Executive Sessions of Your Board

WHAT COUNTS

Strategies for your financial success

Federal Home Loan Bank Seattle

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Conducting "Regular Executive Sessions" is prominently displayed on every list of board "Best Practices." However, practical guidance is seldom provided to board members about when and what they should do in such sessions—and who should be involved. Because every board is comprised of individuals with different personalities, experience levels, and professional backgrounds, there is no "right answer" for every board. This brief article, based on our experience, provides a few thoughts and suggestions to help your board conduct effective executive sessions.

We recognize that many CEOs and board members really don't think a "regular" executive session is necessary. After all, "we can always call a meeting if we need to." In fact, this may not be the case, and without an established process, the board may not be able to take action when and if action is required. We believe a regular executive session at the end of every board meeting is in everyone's best interest.

CEOs must recognize that, if the board doesn't provide a regular time and location for such private discussion, directors will discuss bank business with one another informally (at social or business events, at their clubs, etc.) Regular executive sessions help both the CEO and board members avoid "cliques" and "private lobbying" by individual directors. If a topic is important enough to discuss individually, then it should be brought up in your executive session, not outside the board room.

Board members must also recognize that because they are not part of day-to-day management, they may be the "last to know" about sensitive issues. Your executive session provides every director with an opportunity to learn about and discuss any sensitive issue in the privacy of your board room.

Regular reports regarding finance, credit, etc. by senior management to your board are an excellent method for directors to assess the depth of management without interfering in the CEO's day-to-day management responsibility. We think it's a good idea to have your senior managers attend and report at every board meeting. However, when all the reports are completed, all non-board members should be excused as a group, so the board and CEO can discuss bank business in private.

At the conclusion of your board's regular business meeting, the CEO, any other non-independent board members, and board secretary should leave the room and provide the outside board members with the opportunity to discuss bank business privately in "executive session." Your CEO may also be Chairman of the Board; however, every executive session should have a "chair" whose role is to go around the table and ask each director if they have anything they wish to discuss. This is the proper time and location to discuss any issue.

As an example, let's assume your bank's CEO has an incentive compensation plan that requires non-performing assets to remain below a certain level if s/he is to receive the annual bonus, and your CPA firm has told your bank's audit committee they are concerned about a certain credit. The loan is very likely to go on non-accrual, but you don't expect to have a loss after the collateral is liquidated. It's a judgment call. If the credit is considered non-performing, the CEO's bonus will be reduced, but on the other hand, the bank may not suffer a loss. Such an issue that concerns the CEO, the compensation committee, and the audit committee is an obvious topic for your executive session.

It is important for the outside directors to limit discussion to important policy topics. The executive session is not a forum for petty issues and personal grievances (e.g., "the CEO would not approve a loan to my best friend"). The executive session is not an excuse for the board to become involved in day-to-day management issues. It is essential that all parties avoid unintended conflict and clearly define the respective roles of the CEO and the board.

It's also important for board members to remember that the board room is a "fish bowl"—everyone knows your board is in executive session. For this reason, a regular executive session at the end of every board meeting should be "routine," not "special." Board members have a responsibility to allow adequate time for board business and not "rush out" at the end of your board meetings to attend to other matters. You need to take the time to go around the table and conduct a "real" meeting every time. However, board members also need to be sensitive to timing and avoid potential "unintended consequences" of a long executive session—this is not the time or place to have a prolonged private discussion about last night's game.

One board member should always be designated to brief the CEO immediately after the executive session on the topics discussed during your meeting. This might be the "chair," but it doesn't have to be the same person every time. For example, if the topic concerns staffing or succession, it might be the chair of the compensation committee. This follow-up is essential to your CEO-board relations and needs to occur even if no topic of substance was discussed.

On occasion, the board may need to ask for outside independent advice about a sensitive matter, and it's important that the board know in advance who to contact. This may be the senior partner of the bank's regular outside law firm or some other independent advisor the board has identified. Experience has taught many of us that the first actions taken are frequently the most important, and many subsequent problems can be avoided if professional advice is obtained before the board acts. Your designated advisor doesn't need to attend your regular meetings, but you need to know who to call if such a problem develops.

The objective of this brief article is to share a few thoughts concerning your board's executive sessions. The concept of "best practice" is built on the collective knowledge of experienced board members, and we welcome your feedback about what has worked "best" for your board.

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