QUESTIONS THE BOARD SHOULD ASK ABOUT CEO EVALUATION

From the desk of the editor

In response to reader requests, the primary focus of this issue is CEO evaluation. In this, our fifteenth issue of Governance Matters, we explore these main questions:

1. Why are CEO evaluations important?
2. Who does the CEO evaluation?
3. How are CEO evaluations done?
4. What should a CEO evaluation include?
5. When to do a CEO evaluation?

We would like to thank those who took the time to help us with this issue. In particular, many thanks to Denyse Guy, Executive Director of the Ontario Co-operative Association, Camille Bérubé, CEO of Beaumont Credit Union in Alberta, and Ken Elliott, Board President at Co-operative Housing Federation of Canada who shared with us from their experiences.

Also, in this issue, we have reviewed Jim Brown’s book, The Imperfect Board Member.

As always, we hope you find this issue of Governance Matters of value to you and your board, and we welcome your feedback!

Debra L. Brown (dbrown@browngovernance.com)
Editor

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“The only way a board of directors can base its confidence in its executive director upon solid, demonstrated fact is through the mechanism of appropriate supervision. Few things can be worse than a board unsure of its expectations of its chief staff officer, and this same executive not knowing what his or her employer really wants accomplished …performance evaluation is probably the most mutually beneficial of all forms of appropriate board supervision.” — Andrew Swanson, Evaluation: Bane? Or Boon?

Why are CEO evaluations important?

In the co-op sector, only about 64 per cent of co-ops evaluate their CEO, according to the Towards Excellence: National Report on Credit Union and Co-operative Governance Practice national benchmarking report. This is a considerably less than the corporate sector where not doing a CEO evaluation is relatively rare, with more than 90 per cent of corporations doing formal evaluations of the CEO (see Chart 1).

This is not completely unexpected. Because people can be put off by the negative aspects of evaluations (i.e. what went wrong…), co-op boards, at times, consider evaluations risky, something to be feared, and therefore many otherwise worthwhile evaluations are placed on the back burner. This perspective is based on people’s experiences with evaluations that are not conducted effectively and does not account for the
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missed and valuable opportunity for strategic discussions between the board and its CEO — it is like “throwing the baby out with the bathwater.”

All leaders want to perform at a level of excellence and contribute significantly to the success of the enterprise. Steps in assessment and evaluation primarily exist to aid the CEO in knowing about expectations and, only secondarily, to highlight shortfalls in performance. Their purpose is to enable personal responsibility and accomplishment, in other words:

- Individuals want to know what is expected of them and how they are performing.
- Individuals should be held accountable for contributing to the organization’s success, and rewards and corrective action should be tied to expectations and evaluations.

In theory, boards are meant to use CEO evaluation as the main accountability tool for the behaviours and actions of the CEO. In other words, the board was counting on the CEO to accomplish specific goals and objectives. Evaluations ask the questions: “did the CEO do what he or she said they would do” and “how well did they do it — was our trust in them well placed?”

A proper evaluation framework starts with being able to attract and retain a chief executive who is willing and able to do the job. Once you have the right person in place, setting expectations as defined in the employment contract, job description and the annual goals and objectives is the next step in ensuring your co-operative or credit union has the proper CEO evaluation framework in place.

“The CEO evaluation framework provides a clear understanding of what I need to focus on,” says Denyse Guy, Executive Director of the Ontario Co-operative Association. “It also gives us regular opportunities to react to change with periodic board input on progress, and guidance on any necessary adjustments to the plan as the year progresses.”

Evaluations provide an explicit assessment of performance based on available evidence, not merely subjective assessments of performance. The evaluation process identifies areas of strength and suggests opportunities for improvement. CEO performance evaluation requires asking key questions in terms of what the objectives were and whether they were achieved.

In terms of effective governance, it is difficult to think of excellence in governance without some form of formal evaluation of a CEO’s performance. Assessment and evaluation are an important part of corporate governance cycle.

Who does the CEO Evaluation?

There are perhaps as many ways to conduct a CEO evaluation as there are types of boards!

