

REALBoard Advisor

Tips to become R – Results-focused E – Excellent A – Accountable L – Linked to Shareholders/Owners

Out of the Rocking Chair: Using Policy Governance® to Manage Risk Effectively

A considerable amount of board energy is spent on issues related to risk. All too often, boards find themselves in the proverbial rocking chair worrying about risk—moving furiously, but not getting anywhere. To quote Benjamin Franklin, “Never confuse motion with action.”

In this article we will examine how the Policy Governance® “operating system” for boards can be used to provide a comprehensive approach to managing risk. This approach avoids the board becoming embroiled in operational details while at the same time it ensures that risk will be appropriately managed. The board can fulfill its fiduciary responsibility related to risk, while still spending most of its valuable time focused on creating the future by providing strategic leadership.

Risk Tolerance is Value-Based

The fundamental determinant of the risk tolerance of an organization is based on values. It is the board’s job to determine the appropriate balance between risk tolerance and risk aversion. Since the board is acting on behalf of owners or shareholders, the board needs to be aware of the owners’ values in order to determine that balance. Those values need to be explicitly stated, so that they can be translated into operational behaviour. Finally, the board must demand and monitor

management performance in order to be accountable to owners.

Policy Governance® provides a systematic approach that enables the board to meet the governance challenge of expressing the owners’ values in a way that appropriately balances management empowerment and retains control to ensure accountability to the owners. The board makes its values explicit in four categories of policy that, taken together, are sufficient to control everything about the organization. These policies are:

- *Executive Limitations* – values about management means, in order to assure that unacceptable situations are avoided;
- *Board - Management Delegation* – values about passing of power and assessing its use, in order to assure the accountability chain from CEO to Board;
- *Ends* – values about what the organization is to produce on behalf of owners or shareholders; and
- *Governance Process* – values about the process of governance, in order to assure that unacceptable situations at the board level are avoided.

Each of these categories of policy can be utilized as part of the board’s overall approach to risk management.

Executive Limitations and Risk

The Executive Limitations policies quite obviously address risk. The board should systematically consider all areas of operations, identifying any areas of risk that should be addressed in policy. The special distinction of Executive Limitations is that these policies will not prescribe means for the CEO, but will rather identify only conditions or practices that would be unacceptable to the board, even if they worked to achieve the Ends.

The aim of the Executive Limitations policies with respect to risk should be to clearly convey to the CEO in writing the board’s expectations as to what is unacceptable.

The board might choose to develop limitations related to the risk management process itself. For example, “The CEO shall not operate without an effective process for identifying, assessing and managing operational risks.” Note that the policy doesn’t prescribe a specific process that the CEO must use – the CEO will have expertise here that the board does not and need not have. But the CEO does have to produce a reasonable interpretation of an “effective” process, and evidence of compliance.

A major area of risk relates to financial planning, management and controls. When assessing its policies in the financial area, the

board might ask itself questions such as these:

- Does board policy require management's financial plans to be consistent with the achievement of the Ends?
- Does board policy require annual financial planning to be in the context of a longer-term plan?
- Does board policy require sufficient risk management and internal controls systems to ensure sound financial performance and prevent financial mismanagement?
- Does board policy require sufficient internal controls to ensure that accurate financial statements will be produced?
- Does board policy specify the board's desired balance between risk and return, and expectations for prudent management of investments?

If delegation is done in a manner that lacks clarity, the accountability chain is broken, resulting in risk that the organization will not achieve what it should.

What situations related to communications, including communications to the board itself, internal communications, and communications with customers and other stakeholders, would pose unacceptable risk? What level of administrative support does the board expect in its own communications with owners or shareholders? In particular for corporate boards, there is significant risk related to communications, transparency and reporting to shareholders. The board might ask whether its policies clearly identify unacceptable situations related to disclosure and transparency.

