skill gaps.

Director fit was identified as a critical element for boards. Some skills from executive experience become rapidly outdated (even in a short time frame). It is more important to bring agile thinking and depth of experience to the table.

Board diversity should include diversity of age, as well as gender, ethnicity, experience, and skills. The speed of change has meant that non-executive directors who have left the executive suite only a few years ago are becoming aware of the lack of currency of their skills.

This may lead to a push for age diversity on boards, so that the valuable strategic skills held by more experienced directors are coupled with more currency of skills in younger directors, forming a bridge to management. Senior directors can mentor younger directors; the younger can develop the more senior directors by reverse-mentoring. This brings agility, to apply existing experience into new environments and to solve problems outside directors' historical areas of expertise.

While we do not endorse over-boarding, a number of participants also highlighted the benefit of non-executive directors having experience from multiple boards. The ability of boards to respond to specific challenges was aided by the perspective of non-executive directors with access to other organisations and their approaches. Examples included:

- The value of having a member who was also chair of an organisation with Chinese operations. That experience provided valuable lead time to his other boards to comprehend the enormity of COVID-19.
- The speed of response when needs arose e.g. to identify quality consultants that directors had experienced elsewhere.

Interviewees called out as strong chairs those who have had the ability to frame the questions to facilitate discussion, rather than framing the discussion itself. However, some chairs told us they felt they needed to be more directive than usual in the intense early phases of the pandemic response.

Strong chairs also ensured participation of all members, in order to overcome the limitations of using video technology. This was noted as a particular challenge for not-for-profit boards, where younger representative members appeared to feel less comfortable to contribute.

Questions for boards on board strength and resilience

Have you considered the COVID-19 risk profile of your individual board members?

Have you made arrangements to mitigate risks of attendance at meetings? Are you using 'understudies' at critical meetings?

How is the board managing its own interactions and culture?

Are directors making unreasonable demands for information? This could be an indicator that the director is not coping, as well as overloading management.

Are the chair and the committee chairs leading and framing the questions in order to promote strategic thought for operational issues?

Are information flows to individual directors uneven? Who is in the 'kitchen cabinet' and who is not? Why? How can this situation be improved?

Is your board the right size to balance the need for skills, participation levels and workload?

Do you have a board structured for the future? Do you have age, gender and ethnic diversity as well as skills diversity, to ensure depth of talent and opportunities for mentoring and reverse-mentoring?

Have you investigated the operational style of board candidates? Can they work effectively beyond their historical skill areas?

Are board members able to share valuable experience from other companies and sectors?

Management strength and resilience, including succession planning

Key developments

Boards will need to actively monitor management fatigue and develop strategies to ensure management have opportunities to refresh and renew. This is both for the mental and physical health of management, as well as diminishing conduct risks for the organisation.

Succession planning for management has moved from the notion of a 'key person' to the concept of building resilience in teams. This was highlighted by the US and UK directors we spoke with, where operations were at risk of illness striking the management team.

In the not-for-profit sector, CEOs are being asked to develop and demonstrate sustainable business models, where there had previously been a reliance on limited sources of revenue.

The quality of senior management was highlighted.

The majority of interviewees praised their management, while also expressing concern about management fatigue. Similarly, this led to discussions of the depth and breadth of management succession planning which would be required.

> *"When there is light and fire, you see what you always had."*

Praise was also given to other staff. One interviewee felt that teams' ability to perform had historically been underestimated by senior management, and this had been one of the barriers to project execution.

Poor quality was also highlighted, particularly in the not-for-profit sector where business models had not been tested and CEOs may operate the organisation as an autocracy.

One consequence of empowering management teams to be nimble was that some felt unsupported. They felt that the board had left them to deal with the consequences of the board's choices, and to be the front line for difficult decisions.

While there were no unexpected board resignations during this period, there were some surprise resignations from management.

Interviewees expressed their deep concern about the pressure upon management during this period, and the fact that there was no clear end to operating in this environment.

> *"I worry about the fatigue factor for senior executives…For senior people, life changed."*

The military has a concept of 'operating tempo', which prepares forces and commanders for the heightened level of operations when deployed for months at a time, available 24/7.

By contrast, management teams are more used to sporadic increases in workload, such as during a transaction or in reporting periods. They are not prepared for sustained periods. There is no clear end date for COVID-19 or its economic after-effects.

> *"My guidance for the board has been to get out of the road on operational matters - management needs time and space to move quickly."*

Where chairs had healthy, interactive relationships with management, they were able to maintain the necessary level of connection to support management strategically, while permitting management flexibility operationally.

Questions for boards on management strength and resilience

Is your ideal crisis CEO different to your ideal business-as-usual CEO? What qualities differentiate them? Given the indefinite length of COVID-19, what needs to be in your business-as-usual CEO's toolkit? Is your management bench strength capable of more than business-as-usual?

How deep is your management succession planning? Should you use the concept of "stand ins" who may or may not be successors, to future-proof the team for short term as well as long term disruptions?

Is your team using COVID-19 as an excuse for underlying issues with poor execution e.g. delayed customer service?

