How to Recruit, Select and Compensate Board Members

by Charles H. King and Caroline W. Nahas

The first few years of the 21st century brought nothing but turbulence to American corporate boardrooms. Maddening volatility in the markets, a sharp decline in investor confidence, intense scrutiny of financial reporting practices, and many high-profile corporate collapses laid the groundwork for reform. For both better and worse, Sarbanes-Oxley emerged and the forms and functions of corporate boards will never be the same.

Change was clearly overdue in one area, board recruitment. Historically, the search for new directors was led by the Chairman/CEO, who often acted as the critical first screener. He or she would identify a few "good" candidates, meet with a limited number and pick personally acceptable options; then let a board committee make the final decision. While there was nothing inherently wrong with that streamlined approach, it certainly didn't communicate independence and objectivity, nor did it look like the board had done a full and proper job.

In recent years, many boards have gotten far better at candidate identification and selection. Still, they tend to make three important miscalculations: underestimating the degree of difficulty of the task; ignoring the limited supply of and great demand for top talent; and overestimating the attractiveness of the opportunity. One consumer-products client gave us a plum assignment to find three new directors, but they were adamant about only considering current CEOs, one of whom had to be a diversity candidate. As in all aspects of corporate life, successful board recruitment hinges on maintaining realistic expectations.

If assembled properly, a board of directors is the best bargain in modern business because it represents a cadre of expert consultants to management, with a level of talent and experience the company could never hire on a per diem basis. The right directors can make a huge difference in a company's performance, but getting a winning team requires a disciplined approach.

How do boards find the A-List talent they need for sound corporate governance? Ideally, recruitment is led by a strong, organized Nominating Committee, which has the full faith and backing of the chairman, CEO and other key directors. The committee also needs a common commitment to board balance and to finding the best people through a thorough, transparent process. Great recruiting only happens when people are personally engaged and passionate about the work. Anyone involved in a search must be fully prepared and able to answer any question about the company, a director's role, board dynamics and expectations.

The first step is to define the characteristics required in a good director for this specific board. That requires a clear-eyed review of company needs from many standpoints. Where is the business going, short- and long-term? What are the most pertinent performance objectives? What types of people already serve on the board? That data is overlaid on the current directors, producing a human gap analysis and a profile of ideal candidate(s). A simple matrix reveals, for example, the voids in CEO or operating experience, industry or functional expertise, or diversity/gender representation.

With a well-defined director specification in place, the corporation must cast the widest net possible to find true "impact players." Previously, board recruitment relied too heavily on the personal networks of the current board and senior executives. Today, a database of thousands of names is the standard starting point and that must be augmented by original sourcing of good prospects. Candidate identification is an incredibly research-intensive process, with lots of blocking and tackling involved. One common pitfall to avoid is star shopping - compiling a list of marquee names, without really knowing the individuals, their specific skills and personal styles.

In most cases, 120 days is a reasonable length of time for a search, with 90 days clearly falling in the category of fast track. The timeline varies for many reasons, but the biggest problem is calendar crowding. Often, busy executives have extensive scheduling conflicts. A solid slate of candidates can be assembled within 30 days; but then the nominating committee must thoroughly review the list, discuss and prioritize it, and conduct interviews.

Because of the ferocious competition for "A+" and "A" leaders, the greatest difficulty in any director search is simply attracting their attention. Facing greater demands from their own companies and a heightened level of accountability in board service, quality people are not inclined to take on any additional responsibilities - unless there is a huge upside potential for themselves or their businesses.

Many companies envision a board comprised of brilliant sitting CEOs from non-competitors. Given the current business landscape, that is not only unlikely but unwise. To achieve a balanced and effective board, consider taking a "tapestry" approach that integrates sitting chief executive officers with recently retired CEOs, international operating executives, presidents of large and complex divisions, people with functional expertise, partners retired from major public accounting firms, association or nonprofit executives, business-savvy academics, and/or senior consultants.

It is important to look for proven leaders who have effectively addressed the kind of issues and opportunities the corporation is facing. Good candidates must have a well-developed appreciation of group dynamics and a reasoned point of view that can be expressed forcefully, but not abrasively. And, for the foreseeable future, financial acumen is a very desirable quality. To secure one top-drawer director, the nominating committee will need to consider 15 to 20 qualified candidates.

