



# THE **EVOLVING ROLE** OF THE **BOARD OF DIRECTORS** WITHIN THE **SEMICONDUCTOR INDUSTRY** by John Coutts

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## INTRODUCTION

It's a rare moment when a corporate executive isn't overwhelmed by the pressures of today's business environment. As product development cycles shorten and the demand for highly specialized knowledge grows, semiconductor companies are finding that high level strategic thinking is moving front stage center. The decisions that a board of directors makes have a profound impact on the viability and profitability of an organization.

Although semiconductor company boards have always played an important role in defining a firm's direction and its ability to remain on the leading edge of innovation, today's fast-changing business environment has created additional issues...and pressures. In many cases, it's no longer possible to rely on a tightly knit group of directors to make appropriate decisions. It's no longer wise to eschew succession planning and ignore board composition.

Driving this change is a basic shift in the semiconductor industry and the way research, development, marketing, sales and manufacturing activities take place. Digital convergence in the consumer marketplace is placing new demands on executives—and boards—to broaden the scope of knowledge beyond narrow technical concerns such as processing speed, product size, capacity and other technical factors. It also is forcing boards to have a greater understanding of outsourcing and the intricacies of global manufacturing.

Today, consumer electronics devices—televisions, portable music players, PDAs, gaming gear, toys, wireless communications and automobiles—are changing the look, feel and use of products. Increasingly, semiconductor firms must incorporate data, information and knowledge from an array of disciplines. This situation is forcing companies to



develop new product lines, acquire other companies and change the way engineers, designers and others work...and think. A board must not only understand the key factors driving the industry but also overarching marketplace trends.

This evolution in business demands new and creative solutions. Semiconductor companies must look beyond "tried and true" relationships when examining the composition of a board, its role in setting policies and how it deals with rapidly changing consumer preferences. Without a sense of vision—and an understanding of consumer preferences and behavior—an organization risks losing its viability. As Ruben Roy, an analyst for Pacific Crest Securities observes: "It's a very different business environment than only a few years ago."

## RECOGNIZING THE NEED FOR CHANGE

The breakneck pace of change has left many semiconductor companies vulnerable. Too often, management teams continue to conduct business as usual and base board selection and retention policies on longtime friendships and an existing circle of business associates. This cozy link among various members of a board often leads to predictable and less than visionary thinking.

The fallout, Roy says, is that board members—and the companies they represent—often wind up missing market cues and opportunities. "They may be slow to understand the need for diversification or lack insight into why certain products are poised to take off while others are likely to fade away." While general business considerations remain important—and an understanding of key technical issues is a plus—these factors are only part of the picture. Expanding the breadth of board knowledge and expertise should rank as a top priority.

According to Roy, this knowledge typically falls into three main areas within the semiconductor industry: networking, communications and portability. Technologies such as broadband and Wi-Fi have spawned enormous changes in the way people act... and interact. Mobile phones, PDAs, digital cameras and portable music players have revolutionized business and entertainment. In many cases, these product categories have spawned entirely new market needs and niches. They've created opportunities that couldn't have been envisioned only a few short years ago.

Although boards aren't involved in day-to-day decision making, they play a key role in selecting a CEO and evaluating his or her performance. Equally important: the board governs the organization through broad policies and objectives; it assigns priorities; oversees funding and the allocation of

resources; and directs new, innovative and sometimes experimental programs. Ideally, the board's footprint is everywhere within the enterprise.

Rick Clemmer, president and chief executive officer at Agere Systems, an Allentown, Pennsylvania producer of microchips used in communications devices, believes that while every enterprise has different needs and challenges, a common overlay exists. "The demand for microchips is growing exponentially. The focus is increasingly on how to drive unique functions and integrate components to achieve system level solutions," he observes. At the same time, product lifecycles are compressing—even as development cycles improve—and there's greater risk that a new device or system won't gain widespread consumer acceptance.

