

BRIEFING NOTES

Five Theories on Contemporary Board Governance

CFAR's work in governance spans both corporate and not-for-profit organizations across a variety of industries and professional fields. Boards engage us when they are facing a strategic question, looking to evaluate and improve their structure or performance, or need help with a leadership transition. We have a deep appreciation for the importance of governance and the challenges faced by trustees and directors who are willing to take up this demanding work. We couple our own practical expertise with the ideas and frameworks of leading thinkers on the topic of governance. In this briefing note, we present a summary of key findings from the work of five authorities on the role of boards and board governance:

1. William Bowen: distinctions between not-for-profit and for-profit boards
2. John Carver: not-for-profit governance
3. Richard Chait: management and governance within not-for-profits
4. Ram Charan: the strategic role of boards
5. Jay Lorsch: corporate governance

Overview

The following table highlights the focus of the historical versus contemporary roles for boards of directors. These observations are based on the concepts presented in the works of the authors named above, and are used to illustrate the shift in current best thinking of board governance.

Historical Role: Based on the personal experiences and connections of board members.	Contemporary Role: Based on comprehensive industry knowledge and research.
With a focus on...	With a focus on...
Regional trends	Global trends
Costs	Investments in the future
Front-line issues	Executive-level issues
Evaluating an organization based on achieving financial goals	Evaluating an organization based on achieving strategic initiatives

William Bowen

William Bowen is an expert in boards from his own service on five corporate boards, six non-profit boards, and in two CEO positions. In his writing, he pays particular attention to the distinction between for-profit and non-profit organizations, with the hope that contrasting types of organizations can create better insight and effective solutions to governance challenges. The following is a summary of selected themes and key points from Bowen's book, *Inside the Boardroom: Governance by Directors and Trustees*.

- ▶ **The role of the board is significant.** Bowen starts by emphasizing that in order to increase effectiveness, both for-profit and non-profit, organizations need to recognize the significance of their leadership board.
- ▶ **Boards exist to encourage the development of an institutional sense of purpose and community.** Bowen's discussion makes recommendations on the general functioning and mechanisms of board governance, along with a list of 20 norms of practice. These "presumptive norms" range from organizational size, the role of the board chair, and frequency of meetings. These are "applications to be tailored to the circumstances of the two sectors."
- ▶ Six general functions of boards according to Bowen:
 1. To select, encourage, advise, evaluate and if need be, replace the CEO.
 2. To review and adopt long-term strategic directions and to approve specific objectives, financial and other.
 3. To ensure, to the extent possible, that the necessary resources, including human resources, will be available to pursue strategies and achieve objectives.
 4. To monitor the performance of the management team.
 5. To ensure that the organization operates responsibly as well as effectively (following policies and procedures that comply with legal and ethical standards).
 6. To nominate suitable candidates for election to the board, and to establish and carry out an effective system of governance at the board level, including evaluation of board performance.

Bowen provides a nuanced view of the relationship between the CEO and the board through his comparison of non-profits and for-profits:

- ▶ As is the case in for-profit organizations, the CEO of non-profits can have too much freedom or be given too much opportunity to "rest on their laurels."
- ▶ As is the case in for-profit organizations, non-profit boards are tempted to do the job of the CEO. Nonprofit CEOs can be reluctant to lead as a result.
- ▶ Nonprofit boards are more important to the organization than for-profit boards—non-profit boards typically have more decision-making impact and more room for judgment.
- ▶ A partnership approach between the CEO and board yields significant benefits. Nonprofits should strive for both the flexibility and yet rigorous application of norms to develop a specialized structure of governance.
- ▶ Nonprofits should create machinery that allows directors to focus on substance and not to be preoccupied with process.

John Carver

John Carver, an expert in non-profit governance, has designed a results-oriented approach to board governance through his policy governance model. The following is an overview of several of the main themes of Carver's policy governance model taken from his book, *Reinventing Your Board*.

- ▶ **The policy governance model requires that the board establish an explicit set of policies used to govern the organization.** Under Carver's model, the board's primary responsibility is to represent the organization's stakeholders by establishing this set of policies. The policies that the board establishes can be divided into two general categories: Ends and Means.
- ▶ *Ends policies* are used to define the strategic objectives of the organization. These policies reflect the benefit, difference, or outcome in members' lives that the organization is attempting to produce and the value-added implications.
- ▶ *Means policies* are established by the board to act as the vehicle for achieving the organization's Ends policies. Means policies include governance process, executive limitation, and board – CEO linkage policies. Under this model, the board defines, delegates, and monitors but does not carry out organizational work.
- ▶ Performance monitoring is conducted by measuring the CEO's progress and performance against the objectives defined by the policies. Under Carver's policy governance model, performance monitoring is done by examining whether the CEO has achieved the Ends policies while still remaining within the limitations (Means policies) established by the board.

