

"Across the Board"



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Does size really matter?

By Phil Khoury, Joint Managing Director, Cameron Ralph Pty Ltd, a consultancy which assists boards to provide effective leadership, improve their performance and build positive reputations.

In a recent edition of *Across the Board* (Issue 128), Alan Cameron explored the issue of tenure of directors and of the board as a whole, with his conclusion being..." The focus should be on succession planning, to ensure accountability and fresh strategic inputs, while keeping the board at a manageable size. Perhaps size does matter, and that is a question for another day....."

The 'size' of a board doesn't often get much attention as a governance issue, but it certainly plays a role in a board's ability to produce consistently high quality decisions.

Traditional research on groups has told us that teams of people operate most effectively in numbers from 5-10 and some theorists narrow this to 8 or 9. The recent fashion among Australian listed companies has been to reduce the size of the board, with it not unusual to see boards of 6 amongst the Top 200. Even the Federal Government acknowledged this trend in two places recently: the APRA draft Prudential Standards for the Governance for APRA-regulated institutions which stipulates a minimum of 5 directors, and the National Governance Protocols for Higher Education, which stipulate a maximum of 22(!) persons for the governing body.

It is not difficult to see the attractions of a smaller Board – fewer people require less 'air time'. They are generally less expensive, more flexible, easier to keep informed, easier for the Chairman to

manage and, all things being equal, enjoy greater cohesion and quicker decision-making. Of course, it must be said that reducing the size of a board (under the guise of improving efficiency), can also be a covert way of removing under-performing or disruptive directors.

On the other side of the coin – there are many forces today that push the size of boards to be larger, including ever-expanding regulatory and compliance obligations, demands from both the market and regulators for the presence of specific skills and for sufficient numbers of independent directors. So, is it just a question of having the smallest board you can afford? It will surprise no one familiar with Cameron Ralph's approach to board performance generally to hear that our view on size is "it depends"!

The first thing we recommend to clients is to think through the nature of the decision-making tasks that the particular board must deliver. Is the organisation one in which the speed of decision-making is really at a premium? Or are the decisions at the opposite end of the decision scale - long term major investments which are betting the company? How well established is the company? How experienced are the senior executive team? Will the board be involved more or less in guiding management? As a general rule, a more hands-on board will need to be smaller to be effective.

A second consideration is the nature of the 'audience' for the board's decisions. Are there significant community risks attached to the organisation's business – environment or safety issues? Are there significant

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government or regulatory interests in the business or its outcomes? How investor or market-sensitive is the company? Is the company's target market highly diverse – or international? These factors may well make more rather than fewer directors a better structure.

The sheer workload for non-executive directors on small boards can also be a significant issue. We have recently worked with a couple of small (5-7) boards who have found that when things get tough, and particularly if there some sort of crisis which results in a breakdown of confidence in the management team, the once-manageable workload soars with NEDs having to put in upwards of 60 days per year. In these circumstances, boards find it difficult to 'call in reinforcements' and have to struggle through until the storm is weathered.

Tenure of directors and succession planning are also a consideration. Best practice suggests a mix of long and short tenured directors to bring a mix of experience and fresh perspectives. Combine this with the reasonable expectation that one or more of the successors to the Chairman and the Committee chairs may be on the board and again prudent management suggests a larger board.

This brief rehearsal of the factors that influence optimum size quickly illustrates that there can be no magic number. The most effective boards that we have seen have been in the 8-10 range – although we would not suggest there was anything magic about that number either. The guiding principle must be to configure the board to make quality decisions in its unique circumstance – in other words, being 'fit for purpose'.

We recommend that the size of the board be reconsidered regularly and a flexible approach taken to either up or down-sizing as is sensible.

Sensible use of ad-hoc and standing committees can help avoid some of the dysfunction of larger groups. We also caution against mistaking cohesion and efficiency for decision-making quality – much value is added by appropriately managed creative tension and disagreement.