Failure to comply with laws and regulations is an obvious area of risk. Generally, this risk can be addressed at the "mega" or broadest policy level of Executive Limitations. Most Policy Governance[®] boards use language such as "The CEO shall not cause or allow any practice, activity, decision or organizational circumstance which

is either imprudent, illegal, or in violation of commonly accepted business and professional ethics" as the largest policy in Executive Limitations. Use some "what if" scenarios to consider whether the board is comfortable that "any reasonable interpretation" of this policy would include, not only all laws that apply to the organization, but all government regulations, and, in the case of publicly-listed companies, all securities regulations. Whether or not the board amends the wording of this policy, it is important that in the monitoring process the board does not accept as reasonable an interpretation of "illegal" or "imprudent" that omits major areas of risk for the company that have not been explicitly addressed by the board in any lower-level Limitations policies. In my experience, the

monitoring for this mega-policy is often poorly done, leaving the board at risk of potential violations. In order to ensure that policy addresses these issues, it is important for the board to be familiar with key laws and regulations that are applicable to the company.

There is increasing emphasis in corporate literature and conferences around the issue of "tone at the top" – a culture of integrity in the company. Does the board have explicit policy making it clear that it is unacceptable for the CEO to operate without establishing a "tone at the top" that reinforces the company's values and promotes a culture of integrity and transparency?

Two other areas of risk should be considered when developing limitations. What would the board find unacceptable related to how people are treated by and in the organization? Policy in this area

could address relationships with both individuals and groups, including treatment of staff, customers or clients, other stakeholders, members (if applicable), and the general public. In keeping with increasing emphasis on corporate social responsibility, the board should make it clear what situations related to the company's interaction with the external world – the environment, community, stakeholders – would be unacceptable.

Board – Management Delegation and Risk

It is an easy mistake to assume that having dealt with operational risk, the board's job is done. However, there are also risks that relate to the board's own processes. One very specific board process is delegation from Board to CEO and evaluation of the CEO's performance. If delegation is done in a manner that lacks clarity, the accountability chain is broken, resulting in risk that the organization will not achieve what it should. Policy Governance[®] provides a very powerful method of minimizing this risk. The board should have written policy that clearly outlines the process it will use for delegation of authority and monitoring. Does board policy clearly state that there will be only "one voice" delegating to the CEO? Does board policy clearly state that in operational areas the board will delegate *only* to the CEO? Does the board refrain from creating committees that are intended to "help" the CEO?

Is there a systematic and thorough monitoring process described in writing that requires evidence of Ends achievement and compliance with Executive Limitations? If there is a performance component to the CEO's compensation, is policy clear as to how it will be applied? Does the board regularly monitor its own compliance with these policies that describe how it will delegate and evaluate?

One of the board’s options in monitoring CEO performance is to use an external auditor. Is board policy sufficiently explicit to ensure that the independence of the external auditor is not and will not be compromised? Apart from the financial audit, has the need for any additional “external audit” or “direct inspection” of policies been identified? Has the scope of the external audit been clearly defined to include all finance-related policies for which the board wishes an external assessment of compliance?

- Does the board take responsibility for knowing more about the issues than the owners do?

Governance Process, Structure and Risk

In addition to the risks associated with the board paying insufficient attention to its Ends work, and with unclear delegation processes described earlier, there are other board processes that are potential sources of risk.

Consider the structure and composition of the board itself. If it is too large for healthy dynamics, or

- Do at least some of the board members have sufficient knowledge and experience to provide depth to the board’s policy decisions related to fiduciary areas such as risk and finance?
- Is the board a size that allows for the entire board to be actively involved in governing, and contributes to good teamwork as a board?

There is also risk associated with turnover of board members, and compensation plans for board members. Is the board term

Definition of Risk	How Policy Governance® Addresses Risk
Possibility of loss or injury. <i>Merriam Webster</i>	Policy Governance provides a systematic approach to examining and documenting every area of organizational behavior.
Any issue which could impact your ability to meet your objectives. <i>Price Waterhouse Cooper</i>	Policy Governance provides a systematic approach to identifying and documenting expectations, providing clear Ends that make organizational direction clear.
Risk comes from not knowing what you’re doing. <i>Warren Buffet</i>	Policy Governance provides a systematic framework for the <i>entire job of governance</i> , so the board is clear on its direct accountability to owners, and management is clear on its direct accountability to the board.