Carver states that in the area of performance monitoring, boards often drift off course when they begin to implement the policy governance model. It is often very difficult to measure whether the CEO has achieved the objectives outlined in Ends policies.

In summary, under Carver's model of board governance, the board legislates policies that are carried out by the CEO. Carver goes on to say that the process of establishing such policies can become cumbersome and that merely implementing this model will not necessarily change the board dynamics.

Richard Chait

Richard Chait is an expert in the management and governance of colleges and universities. Chait puts forth a model of “generative” governance, which addresses the tension that has resulted from evolving roles of the CEO and Board within non-profits, wherein the Board often ends up micromanaging the organization. Chait’s model blends a rethinking of past approaches to governance with a new idea – governance as leadership – to give board members a new perspective on their role in the organization.

The following is an overview of several of the main themes from the book *Governance as Leadership: Reframing the Work of Nonprofit Boards*.

- ▶ **Boards should spend time rethinking their perspective on their role in the organization.** As the role of the CEO of non-profits has generally become a more active leader in the organization, the board has moved more toward management. This arrangement creates tension between the CEO and the board when board members start micromanaging the organization. The board’s skills and expertise are still relevant, but rethinking the role of the board can enhance their experience as a board member while increasing the board’s value to the organization.
- ▶ **The problem with boards is one of purpose.** Boards are ineffective not because they are *confused* about their role, but because they are *dissatisfied* with the role. Chait argues that board work can be exciting if the board embodies governance as leadership, which involves blending the three types of governance: fiduciary, strategic, and generative.
- ▶ **Organizations are not merely the sum of their productive and logical aspects.** A simple task-and-structure approach to governance, where boards operate in the mode of forming committees around the key business areas to ensure proper resource deployment, does allow the board to match the operational needs of the organization but can oversimplify the reality of the organization. Generative governance requires that the board understand the values, judgments, and insights of the organization.
- ▶ **There should be a collaborative relationship between the board members and executives.** Instead of collaboration based on a basic division of operational functions or developing strategy, it is both, plus a new collaboration that generates new ideas and approaches.

In summary, Chait makes the argument that using three modes of governance together will create a new kind of role for the board and will encourage more dynamic, engaging work for board members.

Table One—Three Types of Governance: Distinctive Characteristics (p. 132)

	Type 1: Fiduciary	Type 2: Strategic	Type 3: Generative
Nature of organizations	Bureaucratic	Open System	Non-rational
Nature of leadership	Hierarchical	Analytical/visionary	Reflective Learners
Board's central purpose	Stewardship of tangible assets	Strategic partnership with management	Source of leadership for organization
Board's core work	Technical: Oversee operations, ensure accountability	Analytical: shape strategy, review performance	Creative: discern problems, engage in sense-making
Board's principle role	Sentinel	Strategist	Sense maker
Key question	What's wrong?	What's the plan?	What's the question?
Problems are to be	Spotted	Solved	Framed
Deliberative process	Parliamentary and orderly	Empirical and logical	Robust and sometimes playful
Way of deciding	Reaching resolution	Reaching consensus	Grappling and grasping
Way of knowing	It stands to reason	The pieces all fit	It makes sense
Communication with constituents	Limited, ritualized to legitimate	Bilateral, episodic to advocate	Multilateral, ongoing to learn
Performance metrics	Facts, figures, finances, reports	Strategic indicators, competitive analysis	Signs of learning and discerning

Ram Charan

Ram Charan, a well-respected and seasoned management consultant and executive educator, puts forth a board-governance model which makes an argument that boards of directors must take up a more active role in working with their CEOs. He goes on to say that a board's most valuable role is as thinking partner to the CEO and that together, the board and CEO should address strategic issues facing an organization.

The following is an overview of several of the main concepts taken from Ram Charan's book, *Boards at Work: How Corporate Boards Create Competitive Advantage*:

- ▶ **The board should act as a "strategic partner" to the CEO.** Boards should engage in an active exchange of ideas with the CEO. Under Charan's governance model, the board and the CEO may work collectively in the strategic decision-making process. To do this effectively, the CEO should provide the board with a clear view of the business and its external context. Charan goes on to state that the board should not get involved in running the operations of the organization.
- ▶ **The full board should address critical business issues facing the organization.** Charan believes that a large number of board committees may be unnecessary. Committees can potentially undermine the board's unity and authority by perpetuating conflicting views represented by these committees. Although not easily accomplished, "boards should learn and act as a single entity."
- ▶ **The firm and the CEO should draw from the collective knowledge of the board.** The board should provide a source of knowledge and business expertise (i.e., company, industry, financial and organizational expertise) to the organization and its management. This broad base of expertise is essential in assisting in strategy formulation and for creating the necessary dialogue with the CEO.
- ▶ **Board members should have a mix of backgrounds and perspectives.** The board's varied expertise should be complementary and useful for the company. There should be significant consideration given to increasing the board's knowledge base during the selection process of new board members.
- ▶ **The board should conduct the CEO's evaluation and ensure a succession plan.** Board feedback is the best way to improve CEO's performance. Feedback should be an ongoing process, based on both formal and informal feedback mechanisms. Succession planning is one of the fundamental responsibilities of the board.

