



A guide to board effectiveness reviews

Why they matter and what good reviews look like.

Board effectiveness reviews have become a more established practice globally as boards increasingly recognise their benefits.

However, LGIM finds they too often remain a box-ticking exercise. While local corporate governance codes might have different standards, this guide sets out LGIM’s expectations on this important but sometimes overlooked exercise.

An important tool for boards & investors

For board effectiveness reviews to achieve their purpose, it is fundamental that the board recognises their role in:

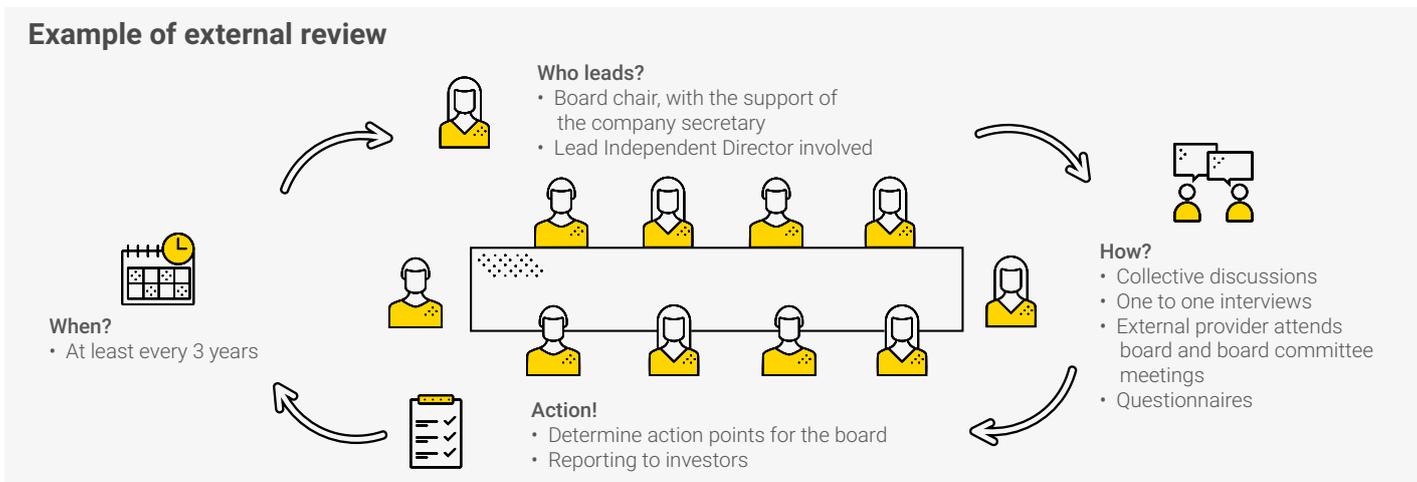
1. Improving the efficiency of the board

An efficient board is central to any successful company. Board reviews help the board identify weaknesses and act on them.

However, they are not just about marking the board’s homework; they are also about making sure the board is fit for the future. In a constantly evolving business environment, they are an opportunity to help a company’s board improve and advance.

2. Providing comfort to investors on the functioning of the board

As investors sit outside board discussions, it can be difficult for them to assess what happens inside the boardroom. The board review can provide investors comfort that the functioning of the board is being regularly assessed and monitored with the aim of ensuring it is constantly challenging itself.



What a good review looks like

We expect all companies globally to put in place a robust process, taking into account the following considerations:

Internal or external?



- ✓ **Internal review:** To be conducted annually. This exercise provides an avenue for feedback by all board members, and for the board chair to assess weaknesses and ensure the functioning of the board.
- ✓ **External review:** We consider every three years to be best practice. An external review allows for an independent assessment of the board to be made by a fresh pair of eyes, with experience in assessing many other boards.

External reviews: choosing the board review provider



- ✓ Put in place a **tender process** to be led by the Lead Independent Director (LID) and company secretary, with the support of the board chair.
- ✓ **Determine the scope and objectives of the review with the provider before their appointment.** There is no one-size-fits-all to board reviews; the provider should tailor their approach to the company's individual circumstances.
- ✓ **Manage conflicts:** can the provider exercise independent judgement? We encourage regular **rotation** of providers and potential conflicts arising from other services undertaken by the provider to be managed.