sufficiently long to allow board members to develop some expertise? Boards that have one or even two-year terms do not permit the development of governance expertise. Just as a board member is beginning to become a useful contributor, the term is over. Policy Governance® does not dictate an appropriate board term,

Ends-Related Risk

While the Ends themselves are not about risk, there *is* a significant risk that the organization will be headed in the wrong direction if the board does not do a good job of developing Ends. So the board should ask itself questions such as the following to ensure that it does its most important job – determining what the organization is expected to produce, for whom, and at what cost – effectively:

- Does the Board have a process to regularly connect with owners so that policy development will be informed by owners’ values?
- Is the linkage process designed to obtain “representative” input?
- Does the board seek out future-oriented information to design Ends that will lead the organization with sufficient foresight?

lacking in diversity, the resultant behaviour will negatively impact the organization. The board might ask itself questions such as these:

- Does board composition provide sufficient diversity and depth of knowledge that the board collectively will be able to develop policies that effectively *govern* the operations of the organization? Note that the board should not be looking for individuals who have expertise in specific management areas such as human relations, finance, and so on, for the purpose of being advisors to the CEO. Rather, look for people who are committed to actively connecting with the owners and understanding their diversity, who have the ability to think in the context of the big picture, and who have the capacity to discuss the values underlying what is done in the organization.

but understanding of the principles makes it a logical consideration to provide for development of governance excellence. Is there a comprehensive orientation plan in place for new board members? Does the Board have a succession plan for recruiting new board members? In publicly owned companies, is director compensation designed as an incentive for directors to act in best interests of shareholders? In non-profit organizations, if there is director compensation, is it designed to encourage the most effective governance – for example, not providing significant stipends for committee work that may tempt the board to create committees simply to generate compensation?

Another significant risk is that the board’s policies will be ill informed because it has a defective decision-making process. Does the Board have a deliberate process to regularly connect with owners so

that policy development will be informed by owners' values? Does the board base policy decisions on timely, accurate and complete information? Does the board receive sufficient information about the risks facing the organization to develop appropriate Limitations policies and keep them current? Does the board actively seek out expertise necessary to make well-informed decisions? Does the board have sources of information independent of the administration? Does the board have a process that ensures due diligence in making policy decisions? Policy Governance® provides a framework within which to address all of these questions in policy, and then to monitor for compliance with them.

Board committees can be a source of risk if they are created without considering whether they may damage the function of the whole board as the authoritative governing

body, or if they are created so as to interfere with the clarity of delegation between board and CEO. Policy Governance® provides the framework for clear delegation when board committees are formed – each committee should have a specific charter or terms of reference that specifies the products the board expects and limitations on the committee's authority.

The board's own behaviour is also a potential source of risk. Does the board set clear value-based expectations for the CEO, but then fail to model those same values itself? Does the board have policy setting out its own commitment for behaviour as a board? Does it have a code of conduct setting out its expectations for individual board members, including conflict of interest policy? Finally, does the board not only have these policies in place, but take responsibility for excellence in governing by regularly

monitoring its own performance against the expectations set out in its policies? When deficiencies are identified, does the board commit to specific actions for improvement?

Policy Governance as a System to Effectively Manage Risk

Policy Governance provides a systematic approach to examining and documenting risk related to every area of organizational behaviour. It provides a vehicle to set clear expectations about organizational purpose and means. It provides for effective delegation and monitoring. In fact, it is a systematic framework for the *entire job of governance*, so the board is clear on its direct accountability to owners, and management is clear on its direct accountability to the board. The board is engaged in an effective process, not merely "rocking" without getting anywhere.

Policy Governance® Primer



Policy Governance ABC's

Policy Governance® is a model of governance created by Dr. John Carver. It enables boards to provide strategic leadership in creating the future for their organization. Policy Governance ensures accountability of the CEO to the Board, and of the Board to the ownership. Its principles are internally consistent, designed to work effectively when used together as a complete "operating system" for a board.

Policy Governance enables the Board to:

- Be accountable in the position of trust in which it has been placed by its ownership/shareholders
- Provide strategic leadership—its key responsibility—by clearly defining, on behalf of the ownership/shareholders, or what benefits are to be produced, for whom, and at what cost
- Distinguish clearly between Ends (see below) and Means (ways of doing things)
- Be involved in appropriate decisions without "meddling" or "rubber stamping"
- Set parameters for acceptable organizational performance and for itself by establishing broad policies in four logical categories that make intuitive sense.