In summary, Charan makes an argument that the role of the board has evolved from being focused on operational, frontline, and monitoring issues to that of strategic partner to the CEO focused on executive-level issues, formulating strategic initiatives, and conducting performance evaluations.

Jay Lorsch

Jay Lorsch, an expert on corporate governance, argues that a board's primary responsibility is to be an active monitor of the CEO's and firm's performance.

The following is an overview of several of the main themes of Lorsch's governance approach taken from his work published in Harvard Business Review's January – February, 1995 issue, *Empowering the Board*:

- ▶ The board should monitor performance of the top management against defined strategic and operating targets. Under Lorsch's governance model, the CEO evaluation should:
 1. At a minimum, be performed annually.
 2. Attempt to compare the CEO's accomplishments to the organization's strategic and operating goals.
 3. Include the CEO's self-evaluation.
 4. Benchmark the organization's performance compared to other organizations.
- ▶ The board should work as a group to define the performance monitoring system. In order to be more effective in establishing a performance monitoring system, board members will need to discuss and agree on the evaluation by working as a group. Furthermore, the board needs to have comprehensive firm and industry knowledge to effectively establish its expectations.

In summary, the board should have the ability to influence the direction that management is moving in if performance, as outlined above, does not meet expectations. However, the board should not attempt to run the company—its primary responsibility is monitoring performance.

Common Themes

There are several common themes that run throughout the work done by Bowen Carver, Chait, Charan, and Lorsch:

- ▶ Boards must address critical issues facing the organization as a single entity.
- ▶ Boards should not focus on carrying out operational work.
- ▶ The evolving relationship between the CEO and the board should be acknowledged and their respective roles adjusted appropriately.
- ▶ There are distinct differences between for-profit and non-profit boards that are helpful to understand as an organization rethinks the role of the board.
- ▶ Retreats are a powerful and effective means for strategy formulation and review.

There are also significant differences among the five scholars on what role the board should take when dealing with the CEO. Figure One on the next page is used to illustrate three distinct views presented in this note on the relationship between the board and CEO with respect to the levels of dialogue and board involvement. (i.e., Carver's *Legislator*, Lorsch's *Active Monitor*, and Charan's *Strategic Partner* models).

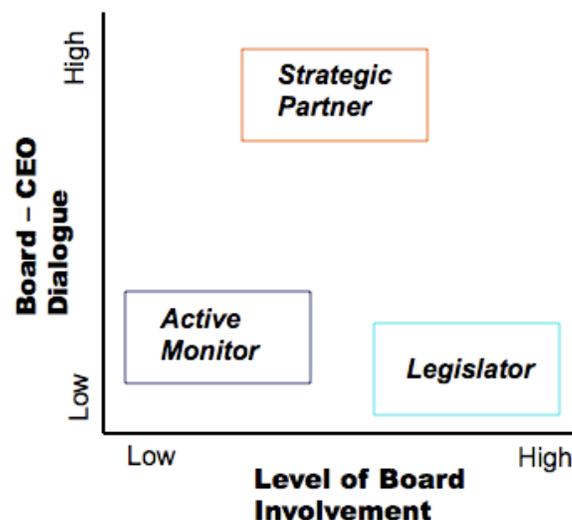


Figure One: *Contemporary Board Governance Models*

Citations

Bowen, William G. *Inside the Boardroom: Governance by Directors and Trustees*. New York: John Wiley & Sons, Inc., 1994.

Carver, John and Miriam Mayhew Carver. *Reinventing Your Board*. Jossey Bass Publishers, San Francisco, 1997.

Chait, Richard P., Ryan, William P., and Taylor, Barbara E. *Governance as Leadership: Reframing the Work of Nonprofit Boards*. Wiley: New York, 2005.

Charan, Ram. *Boards at Work: How Corporate Boards Create Competitive Advantage*. Jossey-Bass Publishers, San Francisco, 1998.

Lorsch, Jay. "Empowering the Board." *Harvard Business Review*, January – February, 1995.

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