What's more, market conditions are changing rapidly. Within a few years, China will surpass the United States as the largest consumer of semiconductors. This creates new challenges for product design and

## 7 STEPS TOWARD BUILDING A BETTER BOARD

Here's how your firm can maximize the effectiveness of the board of directors:

- 1 Develop a board charter.** When it's in black and white it's possible for everyone to be on the same page. A charter clarifies goals, objectives and practical realities. It also provides metrics for determining whether the board and the company are succeeding.
- 2 Look to create diversity on the board.** Too often, executives—and boards—surround themselves with others who share their view of the world. Different perspectives, ideas and knowledge are essential—particularly in an era of digital convergence and rapid change. Different genders, ages, cultures, industries and geographies generate the spectrum of thought required to lead a company.
- 3 Identify the required skills. Hiring a celebrity board member or a golf buddy can prove to be a huge mistake.** If the person doesn't bring needed skills to the table then board performance will almost certainly fall short. Understand what a particular candidate offers and ensure that, for the board as a whole, there's adequate knowledge in areas such as financials, customer relations, human resources, marketing and operations.
- 4 Recruit according to the competencies and skills needed** for a particular position. Once a company has defined the skills it needs on the board, it can proactively research candidates and recruit the right person. One organization may need someone versed in mergers and acquisitions, another in IPOs or digital entertainment. At the same time, board members must be capable of seeing the big picture.
- 5 Encourage independence.** A group of insiders can wreak havoc. That's because their allegiance lies with their boss—the CEO—and they're not as inclined to think out of the proverbial box. Moreover, a CEO may be reluctant to discuss issues such as compensation and succession planning in front of employees.
- 6 Evaluate performance.** Few companies evaluate board members. That's a mistake in today's highly competitive business environment. Like everyone else at a company, board members should know where they're succeeding and failing—and what steps they can take to improve.
- 7 Embrace change. A board must not shy away from the brutal realities of today's business world...**and the changing face of the semiconductor industry. Even the most successful companies may find themselves languishing without a board that understands—and accepts—the evolving dynamics of the marketplace.



functionality but also puts the spotlight on the management of intellectual property. In addition, a growing focus on addressing niche markets has spawned an array of startup firms within the semiconductor industry. All while more familiar challenges, including outsourcing and low-cost foreign competition, continue to demand attention and resources.

Finally, all public companies and their boards face growing regulatory and compliance challenges. Sarbanes-Oxley, the Health Insurance Portability and Accountability Act (HIPAA) and a slew of other regulatory initiatives create new responsibilities. Foreign government regulations and industry standards create additional stresses. Increasingly, firms that lack a solid auditing structure and formal measurement tools find the entity—and their board members—at risk for sanctions and fines.

Of course, filling a board vacancy with the right candidate is no simple task. Ultimately, an organization must achieve the right balance between experience and fresh thinking; practical grounding and wide-eyed vision. An enterprise should aim to break free of “business as usual” thinking and embrace a new model for recruiting and managing a board of directors.

## TRANSFORMING THE BOARD

While the general principal of expanding and redefining the role of a board of directors makes perfect sense, the actual process of driving change can prove daunting. First, there's the task of determining the composition of the board and the length of terms for those serving on it. Then, there's the actual job of selecting board members and defining their roles and responsibilities. Finally, there's the process of optimizing interaction and ensuring that ideas gain a legitimate forum.

According to Bill Bock, a board member for Silicon Laboratories Inc., an Austin, Texas manufacturer of mixed signal integrated circuits used in cellular phones, set-top boxes and computer modems, a CEO should drive the change process. “A CEO should raise key questions about board change, succession and the ability to develop a viable long-term strategy,” he says.

Board composition is at the center of this analysis process. Age, ability to commit adequate time for board responsibilities and meetings, and the knowledge that an individual can bring to the table are all crucial. It's also essential to engage in a frank analysis of what the board has achieved, how prepared it is to deal with evolving industry conditions, and who will replace those leaving the board or retiring within the next few years. Too often,

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companies have no board succession policy in place and the nominating committee winds up making decisions on the fly.