The policy categories are:

Ends – what benefit, for which people, at what cost? Ends are developed based on the Board's knowledge of and interaction with the "ownership" – those to whom the Board is morally accountable.

Executive Limitations – the boundaries of prudence and ethics within which the Board allows staff to make further decisions about means.

Board-CEO Linkage – the manner in which the Board delegates authority to staff through the CEO, and how it evaluates staff performance.

Governance Process – the manner in which the Board itself will operate, including its philosophy, accountability, discipline, and its own job.

About Us

Jannice Moore

Jannice Moore, President of The Governance Coach™, is an independent consultant to governing boards and senior management. She has over thirty years experience as a manager, planner, consultant and educator. She has worked with the Policy Governance® model developed by John Carver for over fourteen years, and has studied directly with Dr. Carver, graduating from the first Advanced Policy Governance® AcademySM. Jan has coached a wide variety of boards in the use of Policy Governance, including membership and voluntary organizations, trade associations, regulatory bodies, health care, business, and education boards. She has facilitated numerous board and management retreats, and designed award-winning board development programs. Jan holds the designation of Certified Health Executive from the Canadian College of Health Service Executives. She has a Masters degree in Health Services Administration from the University of Alberta. Most recently Jan has written the book *Governance for Health System Trustees*, published by the CHA Press. She has also authored several articles and monographs and contributed chapters to a number of books. She has contributed to *The Policy Governance® Fieldbook*, published by Jossey-Bass, and is a regular author in *Board Leadership*, also published by Jossey-Bass. Jan has been a speaker at conferences and seminars in Canada, the USA and Europe. She has been a member of the founding board of the International Policy Governance® Association since its inception, and is currently Chair. Jan is also Chair of the founding board of Greenleaf Canada Institute.



Associates

Susan Mogensen

Susan is a graduate of the Advanced Policy Governance® AcademySM, personally trained by John and Miriam Carver in the principles and implementation of Policy Governance. She holds a B.A. (Honours) in Political Science from Carleton University, and certificates in Participative Training Techniques (PTT), Group Facilitation, and Small Business Development as well as designation as an IAF Certified Professional Facilitator. After providing organizational, communications and senior legislative assistance to federal level Parliamentarians for 12 years, and developing additional experience in the non-profit sector, Susan is now associated with The Governance Coach™ to assist boards in implementing the Policy Governance® model. Susan's services reflect her passion for helping groups of people work together effectively. She believes in strengthening clients' abilities to create their own solutions, and places a high value on integrity, logic, and fun. Her clients have included small businesses, the City of Ottawa, the federal government, health and education boards, and non-profit associations.



Richard Stringham

Richard is a graduate of the Advanced Policy Governance® AcademySM, personally trained by John and Miriam Carver in the principles and implementation of Policy Governance. He holds a B.Sc. in Agriculture from the University of Manitoba, and is a Professional Agrologist. He has over twenty years of experience as a manager, educator and consultant, including senior level management in an organization using Policy Governance. Past clients include Associations at the provincial and national levels as well as co-operatives. He brings with him a combination of facilitation and training skills, and knowledge of co-operative and agricultural organizations, in addition to his Policy Governance® skills.



Karen Fryday-Field

Karen is a graduate of the Advanced Policy Governance® AcademySM, personally trained by Dr. John Carver in the theory and implementation of Policy Governance®. She has twelve years experience assisting non-profit, public and for-profit boards in implementing Policy Governance, and over eighteen years of experience in both public and for-profit management and consulting. She is an Ivey Scholar and graduate of the Executive MBA at the Ivey School of Business at the University of Western Ontario. Karen has completed an international benchmarking study on corporate governance best practices which included an evaluation of the unique work of the Board, communication systems within corporate governance, and the roles of the Board and Chief Executive Officer. She holds a Bachelor of Science in Physical Therapy and has completed the course work for the Masters program in Epidemiology at The University of Western Ontario. Karen is the author of several articles, and is dedicated to enabling organizations to lead and embrace change in order to accomplish their goals. She is Board Chair and Past Chair of the United Way of London and Middlesex, and has served on various Boards and committees.



