BOARD EVALUATIONS – SELF-EVALUATION OR THIRD PARTY EVALUATION?

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There is often tremendous resistance to the idea of board evaluations, even self-evaluations. No one likes to be evaluated. Evaluations can be messy and unpredictable in nature. Some board members may feel that their position is on the line. Some CEOs may feel that a board evaluation will lead to a more assertive or even intrusive board.

Many boards won't do them. In a study conducted about ten years ago, the Federal Reserve Bank of Richmond found that a majority of banks under its jurisdiction did not conduct any formal evaluations of the board or board members. I don't believe that has changed much over the past ten years, with the exception of companies whose stock is listed on the NYSE or, perhaps, on Nasdaq.

Then there are other boards that do board evaluations but simply go through the motions. These are evaluations designed to enable the board to check them off on the list of things to do, not to learn from the experience. The questionnaires completed by board members often reflect satisfactory or outstanding ratings for themselves and for the board as a whole. "Needs to improve" or "unsatisfactory" ratings are rare or nonexistent, and comments supplementing the check-off items are uncommon.

In my view, these evaluations are worse than not doing them at all, because there is a self-delusional aspect to them. A poorly done board evaluation gives the impression that something meaningful has been accomplished, when in fact it is all appearances and no substance.

Who will evaluate the board if the board or a person designated by the board doesn't do it? Probably no one. Even if your company's stock is listed on the NYSE (which requires board self-evaluations at least annually), the NYSE does not evaluate how the company is meeting its obligation. There is no qualitative check. The shareholders normally rubberstamp the nominees chosen by the board or the nomination committee, and even if shareholders were to evaluate a board member or the board, they would be ill-equipped to do a good job.

Bank examiners will evaluate the board as part of their review of management, but their focus is more on senior and other active management (although the boards of large banks are increasingly of interest to examiners), and they certainly cannot perform an in-depth review of the board or board members that the board or someone designated by the board could accomplish. Bank examiners normally also focus more on results than they do on the finer points of corporate governance.

Other than the NYSE rules applicable to companies whose stock is listed with NYSE, there are no legal or regulatory requirements for a board evaluation other than the OCC's "heightened expectation" rules applicable to national or federal savings banks with assets of at least $50 billion, which state that the boards of covered banks should conduct an annual self-assessment..

In other words, for most of you, a board evaluation is entirely voluntary. It's your choice as to whether to conduct a board evaluation and, if so, how.

A board evaluation conducted by an independent third party can take different forms.

The evaluation can be of the entire board, not singling out any individual board member. Or it can be done through both an evaluation of the board as a whole and an evaluation of individual members of the board.

In light of the recent turmoil in the banking industry and the concerns that AABD and others have expressed about the risks of personal liability of bank directors, AABD offers independent board assessments that evaluate the effectiveness of a board of directors and provide practical advice. Given the heightened concern about the personal liability of bank directors, AABD also includes in the assessment suggestions on how a board of directors might minimize the risk of personal liability of its members by changing certain practices, procedures or policies.

AABD will review Board structures, practices, and policies and prepare a written report summarizing our review and identifying what we believe to be the strengths and weaknesses of the Board and its operation, with a set of recommendations. The study and report are designed to be constructive and will not single out any individual board member or conduct any individual assessment of a board member unless the Board requests us to do so.

The review will be based, among other things, on the following:

- A detailed questionnaire identifying existing corporate governance practices, systems and controls, and attitudes and knowledge base of the board of directors
- Review of the current written corporate governance policy of the Bank and the Bank's articles of incorporation and bylaws
- Board reports, board packages, and minutes from board meetings
- Committee reports, committee packages, and minutes from committee meetings, with an emphasis on the audit, loan, compensation, risk, governance and nomination committees
- Interviews with the CEO, Chairman of the Board, and all of the outside directors

The report will be presented in draft form for the review and comment by each member of the board and the CEO. After considering all comments, we will finalize the report and submit it to the Board of Directors. All comments will be incorporated into the report, either as those accepted by us or through an addendum. We will be available for questions about any aspect of the report.

An AABD representative usually visits the Bank two times; the first time, to review documents and interview members of the Board, and the second time, to meet with the Board of Directors to present and discuss the report. We can also conduct the review the appropriate documents, interview individual directors and the CEO, finalize the report, and discuss it with the Board of Directors entirely off-premises. Discounts are available for banks whose board members are AABD members.