Is your management team coping with fatigue? Can you encourage the CEO to lead by example, such as taking a short burst of leave for 7 days after the scheduled board meeting?

Does a rest improve management operations?

Is management's refusal to take leave or blocking of information flows creating or masking risk issues?

Governance of operational settings

The re-setting of how the board and management interact

Key developments

Board and individual director interactions with management have increased, resulting in a more open way of communicating and leveraging each other's skills and experience. Management is gaining a better understanding of directors' technical skills, experience from multiple directorships, and from managing through previous crises as senior executives.

Non-executive directors are traditionally very careful to strike a balance between open interactions with management and management contact levels that may impede the ability to oversee that executive. Directors do not want to be so involved in an operational issue that they are no longer able to exercise oversight, or that there are uneven information flows to some board members compared to others.

A consequence of the pace of execution during COVID-19 has been an increase in management-driven engagement with the board. Interviewees noted this as a positive, with barriers to contact reduced.

Also, management are learning to leverage the skills of their directors. In addition to their technical areas of experience, board members with multiple directorships are sharing more information with management. Directors who were senior executives through previous downturns have unique insight to managing through crises.

Relationships with those deeper within the staff teams has also been enhanced.

> *"Some of the artificial boundaries between management and the board are challenged."*

While people told us it was harder to read the body language in on-line sessions with executives, we hope that having more interactions with executives has filled some of the gaps arising from directors being unable to "walk the floor". Ideally, it could lead to fewer surprises for the board, as management has the opportunity to be more open when communicating live issues.

It may also result in more mentoring of executives by directors, and potentially in reverse-mentoring. As noted by one chair, the shelf-life of executive skills is becoming shorter, and directors will need to develop their governance skills in response to the new skills of executives.

Questions for boards on re-setting of board and management interactions

What is the profile of your management team? Have they been senior executives during previous crises?

Does management appreciate the experience of board members as senior executives during previous crises?

Does the board have a deliberate strategy or insight into managing interactions of directors with executives, to maintain a healthy level of interaction, without overloading management with contact or losing board oversight? This should be re-assessed as circumstances change.

Are board members focused on sharing valuable experience from other companies and sectors?

Execution pace and quality

Key developments

Internal barriers to development and innovation (at board and management level) have been reduced by necessity. This has taught boards and management to have the confidence to implement developments quickly and with a solid level of performance, perfecting them later.

Boards are testing risk settings for operations, with a focus on making them scaleable and modular.

COVID-19 made organisations reduce lead times and launch developments, rather than only launching the refined product. We heard multiple stories of how businesses responded within days or months to produce digital outcomes which were previously thought to require 2 to 3 years to be implemented.

> *"We have been moving on 'good', and perfecting on the way through, rather than waiting on perfection. Strangely, this has bolstered the confidence of the management team."*

Senior management found increased confidence in themselves, as well as being surprised at their own teams' ability to execute.

Some of this acceleration of development was necessary to save business models. For other organisations, the acceleration was to service urgent needs of its customers and other stakeholders. Several directors stated that they had not appreciated prior to the pandemic that their organisations were essential services; they now realise that their services are part of the architecture of supporting workforces and communities.

Questions for boards on execution pace and quality

What have you done successfully at speed and how can you replicate that as business as usual?

What don't you want to revert to? Restructure while you have the opportunity.

How scaleable and modular are your operations, to respond rapidly to ongoing change?

Conclusion

We started thinking about this topic from the perspective of what latent governance issues were being exposed by COVID-19.

As we spoke to more directors, including those with international perspectives, our focus shifted. We wanted to find positive impacts from the pandemic on governance that would support and strengthen organisations and communities at a time of ongoing and extreme change.

This crisis has re-set how organisations and their boards and management operate. It has given them a new perspective, one that is more externally focused. It has reinforced the importance of corporate purpose and of balancing and protecting the interests of multiple stakeholders.

When threatened by the scale of the detail and its difficulty, boards and management are doing their best to focus on the bigger picture – for their organisations and their relationships with each other.

About the authors

Karina Marcar is the founder of Brabourne. Her board review and governance experience ranges from the S&P/ASX 100 to public institutions, in sectors spanning financial services to infrastructure. She understands commercial drivers for Australian and multi-national businesses. She is people-focused and builds trust with interviewees in order to draw out critical themes for how boards can enhance their performance.

Her skills working with boards are enhanced by her previous career of 25 years in mergers and acquisitions and corporate law in Australia and the UK, including over 17 years as a partner at Johnson Winter & Slattery and Blake Dawson Waldron (now Ashurst). At the time of leaving legal practice, Karina was listed as a leading lawyer for Corporate Law and Mergers and Acquisitions Law in *Best Lawyers Australia*.

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Brian has established a number of very successful companies. He was a founder of the Calan Group, a health-sector investment bank in New Zealand, of which he was Executive Chairman. His achievements include the launch and listing on the NZX of Calan Healthcare Properties Trust, a healthcare property REIT (NZX:VHP) from start up to $NZ225 million, as well as private equity investing in the health sector.

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