Scope of the board review – a non-exhaustive list



- ✓ Board dynamics and interactions.
- ✓ Board composition including succession planning.
- ✓ Contribution of individual board members to board discussions.
- ✓ Board meeting agenda.
- ✓ Role of the board vis-à-vis management – is there enough challenge?

- ✓ Effectiveness of board committees and their contribution to the board.
- ✓ Feedback from stakeholders, including company internal and external auditors.
- ✓ Feedback from the executive team.

Who leads the board review?



- ✓ The **independent board chair** should lead the process, with the help of the company secretary.
- ✓ The **LID** evaluates the performance of the board chair or may under certain circumstances lead the process.

What tools to use in the board review?



- ✓ **Questionnaires** can be used but they shouldn't be the only way of assessing the board, especially for external reviews.
- ✓ **Discussions** are important. This means going beyond a simple form-filling exercise:
 - Collective discussions; and
 - One-to-one interviews with all board members and the company secretary.
- ✓ Our preference would be for boards to allow the external review provider to **observe board and board committee meetings**.

What next?



- ✓ Determine the outcome of the board effectiveness review with the board review provider in case of an external review.
- ✓ The board should discuss the outcome.
- ✓ The board should determine the action points.
- ✓ There should be reporting, as detailed below.
- ✓ Open engagement with investors on the topic.
- ✓ Follow up to see if actions have been taken.

Best practice in disclosures

For the board effectiveness review to provide comfort to investors on the functioning of the board, sufficient information must be disclosed to them in the company's annual reporting. This is because investors rely on the information the board is willing to provide to them.

Too many companies only disclose that a review has been undertaken, without providing any details. While we understand some of the information might be confidential, many companies have already started to provide a great level of detail. LGIM encourages all companies to provide more information around the following elements:

Board review methodology

LGIM expects companies to **disclose how the review was undertaken, the scope of the assessment, and the objectives of the review.** This is important for investors to assess how thorough the review was and therefore informs their judgement on the quality of the review.

Management of conflicts

We find there is an inherent conflict when the external board review provider also provides other professional services to the company. **We would therefore encourage the board to refrain from contracting a provider who also provides additional professional services to the company.** Where they choose to ignore this, we expect any additional services provided by the board review provider to be disclosed and minimum periods of being offside must occur and be disclosed.

In addition, in order to ensure board review providers remain independent in their assessment, we would like to see companies disclose information around the rotation of their providers. **LGIM would expect the same board review provider to undertake no more than two consecutive reviews before the company uses a different reviewer.**

Reporting the outcome in the annual disclosures

We expect the board to communicate the outcome of the board effectiveness review in its annual disclosures to investors. Therefore, **companies should avoid general statements and focus on the quality of the disclosures.** This is essential for investors to get a real insight into the functioning and dynamics of the board. It can also help them

assess whether progress has been made in comparison with previous reviews. Open and honest disclosures will demonstrate to investors a commitment to improvement and evolution.

We would not expect the same level of detail for an internal versus an external review, as we expect the external review to be more thorough. While we acknowledge some of the information might be sensitive and prevent full public disclosure, we would expect disclosures in annual reporting to comprise:

- A list of the areas of strengths and weaknesses identified; and
- The action points for the board and timescale.

For external reviews, LGIM encourages all boards to agree the disclosures with the provider and have them sign off the company statement in the annual reporting. We would also encourage the board to state in its annual disclosures whether sign-off was obtained. This would give investors greater trust in the disclosures provided.

Reporting on progress

Communication to investors should not be limited to the initial outcome of the review. **LGIM expects companies to continue to report annually on the steps the board has taken since the last review.** This is for investors to assess whether the board has acted on the previous action points or whether they remain outstanding.

Creating industry codes of practice

LGIM encourages the creation of industry codes of practice in all local markets. We find they help contribute to raising the overall quality of board reviews. They provide a framework to ensure that a minimum standard of board review is upheld and that potential conflicts of interests are managed appropriately. They also guide boards in approaching this challenging exercise. This ultimately helps boards improve and raise investors' confidence that the company is striving to the best it can be.

Contact us

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