We welcome Karen as the newest Associate with The Governance Coach™.

Our Services

Introductory Workshop

Includes:

- ✓ One-day introduction to the principles of Policy Governance
- ✓ Sufficient detail and opportunity for questions, to enable a board to make an informed decision as to whether it wishes to proceed with Policy Governance

Appropriate for:

- ▶ Individual boards and CEOs in the exploratory stage, wishing to learn more about Policy Governance
- ▶ Groups of boards and management in any community, all interested in exploring the possibilities of Policy Governance
- ▶ Orientation for new members of boards already using Policy Governance
- ▶ Boards who have implemented Policy Governance on their own or with an outside helper, as a "refresher", given by a qualified coach who is fully conversant with the details of the model

Full Implementation

Includes:

- ✓ Two-day initial workshop, including review of principles of Policy Governance, and development of a majority of policies other than Ends.
- ✓ Two-day follow-up workshop to complete policy development and begin work on Ends
Note: Some boards may require additional time for policy development, depending on board size, type of organization, and other factors
- ✓ Coaching during first year of implementation (See below)

Appropriate for:

- ▶ Boards who have made a commitment to implement Policy Governance

Coaching

Includes:

- ✓ Regular contact, providing check-points against which to measure your progress in applying Policy Governance
- ✓ Regular reviews of complete board agenda and package, with written suggestions for improvements in the application of Policy Governance
- ✓ Assistance to the CEO in developing monitoring reports
- ✓ E-mail, phone and/or fax answers to questions as they occur
- ✓ Regular updates and implementation tools when you need them
- ✓ Customized services added as indicated

Appropriate for:

- ▶ Boards that have implemented Policy Governance
- ▶ Coaching is recommended for at least one year after implementation. It is based on an annual retainer agreement. Preferred client rates are offered for coaching clients for any on-site follow-up desired

Policy Governance® “Users Conference”

Includes:

- ✓ Elements from any of our programs—a customized design
- ✓ Network facilitation and idea sharing

Appropriate for:

- ▶ A group of boards in any geographic area who are all using Policy Governance

Conference Presentations

Invite The Governance Coach to stimulate dialogue at your next conference or convention, with one or more of the following presentations. Custom presentations will be prepared on request.

- ▶ Using Policy Governance® to Shape Corporate Risk Culture
- ▶ Developing a Culture of Governance Accountability
- ▶ Structuring Boards to Make a Difference
- ▶ The Board-CEO Team
- ▶ Does Your Board Measure Up?

Workshops For Management

Includes:

- ✓ Introduction to Policy Governance, to understand implications for management
- ✓ Facilitation of strategic planning sessions following board development of Ends
- ✓ Development of monitoring reports that meet board needs
- ✓ Application of Policy Governance principles to the managing of staff

Appropriate for:

- ▶ Management and/or all of the organization staff

Designing Future-Focused Board Meetings

If your board has “the basics” of Policy Governance in place and is wondering “what do we do now?” you are ready to move to a whole new level of engagement. Explore practical methods of designing and using “future-focused agendas” through which the board can set the course for an organization that is healthy and viable not just today and tomorrow, but for the long-term future.

Policy Governance® 202 , 303 and...

Customized workshops appropriate to your board's stage of implementation designed to address your board's issues:

Meaningful Monitoring

Learn about monitoring “in the real world” by looking at actual examples of monitoring reports from a variety of organizational types. We will discuss examples to emulate, and traps to avoid. At the end of this session participants will know:

- ✓ How to properly assess a monitoring report (if they are board members)
- ✓ How to prepare a good monitoring report, including interpretation and evidence (if they are staff)
- ✓ How to identify common traps in monitoring and avoid them

How to Eat an Elephant – Ownership Linkage

Ownership Linkage is a key element of the board’s job, and an essential part of creating Ends. To many boards it seems such an overwhelming job that it feels like trying to eat an elephant. This session will break that elephant into some “bite-size” pieces. We will examine the key elements of creating a “perpetual” comprehensive ownership linkage plan. Who are your owners? How do you “get to” them? What about “representative” input? What kind of questions do you ask? What do you do with the information when you get it? This session can be expanded to actually develop your customized ownership linkage plan.