Many organizations conduct the CEO evaluation using the board as a whole, either as part of scheduled in-camera or CEO evaluation sessions, or by using evaluation questionnaires. This process is often supplemented by informal direct and regular contacts between the CEO and the chair where performance issues are discussed.
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Other boards use their Corporate Governance Committee to analyze performance results and earmark actions to be derived from them, and/or use the Human Resources Committee to administer the CEO evaluation process and make recommendations to the board.

Some boards, which use evaluation questionnaires, prefer a high level of confidentiality and, therefore, choose to have an outside consultant receive and compile the results of questionnaires. Yet others have someone internal to the organization gather the evaluation questionnaire results.

Best practice is to have the evaluation results summarized by an individual knowledgeable in the subject that is objective and independent, and able to preserve confidentiality of sources of questionnaire information, so that results are conveyed to the board and CEO in a meaningful way. Each board must carefully decide to whom results of evaluations will be communicated early in the development of any assessment and evaluation process.

The key is to make sure the whole process — from the setting of expectations, to taking measures, through to communicating and acting on results — is aligned and oriented on improving future performance.

How are CEO evaluations done?

“Our goal is not to survive — our goal is to prevail!” — Winston Churchill

An amalgam of best practices can best be reduced to the following five-step cyclical process leading to excellence in assessment and evaluation of the CEO (see Exhibit 1). Each of these steps is undertaken against a backdrop of open, transparent and frequent two-way communication.

Strategic planning (step 1) is all about meeting the challenges faced by your co-operative head-on with a longer term winning strategy in order to satisfy member needs. Co-ops are under unprecedented pressure to perform — from their members/customers/users, competitors, communities and employees. An integrated approach to planning engages each stakeholder group at each step, from vision through action to change.

The main components of modern strategic planning are consistent across all industries and endeavours, and typically comprise the following elements:

- **Mission and vision:** the overarching purpose of the co-op (the “why are we here?”)
- **Goals and objectives:** the components of the mission of the coop, what it strives to achieve (the “where we are going?”)
- **Strategies and actions:** the ways in which the co-op will achieve its objectives (the how we will do it? exactly who will do what? and when?)

Strategic planning is often the best opportunity for the board of directors to exercise leadership and stewardship. “Living the mission” is what the board imparts to the CEO’s performance evaluation process by using the strategic plan, and its goals, objectives and values to set the strategies and actions that will guide the CEO for the foreseeable future.

The strategic plan is initially done by the CEO, usually with the assistance of senior staff, and is typically presented to the board at the annual retreat. As a long term planning document, the strategic plan normally assesses the issues and challenges faced by the co-operative over the foreseeable future (typically three-to-five years), and identifies the goals and objectives to be accomplished in the medium term. It also identifies
the strategies and actions to be undertaken over the period to achieve the goals and objectives. The board discusses the draft strategic plan in the context of environmental and strategic risks and opportunities, and

### Exhibit 1: Steps to Assessing and Evaluating the CEO

<table>
<thead>
<tr>
<th>Step 1: Strategic Planning</th>
<th>Board and CEO set goals and objectives for next three to five years.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Step 2: Business Planning</td>
<td>CEO and executive management team develop one year specific plans — objectives, strategies, marketing plans, departmental plans, HR plans and other resource allocations — aligned to the overall strategic plan</td>
</tr>
<tr>
<td>Step 3: Performance Mandate</td>
<td>Setting of CEO’s targets and expectations directly measurable against the strategic and operational plans.</td>
</tr>
<tr>
<td>Step 4: Informal Performance Evaluation</td>
<td>Comprised of periodic, regular, informal discussions and meetings between the Chair and CEO</td>
</tr>
<tr>
<td>Step 5: Formal Performance Evaluation</td>
<td>Formal evaluation of the facts and results, as measured against plans and agreed upon expectations leading to affirmation, change and process enhancements and improvements</td>
</tr>
</tbody>
</table>

Sets the strategic priorities and expectations for the organization. The CEO then uses the direction received from the board to prepare business plans.

Business planning (step 2) is all about meeting the day-to-day challenges faced by your co-operative in order to satisfy member needs day in and day out. Business plans are the way choices are made by the organization to ensure it is delivering on the strategic plan.