In fact, succession is often the Achilles heel of a board. Many semiconductor companies do not bother to address specific qualifications or tie the hiring of a board member to precise needs, such as finding an outsourcing guru or an expert in digital video or music. Moreover, it's important for members of a board to bring complementary skills and abilities to the table. The resulting synergy can create a foundation that helps the company boost performance and profits.

Other important factors include: determining the length of board terms, how many individuals should serve on the board and how all the people and pieces should fit together. While most companies rely on 6 to 10 board members, every company must find an optimal number. Finally, many, including Agere's Clemmer, believe that an organization should establish a maximum period for serving on a board. “It's difficult to imagine that a person—or management team—can be effective over an extended period of time such as 15 or 20 years,” he states.

No less important is determining how many boards an individual should sit on. Clemmer and many industry observers believe that anyone serving on more than 3 or 4 boards of public companies isn't likely to be fully effective on any of them. The time requirements are simply too steep. Yet, as he puts it: “It depends a great deal on the



company, its position in the industry and how well things are running. There's some room for flexibility."

To be sure, industry leaders are now taking a proactive approach—even setting up board charters that define goals and expectations. Some are now seeking candidates with cross-industry experience. For example, a board member for a consumer electronics chain might bring valuable insights to the board of a semiconductor firm. An executive from a PC manufacturer, software producer, entertainment firm or automobile manufacturer can provide a valuable perspective. This cross-pollination can help the enterprise recognize opportunities, determine how to allocate resources and better understand the continually evolving dynamics of the marketplace. Yet, the possibilities extend far beyond industry circles. A few innovative firms have turned to key customers or business partners to fill a board spot. Some have tapped individuals from important markets, such as Europe or Asia. Although the logistics and travel typically required of a faraway board member can pose difficulties, today's communication and collaboration tools, including videoconferencing, can bridge geographies and time zones. "A multinational board makes perfect sense," says Pacific Crest Security's Roy.

The end goal, Bock says, is to assemble a group of board members that has the domain expertise to answer major business questions and thoroughly

understand the implications and ramifications of a decision. "The board must play an active role in guiding the business," he explains.

## PUTTING A STRATEGY TO WORK

The cyclical nature of the semiconductor industry means that management teams will always face formidable business challenges. Despite sophisticated enterprise information technology systems and advanced analytics, business challenges aren't about to vanish. Nevertheless, recruiting board members strategically can pay enormous dividends. Devoting the same level of energy to selecting board talent as the enterprise does choosing C-level executives leads to long-term gains and bottom line results.

What's more, a company must be willing to dismiss board members who aren't contributing adequately and are unable to adopt a big picture mentality. According to a 2003 survey of 360 companies conducted by Boardroom Consultants, a New York City-based firm, overall organizational success spiked from 20 percent to 70 percent when companies establish independent boards. Too many insiders create a myopic view while undermining essential checks and balances. Nowhere is this situation more apparent than in the semiconductor industry.



Finally, savvy organizations cultivate board members willing to challenge conventional thinking and raise issues that aren't particularly appealing to management. At the same time, management must make a commitment to board members that it will inform them of news and events that are both good and bad. Anything less undermines trust and interferes with cooperation. If a company adopts a rubber stamp mentality than it is likely setting itself up for future problems.

Ideally, all members of the board and the CEO are willing to step beyond the flat earth of conventional thinking. They're willing to take risks...but also embrace the opportunities that come with a more innovative and strategic environment.

## CONCLUSION

While it's clear that the semiconductor industry is changing, there are no easy answers for how to select, manage and interact with a board of directors. Yet, as the marketplace evolves and shifts, only the most visionary and innovative firms will thrive. New startups constantly challenge established companies and bring forward new technology and better business processes. Yesterday's hot company can quickly find itself relegated to the dustbin of history. Producing bottom line results and maximizing shareholder value is increasingly about building a better management structure.

It all starts in the boardroom. Semiconductor companies that assemble a board of directors that truly understands the dynamics of the marketplace are at a distinct advantage. Firms that have their finger on the pulse of product development, management structure and industry conditions are in a position to reap the rewards of the digital age. Make no mistake, companies that build a foundation for success almost always emerge as winners.



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