Contacting and evaluating candidates must be done systematically because every top person requires a precisely tailored approach. The initial point of contact can range from the recruiter to the chair of the nominating committee to a board member acquainted with the prospect. Face-to-face meetings with board members are an essential part of learning more about the person and of sharing company strategy and board expectations.

No matter how persuasive the candidate or sterling his or her pedigree, the best approach is to trust but verify. Reference checking is a crucial and time-consuming part of the exercise, often done best by a third party who can pose delicate questions without seeming to snoop. Some of the more reliable information sources are directors or executives with whom the candidate serves elsewhere. "Does he or she understand the business, take the role of director seriously, ask good questions, offer relevant insight, do a fair share of work, not hold a grudge, listen to peers, and in general make the organization better?"

The most devastating consequence of choosing poorly is the least obvious. A bad selection represents a wasted opportunity to add someone of genuine value. Since most boards don't have term limits, the company must assume it will live with a director for a very long time. Clearly unproductive board members aren't allowed to languish anymore, but it is not easy to replace one. That can have a negative affect on group dynamics and distract the board from more pressing matters.

There is no magic formula for compensating directors, but there is a fundamental principle. It has to be fair - both to the person contributing valuable time and to the corporation. A-List people don't serve on boards for the money. They usually want three things out of their involvement: to make a valuable contribution; learn something useful; and associate with other interesting people. If a candidate's first question is some form of "What's the comp package?" you probably want to look elsewhere.

In general, excessive board compensation is a thing of the past. Companies striving for fairness and balance usually arrive at around 50% cash and 50% stock, so directors benefit from strong corporate performance but not excessively. It is not uncommon, however, for directors in critical, time-intensive roles such as audit committee chair to be compensated more than their peers.

If a company conducts its own director search, it can be difficult to maintain a truly independent process, or the appearance of one. However, if the corporation uses an executive search firm, the result will only be as good as the consultant leading the search. Boards that do their own recruitment must clearly acknowledge the limits of their reach and research. Recently, a client engaged us after trying and failing on a crucial search. The company wanted an African-American with Ph.D. in Thermal Chemistry who was not an academic - a microscopic needle in a field of haystacks.

An outside firm creates a useful buffer between company and the candidates. Professional recruiters can manage candidate expectations, so the organization won't alienate the unsuccessful candidates. With, say, five finalists for one position, no one wants to lose - and this caliber of person isn't used to coming in second. Also, search professionals can help a board realistically assess its current situation, do a thorough needs analysis, and share best practices of other high-performance boards.

Attractive candidates have a shelf life, so a company must be prepared to move quickly after completing its due diligence. On the flip side, persistence can pay off. In one instance, the perfect candidate was not interested at first; but the executive recruiter, chairman and CEO maintained contact over the next two years. A relationship of trust developed and finally the board secured exactly what it needed.

Charles H. King is Managing Director and Head of Global Board Services at leading executive recruiting firm Korn/Ferry International.

Caroline W. Nahas is Korn/Ferry International's Managing Director/Southwest Region and a member of the Board Practice.

Korn/Ferry International has conducted director searches for ExxonMobil, Lincoln National, Goodyear, The Southern Company, Aramark and many other prominent corporations.

What makes a great director?

- Relevant skills and experience
- Competence in a specialized area (accounting, finance, marketing, technology, law, international, etc.)
- Demonstrated track record of success
- Independence and objectivity
- Willingness to challenge prevailing opinion, and do it productively
- Consistent availability
- Sound judgement and broad perspective
- Ability to not interfere in day-to-day operations
- Integrity
- Intellectual curiosity about the company
- A good cultural fit with other board members

Sample Composite of a Well-Rounded Board

Board Skills Matrix: ABC Company

	CEO/COO/ President	CFO/Finance	Healthcare	International	Acquisition Experience	Public Board Experience	Diversity	Human Capital/ Performance Measurement	Growth Orientation	Investor/Gov't Relations
Director #1	X		X	X			X	X		X
Director #2	X		X							
Director #3	X		X			X	X		X	
Director #4	X	X	X	X	X	X			X	
Director #5	X		X	X		X				
Director #6	X		X	X	X	X	X		X	
Director #7	X		X			X	X			
Director #8		X		X	X	X		X	X	X
Director #9	X	X	X	X	X	X			X	

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