This is usually done by the CEO, working closely with senior staff to identify the short term strategies and actions to be undertaken to achieve each strategic goal and objective. This is usually where measures are created to inform the board on progress throughout the year. A critical step undertaken by the CEO is to ensure the strategic plan permeates throughout the organization. The board may also review the business plans to ensure that are aligned with the strategic plan and incorporate effective measures of performance.
“We start with the strategic plan approved by the board, then work with senior staff on aligning the yearly operational plans to the priorities identified in the strategic plan,” says Camille Bérubé, CEO of Beaumont Credit union in Alberta. “By involving senior staff in the process of marrying individual goals and objectives to the key strategic priority areas, we ensure that staff understand and buy into the key priority areas, and help cascade those priorities down the organization. The team is then in a position to help me deliver on the board’s expectations.”

Within the context of a CEO evaluation, the board needs to ask whether the CEO sought acknowledgment from critical stakeholders (e.g. board, staff, members) that they understand and agree with performance mandates, terms of reference and specific criteria, and have the resources necessary to achieve the plans. The board also reviews changes in compensation, reporting and authority levels to ensure they are correct and are having the expected effect.

What should a CEO evaluation include?

The evaluation process should be both an informal (step 4) and formal (step 5) process, and should, wherever possible, avoid subjective judgments of performance (step 3).

By using a robust evaluation process, performance expectations can be:

- made clear for both the board and CEO,
- made to align with the your co-op’s mandate and strategic plan, and
- focused on the direction the board wants the co-op to take over a given time frame.

Perhaps the most universal truth about any system of assessing and evaluating the CEO, or the board of directors for that matter, is that one size does not fit all. The system is dynamic, made up of separate and distinct aspects of an interdependent process. To be truly effective, it needs to be entirely tailored to the needs and expectations of the CEO as an individual, of the board as the main organ of direction and control, and of the co-operative as a collective of members with needs and expectations.

Questions that will help you customize your CEO evaluation framework include:

- What are CEO strengths and weakness relative to the priority aspects of the strategic and operational plans? For example, the CEO may have a strong financial background but have little experience in human resources, or may have familiarity with facilities and IT, but not so much with marketing.
- How good is the CEO’s relationship with colleagues and subordinates?
- How much experience does the CEO have?

Performance measures (step 3) are how the CEO and his/her staff know “how well” they are doing and the areas of feedback that may lead to improvement. These have to be intimately related to the mission and values, or the raison d’être, of the co-op, espoused by the co-op and its members, and created in the context within which each of the elements of the strategic and operational plans are made.

“We can’t just make motherhood statements about goals and objectives and expect our chief executive to magically know what the board wants them to do with an issue,” says Ken Elliott, Board President at Co-operative Housing Federation of Canada. “We have to tighten the words we use to more effectively describe the measurable aspects of the goals we seek, and help the CEO focus on those aspects that we want delivered on a priority basis.”
At the core of the strategic plan, operational plans and evaluative frameworks are the values of the co-op. Which “what’s,” “where’s,” “when’s” and “how’s” are acceptable to the co-op community and how are they reflected in plans? This can mean that measures can be particularly challenging for co-ops whose objectives are not always readily quantifiable into discrete metrics (such as profits, products sold, employee and member satisfaction).

For this purpose, leading co-operatives make use of some sort of 360 feedback tools for managers and staff, and periodic assessments of community performance using community satisfaction surveys. If 360 degree feedback is used, one must be careful to differentiate between real performance data on situations and “sour grapes” feedback on the part of one or more individuals. Such tools are now much easier and cost effective to use thanks to the availability of web-based surveys.

Ideally, the strategic plan will have already identified the types of actions, behaviours and results that the co-op is looking for. The challenge is then to characterize the range of desirable outcomes that the co-op seeks to achieve over the given time period and turn them into (see Exhibit 2) into Specific, Measurable, Achievable, Realistic and Time based goals — “SMART” goals.1 Often, this is where creativity and significant work is required to turn the somewhat “softer” co-operative community goals into measurable goals that can be used to evaluate results, impacts and outcomes.

One way to identify an effective range of goals and measures for the chief executive is to go back to the very characteristics that progressive organizations want to see in their CEO, including:

- leadership and stewardship
- strategic planning and vision
- achievement of organizational objectives
- human resource management and succession planning
- relationships: shareholder, stakeholder, board
- integrity and ethical leadership
- financial performance

The CEO evaluation process should also assess how the CEO is managing the human resources of the credit union or co-operative, including how well the performance management system of senior staff is aligned with, and ensuring delivery of, strategic and operational plans.