Servant Leadership in Policy Governance

Examine how the concepts of Servant-Leadership enunciated by Robert Greenleaf, and the Policy Governance model can be integrated. We will look at how a board can apply the concepts of Servant-Leadership within the principles of the Policy Governance model, using specific examples of how policies can be developed to make this possible. At the end of this session, participants will understand:

- ✓ The major concepts involved in Robert Greenleaf’s writings about Servant-Leadership
- ✓ How an organization can integrate the concepts of Servant-Leadership into its policies
- ✓ The synergies between Servant-Leadership and Policy Governance

Board Self-Evaluation

As a board, you are entrusted with the stewardship of resources on behalf of someone else. That places a moral obligation on you to use those resources most effectively. This means that the board must be able to show accountability for the organization as a whole. Is it achieving what it ought to achieve? The board sets the direction for the organization. If the board is not doing its job effectively, the whole organization suffers. The board is responsible for its own development, job design, self-discipline and performance. These are not areas that can be delegated to the CEO. Self-evaluation is a way to assure yourselves and your ownership that you take accountability seriously. Learn the details of how to do a good self-evaluation. This session may be expanded into a guided self-evaluation.

IPGA News

“Responsible Governance: The Power of Accountable Boards” is the theme of the IPGA Annual Conference June 1-3, 2006 in San Antonio, Texas.

Last year’s conference saw nearly 200 people gathered from around the world to share ideas about using Policy Governance®. This is an excellent educational and networking opportunity.

Register before April 15, 2006 and save!

To find out about the IPGA, to become a member, or to register for “Creating the Future: Good Governance in Action” please see the official website

www.policygovernanceassociation.org

Or email Susan Mogensen at membership@policygovernanceassociation.org

IPGA Board News

Jannice Moore was recently re-elected Chair of the International Policy Governance® Association (IPGA).

Upcoming Policy Governance® Seminars

Download the brochure at www.governancecoach.com, email marlodevouge@cs.com or call 780-465-4581 for further information.

Policy Governance® Board Chair Forum

April 24 & 25, 2006
Calgary, Alberta

With Jannice Moore and guest
presenter Pat Knoll, Q.C.

Seminar for Board Chairs, Board
Vice-Chairs and Board
Chairs-Elect

Practical Tips and Tools for the
“Chief Governance Officer”

Attendance is limited at this
session. **Reserve your place now.**

Policy Governance® Adding Value as a Governing Board

April 26, 2006
Calgary, Alberta

An Introduction to Policy
Governance®.

Appropriate for board members or
executives wanting to learn more
about Policy Governance.

Also valuable as orientation for
new board members and senior
staff of boards using the model, and
for those wanting a refresher.

Policy Governance® Behind the Scenes: Helping Your Board Run Smoothly

April 27, 2006
Calgary, Alberta

Seminar for administrative staff
that support board function.

Boards that have administrative
support staff who themselves have
a solid understanding of Policy
Governance®, and who proactively
handle the logistical details of
policy housekeeping, governance-
friendly board materials, and
agenda detail are much more likely
to succeed in using the model
effectively.

Coming this Spring REALBoard Toolkit™ Volume 2

The Governance Coach is proud to present the second in a series of governance tools, *Board Self-Evaluation*. This Toolkit will assist your board in effective self-evaluation.

Pre-publication special: Order Volume 2 now for a 10% discount effective until March 17, 2006.

Don't forget *Volume 1: Meaningful Monitoring*. The Who, What, Where, When, Why, and How of Monitoring, as well as a variety of samples and tools to move your board from monitoring novice to monitoring expert.

Orders of 8 or more copies of the same volume include a free CD with an electronic copy of the tools that can be used by your board.

\$29.99 CAD (\$25.99 US) each or \$19.99 CAD (\$17.25 US) each for orders of 8 or more of the same volume, plus shipping and handling. Prices effective until June 30, 2006.

Please email your order to marlodevouge@cs.com

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