Independence: Unintended Consequences

In many parts of the world, shareholders, commentators and regulators are pressing companies to shake up their boards. The economic fall-out from the global pandemic, and concerns about the impact of climate change, fuel calls for better governance. It all starts in the Boardroom.

Diversity demands are not simply a gender issue. The skill mix and breadth of experience available amongst board members are coming into sharper focus. Are these what the company needs to take it forward? Is the board alert and ready to change to meet tomorrow's challenges?

Much of this comes coupled with a push for greater board independence.

Unfortunately, this is accompanied by an increasing tendency for a new board to take legal action against the previous board members for decisions that went wrong. If that is linked with reminders about a director's fiduciary duties, a climate of fear is the result.

Not wanting to be caught in the trap, the new directors and others who are looking on, especially those deemed to be independent, may well become risk-averse. Better to say "NO", than get caught being wrong.

The carefully constructed, multi-talented, diversified, and largely independent board no longer acts as a force for change; it has become a barrier to achieving what the company's stakeholders expect of it.

Independent directors are expected not to go blindly with the flow, but that should not translate into negativity. The primary fiduciary duty of a director is to always act in the best interests of the company, taking into account the legitimate expectations of a variety of stakeholders.

In times when change is vital to survival, obstructiveness equates to voting for the status quo. That could be the opposite of the company's best interests. Where does that leave fiduciary duty?

It is worth remembering that a board doesn't have the benefit of hindsight when it makes a decision. That is based on the information available to the board at the time. So, when the board arrives at a decision, it cannot be a question of making the right decision. Instead, it is a question of making the decision the right way.

To determine this, a board should consider the following issues:

- Is the information comprehensive, current and coherent?
- Has independent professional advice or opinion been obtained, possibly from more than one source, and can that opinion be relied upon?
- Have alternatives to the recommended course of action been considered?

- Have the risks associated with all alternatives been thoroughly evaluated, including not taking any action?
- What is in the best interests of the company and its stakeholders?

Later, if the decision has an adverse outcome and becomes a legal issue, the Courts will not be inclined to second guess the decision itself. It wasn't made with the benefit of hindsight. Rather, the Courts will likely look at the process which led to the decision. Was that flawed?

What the Courts will consider is the circumstances which led to the adverse outcome. Could, or should those circumstances have been predicted at the time the decision was made?

Did the directors, at the time they made the decision, act in the company's best interests, having thoroughly assessed the information then at hand and the risks associated with the decision?

Today's world demands responses. "Do nothing" boards, which lack the ability to move or act, will be judged harshly. Good boards will try to think like their critics and see themselves through the lens of those who observe them.

Independent directors should be judged through the same glass.

"NO" is not always the right answer, nor will it deliver safety from criticism. Good directors are not afraid of change; they act diligently and embrace it. They turn stakeholder expectations into their own objectives.

It is their duty to do so.

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