A successful performance management framework will:

Exhibit 2: SMART Goals

<table>
<thead>
<tr>
<th>Specific</th>
<th>Measurable</th>
</tr>
</thead>
<tbody>
<tr>
<td>Well defined</td>
<td>Know if the goal is obtainable and how far away completion is</td>
</tr>
<tr>
<td>Clear to anyone that has a basic knowledge of the co-op</td>
<td>Know when it has been achieved</td>
</tr>
</tbody>
</table>

Exhibit 3: Examples of Measures in a CEO Evaluation

<table>
<thead>
<tr>
<th>Result Measures</th>
<th>Competency Measures (from Competency Dictionary © Hay Management Consultants 1999)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Profitability</td>
<td>Developing Others</td>
</tr>
<tr>
<td>Membership</td>
<td>Impact and Influence</td>
</tr>
<tr>
<td>Service Quality</td>
<td>Initiative</td>
</tr>
<tr>
<td>Employee Satisfaction</td>
<td>Self-Confidence</td>
</tr>
<tr>
<td></td>
<td>Service Orientation</td>
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<tr>
<td></td>
<td>Team Leadership</td>
</tr>
<tr>
<td></td>
<td>Teamwork and Co-operation</td>
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</tbody>
</table>
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• Combine strategic and business plans targets with generally desirable characteristics of managers to come up with measures, as well as acceptable ranges of performance relative to each measure.

• Include result measures (results measures are the ones developed as part of the strategic plan, and associated with SMART goals) and

• Include behavioural measures (drawn from skills and competencies required or needing to be developed) for the CEO, as shown in Exhibit 3.²

When to do CEO evaluations?

This is not as straightforward as the typical “once a year” answer that many expect at this point.

Effective communication between the board and its CEO, as well as the transparency of the evaluation system within the governance infrastructure, underlies successful assessment, evaluation and accountability. Effective communication between the board, the CEO, and senior staff is not something that happens once a year — instead it means embracing an environment of constant two-way communication between the members of the board, its chair and perhaps even committees, and the CEO and his/her senior staff.

The best processes have built-in flexibility and a component that is informal (step 4). However, this is meant to augment, not replace, the formal practices (step 5). A formal written process that is conducted quarterly, or at least twice each year, combined with informal discussions, as required, is at the core of best practices.

Performance discussions can take the form of brief conversations between the chair of the board and the CEO on emerging performance issues. The chair can then draft communications to the board or its committees describing the challenges and the actions taken.

Many co-operatives are moving to more regular and informal discussions of performance, including the use of performance dashboards. A performance dashboard is a one- or two-page, high level scorecard of performance measures — like the dashboard of a car — that is provided to the board and others indicating how the organization is doing vis-a-vis targets. Informal discussions can then be used to effectively set up more formal reviews of performance that happen quarterly or every six months. The goal should be “no surprises” for both the board and the CEO.

“The process of quarterly reviews serves many purposes at Beaumont”, says Camille Bérubé. “First, it is a regular opportunity to update senior staff and the board on our ability to deliver on the plan, and contributes to a no-surprise policy. Second, it provides scheduled opportunities to identify and discuss challenges as situations arise. Finally, we use quarterly reviews to change priorities and adjust targets and measures as required, making the plans continuously relevant.”

There should be a close parallel between the overall objectives, strategies and performance measures set for the organization and for its leaders, the CEO, chair and board.

The best practice is to have all the forms designed and criteria agreed upon by all parties, then to sit down and go through the entire process at the very beginning of the year or evaluation period. Any questions or misunderstandings can then be dealt with to everyone’s satisfaction before the performance

² According to Competence At Work, by Spencer and Spencer, “A competency is an underlying characteristic of an individual that is causally related to criterion-referenced effective and/or superior performance in a job or situation.” Please see Hay Management Consultants at www.hayresourcesdirect.baygroup.com/Competency/Default.asp
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measurement begins. Clear communications in assessing the position helps the CEO to maintain a focus and sense of direction. It also avoids finger pointing and hurt feelings later because of misunderstandings.

A final step is using the CEO’s performance evaluation results as the primary input into CEO compensation decisions for the coming year. While executive compensation is such a large and complex area to require its own newsletter article, one summary model is illustrated in the graphic above — each CEO evaluation should contain three distinct components and levels, and each of these informs different elements of the CEO’s compensation package.

![Aligning CEO Evaluation and Compensation](image)

Personal accountability has tremendous value and effect. Individuals both want and need to know what is expected of them as well as how they are doing. It is the assessment and evaluation process that is the mechanism for communicating expectations, accomplishments and accountabilities, leading ultimately to individual and organizational success.

Book Review

The Imperfect Board Member: Discovering the Seven Disciplines of Governance Excellence
Author: Jim Brown ([team@strive.com](mailto:team@strive.com))
Published by: Jossey-Bass, 2006
ISBN 0-7879-8610-0

Brown has articulated a conceptual model of governance based on what he calls the “seven disciplines of governance excellence.” It is a business book written as a novel — or as some have labelled it, a
leadership fable — which has broad governance application to any sector be it private, public, not-for-profit, co-operative, church, or otherwise. It is a quick and simple read.

The book claims to be one that is “written for the millions” of directors. It explores “how boards can truly add value and … why they are so important.” The book includes an afterword that recaps the “seven disciplines” model and provides additional tools and resource suggestions.

I must admit, when I first picked up the book, I thought “not another governance model — just what we need — not!” But the book grew on me. Brown has found a fresh way to communicate the governance disciplines that every director needs to understand and live out as they serve their organizations. Simply put, what he calls the seven disciplines are:

1. Direct: the board must direct the organization
2. Protect: the board must protect the interests of the owners
3. Respect: the board must respect the expectations of the owners
4. Reflect: the board must reflect on the results of the organization
5. Select: there must be a disciplined approach to the selection of leaders
6. Expect: the board must expect the best of the CEO and of itself
7. Connect: the board must connect deeply as a team, capitalizing on one another’s strengths

The story takes its main character, David, from being a stressed-out and ineffective board member who does not understand his role, (let alone the “seven-disciplines,”) to a value-adding director on a journey toward governance excellence. My suspicion is that many readers will see themselves in David. I also suspect that this light read will help you move along in your own journey toward governance excellence.

If you are looking for an academic governance text book, this is not the book for you. If you are looking to understand the behaviours and disciplines that truly make boards work, then you will want to give this book a read.

Additional Resources

*Questions the Board Should Ask about CEO Evaluation*, [www.browngovernance.com](http://www.browngovernance.com).

*Annual Evaluation of the Executive Director*, Board Cafe, September 1999.

*Hiring and Performance Appraisal of the Executive Director*, Muttart Foundation and Board Development Program (Alberta Community Development, Government of Alberta).

Contact Us

We encourage you to submit articles, case studies, links or other resources for future newsletters. Please contact Quintin Fox ([Quintin.Fox@CoopsCanada.coop](mailto:Quintin.Fox@CoopsCanada.coop)), CCA’s Manager of Member Services, (613) 238-6711 ext 234.

First published in 2004, in partnership with Brown Governance, CCA’s comprehensive report on co-operative and credit union governance practices in Canada includes data from over 400 Canadian co-ops and credit unions and provides the first and only national picture of Canadian co-operative board practices.

CCA is pleased to announce that it is partnering with Brown Governance to conduct the second national governance survey. **Towards Excellence: National Report on Credit Union & Co-operative Governance Practices 2007**, will examine such areas as:

- board selection practices
- board and committee composition
- director terms and tenure
- board and committee compensation
- board responsibilities
- board and director evaluations
- director education
- board reporting and measurement practices
- member and stakeholder relation practices

Data on corporate sector practices will also be included, allowing co-operatives to see how their governance practices either lead or lag the corporate sector.


CCA Launches Governance Award

CCA will be launching the first national governance award for the co-operative and credit union system at its Annual General Meeting and Congress in Newfoundland in June 2007. The award will acknowledge examples of best practice and innovation amongst boards and directors within the co-operative system. CCA has brought together leading corporate governance experts, academics, directors and staff responsible for the board together to identify the unique elements of corporate governance within co-operatives and credit unions. The first awards will take place at the 2008 AGM and Congress with details, including criteria and categories, of the award being announced in St John’s.